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Special Issue S1: Is there a need for ‘Reforms’ in IMF?

Guest Editor: Prof. Dr. Badar Alam Iqbal

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Editorial Note

The Second World War was responsible for the creation of two multilateral financial institutions because of the abolition of the gold standard. The war had created two sets of global problems: first, problems of world trade and currency issues; second, how to reconstruct the world economy ravaged by the Second World War. Accordingly, multilateral institutions, namely, the International Monetary Fund (IMF) and International Bank for Reconstruction and Development (the World Bank), were established on July 24, 1944. They started functioning in 1945.

For creating multilateral institutions for solving trade and currency issues, 44 nations had gathered at Bretton Woods in New Hampshire, United States. The primary objective of establishing the IMF was to foster global monetary cooperation among the member countries on the one hand and on the other hand to create a conducive environment to facilitate trade and currency issues.

Since its inception, the IMF has been playing a positive and constructive role in the promotion of world trade and solving balance-of-payments crises, particularly in developing economies.

More than 73 years have elapsed, and the world economy has been witnessing radical changes in terms of contents and role. However, the IMF has not caused any change in its structure, management, and functioning. Therefore, the countries across the world have started raising their voice to bring the considerably required reforms in the 73-year-old Fund.

REQUIRED AREAS OF REFORMS:

Although the IMF has been playing a significant role and contributing considerably in solving trade and currency issues, there has been a persisting opinion that the IMF is constantly dominated by the developed countries. Hence, reforms are the need of the hour. The developing and emerging economies have been demanding reforms in the IMF in the following segments:

1. Reduce domination of developed economies;
2. Modify IMF's existing activities;
3. Expand lending facilities to the least developed economies;
4. Governance.

The emerging and developing countries have identified areas for reforms that are as follows:

(a) Reinforcing the growth momentum among developing and the least developed nations;
(b) Sharing gains more equitably;
(c) Strengthening long-term growth;
(d) Creation of strong and rules-oriented trade and currency framework.

CONTRIBUTION OF MERJ:

Considering the problems and issues of emerging and developing countries, it was thought by the Management and Economics Research Journal (MERJ) to invite academic and policy makers to undertake a soul searching in terms of required reforms in the management and functioning of the IMF. The soul searching has been transformed into reality, and you have a special issue in hand. The academicians and policy makers across the world have penned down their opinions and explored new ways and methods to bring the required reforms in the IMF, which is overdue.

The MERJ Special Issue contains nine papers that have covered different aspects of management, governance, and functioning of the IMF. I am sure the readers would find it an interesting and thought-provoking read in respect of the management and functions of the fund.

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I am of the view that MERJ is the first journal worldwide that has provided a special issue on the IMF. I have not come across any such publication as yet that has covered the topic of reforms in respect of managing and running the IMF. Hence, this issue would be an asset for academicians, policy makers, and researchers.

Prof. Dr. Badar Alam Iqbal
Adjunct Professor, School of Economics and Finance, Monarch University, Zug, Switzerland.
Visiting Emeritus Professor, CBA, International University of Business Agriculture and Technology (IUBAT), Dhaka, Bangladesh.
Former Fulbright Visiting Professor, USA.
Former Ford Foundation Grantee, USA.
Former Dean and Chairman, Department of Commerce, AMU, Aligarh (UP), India.
DAAD Visiting Fellow, SAI, Heidelberg, Germany.
Visiting Professor, IIU, Malaysia.
Visiting Professor, American Central University, USA.
Visiting Professor, IGR, University of Rennes, France.

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Populism versus IMF Conditionalities: Demand Management Policies in Present Regime of Globalization

Ayub Mehar*
Iqra University, Karachi, Pakistan.

***Correspondence:** ayubmehar@yahoo.com

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Abstract

The end of a bipolar regime after the collapse of the Soviet Union diverted the world economies to globalization regime, where economic freedom and liberalization were adopted as most powerful and popular philosophies of the economic welfare and development. The origination of a free trade regime, decentralization in public finance, and revival of the classical school of thought in economic policies are the natural outcomes of the global failure of centrally controlled economic planning experiences. Autonomy of the central banks, market-oriented exchange rates, convertibility of the currencies, privatization, deregulation, and free trade are the banners of classical economic thoughts in the present regime. Meanwhile, the International Monetary Fund (IMF) came into force when the world was divided into left and right arms. The IMF conditionality and recommended measures are still based on demand management mechanism where most of the advices belong to exchange rate mechanism (devaluation), increase in interest rate, increase in tax revenue, reduction in subsidies, transfer payments, so on. The core objective of this study is to review the IMF policies and practices in the contemporary world where supply-side policies and classical theories are regaining their importance in post-Soviet regime. Before any recommendation and contemplating the role of the IMF in the contemporary world, it will be appropriate to review and analyze the current practices of the IMF by three dimensions: History and cause of the creation of the IMF, its governance and financial structure, and its role in global economy and lending activities. The study suggests the change in the IMF governance structure and the coordination between World Trade Organization (WTO), World Economic Forum (WEF), and IMF policies.

Keywords: Supply-side policies; Liberalism; Demand management policies; Small government.

1. INTRODUCTION

The role of the International Monetary Fund (IMF) has been controversial since last 30 years, and its opponents argue against the IMF policies that are typically based on the following common intuitive:

- Some IMF policies may be antidevelopmental. In some countries, the deflationary effects of the IMF programs quickly led to losses of output and employment in economies where incomes were low and unemployment was high. Moreover, the burden of the deflation is disproportionately borne by the poor.
- In some countries, the IMF conditionality forced the curtailment in public health expenditures. Consequently, the underfunded public health systems demoralized the working conditions and fuelled a "brain drain" of medical personnel. The common people in those countries have to experience the severe problems as they have to force the sale of family assets and businesses and spend their life time savings to save the lives of family members or experience the dire consequences.
- It is generally apathetic or hostile to human and labor rights.
- It is a general opinion among the common people and political circles (particularly in opposition parties) that the IMF lending facilities have been used for politically motivated objectives. The IMF policy makers have been supporting military dictatorships friendly to American and European corporations. For instance, the Pakistan political parties and religious circles use the anti-IMF slogan in their election campaigns and claim that they will obtain freedom from the IMF.
- Argentina has always been considered a model country by the IMF in its compliance to IMF recommendations. This country has experienced a tragic economic crisis in 2001. According to the public

opinion in Argentina, it was a consequence of privatization of strategically vital national resources and "IMF-induced budget restrictions," which undercut the government's ability to provide basic facilities including health, education, and security.

- In African countries, the IMF policies and imposed restrictions have prevented spending on education and health. Consequently, they have undermined possibility of meeting the Millennium Development Goals (MDGs).
- Calin Popescu-Tariceanu, former Romanian Prime Minister, claimed that "Since 2005, IMF is constantly making mistakes when it appreciates the country's economic performances."
- Julius Nyerere, former Tanzanian President, claimed that "Debt-ridden African states were ceding sovereignty to the IMF and the World Bank." He asked, "Who elected the IMF to be the ministry of finance for every country in the world?" (Mwakikagile, 2006).
- A number of civil society organizations have criticized the IMF's policies for their impact on access to food, particularly in developing countries. Bill Clinton, former president of the United States, delivered a speech to the United Nations in October 2008. He criticized the World Bank and IMF for their policies on food and agriculture by stating "We need the World Bank, the IMF, all the big foundations, and all the governments to admit that, for 30 years, we all blew it, including me when I was president. We were wrong to believe that food was like some other product in international trade, and we all have to go back to a more responsible and sustainable form of agriculture."
- Raghuram Rajan, former chief economist of IMF and former governor Reserve Bank of India (RBI), criticized the IMF for praising the monetary policies of the United States, which he believed were wreaking havoc in emerging markets. He had predicted financial crisis of 2007-2008 and criticized the IMF for remaining a sideline player to the developed world.

However, popular public views or political statements may not be necessarily trustworthy for sustainable economic policies for the nations. To explain popular public demands, a term of "populism" is widely used in the contemporary literature of economics and political science. It explains the phenomenon when political parties support those public demands that may be harmful in the long term. In recent years, academic scholars have produced definitions that facilitate populist identification and comparison. Populism is most common in democratic nations.

Political parties and politicians frequently use the terms "populist" and "populism" as pejoratives against their opponents. The provision of subsidies, support pricing, nationalization, and over employment in public sector are examples of populism. If the IMF provides loan to a country, then the country has to follow the terms and conditions imposed by the IMF. Moreover, in the presence of those terms and conditions, the popular public demands cannot be provided.

The core objective of this study is to review the IMF policies and practices in the contemporary world where supply-side policies and classical theories are regaining their importance in post-Soviet regime. Before any recommendation and contemplating the role of the IMF in contemporary world, it will be appropriate to review and analyze the current practices of the IMF by three dimensions: History and cause of the creation of the IMF, its governance and financial structure, and its role in global economy and lending activities. The study accomplishes this task.

2. HISTORY AND CAUSE OF THE CREATION OF IMF

During the great depression, countries sharply increased the tariff and non-tariff barriers to trade in order to enhance their domestic economies. The Second World War has further aggravated the economic miseries of European countries. At the end of the Second World War, every affected country has started the job of rebuilding its national economy. Moreover, avoiding from imports and enhancing exports were the focus of economic policies. This led to the devaluation of national currencies and a decline in world trade. This situation led to a collapse of monetary systems in international markets, which created a need of cooperation and a harmonized mechanism. The global economy had experienced two serious issues after the Second World War: (1) How to reconstruct the economy and (2) how to use and determine the value of currencies

for exchange of goods and services. The creations of the International Bank for Reconstruction and Development (IBRD) and the IMF are the results of that post war crisis. However, one cannot isolate the expanding role of leftists in those days, fall of colonialism, remapping of South Asia and Middles East, and inclination of capitalism toward the Keynesian-type fiscal policies that allow the public interventions in commodity pricing through taxation and subsidies.

The idea for the formation of the IMF was floated by Harry White and John Keynes in the Bretton Woods Conference in 1944, where 44 nations came together in New Hampshire. It came into formal existence in 1945 with 29 member countries (currently 189). There were two views on the role the IMF should assume as a global economic institution. American delegate led by Harry White foresaw an IMF like a bank that ensures the timely repayment of debts. Most of White's plan was incorporated into the IMF mechanism. British economist John Keynes suggested that the IMF should be a cooperative fund to help the member countries in periodic crisis, and its major goal should be reconstructing the international payment system and to create conducive environment to facilitate trade and currency issues. This view was incorporated in the IMF's mission that describes the objective of the IMF is to ensure the stability of the international monetary system. In this manner, the IMF is charged with overseeing the international monetary system to ensure exchange rate stability and encouraging members to eliminate exchange restrictions that hinder trade.

Upon the founding of the IMF, its three primary functions were as follows: to oversee the fixed exchange rate arrangements between countries, thus helping national governments manage their exchange rates and allowing these governments to prioritize economic growth, and to provide short-term capital to aid the balance of payments. This assistance was meant to prevent the spread of international economic crises. The IMF's role was fundamentally altered by the floating exchange rates post-1971. It shifted to examining the economic policies of countries with IMF loan agreements in order to determine if a shortage of capital was due to economic fluctuations or economic policy.

The organization's objectives stated in the Articles of Agreement are as follows: to promote international monetary co-operation, facilitate the expansion and balanced growth of international trade; promote exchange stability; make resources available (with adequate safeguards) to members experiencing balance-of-payment difficulties, assist in the establishment of a multilateral system of payments, and ensure sustainable economic growth and high employment.

According to the IMF itself, it works to foster global growth and economic stability by providing policy advice and financing the members, by working with developing nations to help them achieve macroeconomic stability and reduce poverty. The imperfection of private international capital markets provides the justification for official financing, without which many countries could only correct large external payment imbalances through measures with adverse economic consequences. The IMF provides alternate sources of financing.

From the academic point of view, the history of the IMF can be divided into five stages:

2.1. Stage I: Reconstruction of Global Economic Architect

After its inception in 1945, the IMF has become the key organization to rebuild international capitalism with the maximization of national economic sovereignty, which is defined as embedded liberalism. The end of colonialism in Africa and Asia in the 1940s has caused the increase in the IMF membership. Moreover, the IMF's influence in the global economy steadily increased as it accumulated more members.

2.2. Stage II: Nixon Shock and End of Fixed Exchange Rate

The Bretton Woods system prevailed until 1971, when the United States government suspended the convertibility of the US dollar (and dollar reserves held by other governments) into gold. It led to the collapse of fixed exchange rates, and countries independently decided to choose their exchange arrangement. After that the IMF helped the countries in oil shock periods of 1973 and 1979.

2.3. Stage III: Global Reforms and Growing Debt

This regime started since the second oil shock in 1979 and ended with the fall of bipolar regime after the collapse of the Soviet Union in 1989. Currently, it has become a practice that when oil shocks lead to an international debt crisis, the IMF assists in coordinating the global response.

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2.4. Stage IV: Unification and Transition in Europe

The dissolution of the Soviet Union has pushed the transitional economies to join the IMF in the 1990s, and the IMF membership reached at 189 that make up its near-global membership. The IMF plays a central role in helping the countries of the former Soviet bloc transition from central planning to market-driven economies.

2.5. Stage V: Economic Liberalism and Globalization

Currently, the collapse of bipolar regime and technological advancement has led to the rapid growth in the cross-border movements of the people, ideas, and capital goods. World Trade Organization (WTO) and World Economic Forum (WEF) along with leading universities and multilateral institutions played a central role in the connectivity of people from different countries. This movement created fast growing liberalization, cultural transformation, and globalization. The cross-border flow of capital is one of the consequences of globalization. The credit crisis and the food and oil price shock in recent past indicate new challenges for the IMF, while implications of the continued increase of capital flows and its impact of the stability of the international financial system are still unknown. It implies the further prudence and change in the scope and policies of the IMF.

3. GOVERNANCE AND FINANCIAL STRUCTURE

Tables from 1 to 7 summarize the structures of the IMF board and its financial controls. IMF lending and support to countries under monetary crisis, attached conditionalities, and policy recommendations are largely determined by the Executive Board; whereas, the structure of the board is derived from the structure of financial contribution by its members. It is quite obvious that a significantly large part of financial resources are contributed from the rich industrialized countries, while this fund is used primarily for the developing countries that are experiencing liquidity crisis. The selection of the members of executive board and voting patterns are associated with the size of contribution. The decisions are not made on one country one vote basis.

Any country can apply for the IMF membership. However, the members have to pay their share according to their assigned quota. The IMF's quota system was created to increase funds for loans. The assigned quota reflects the country's relative size in the global economy. Each member's quota also determines its relative voting power. Thus, financial contributions from member governments are linked to voting power in the organization. This system follows the logic of a shareholder-controlled organization: wealthier countries that provide more money to the IMF have more influence than poorer members that contribute less. It implies that decision making at the IMF was designed to reflect the relative positions of its member countries in the global economy.

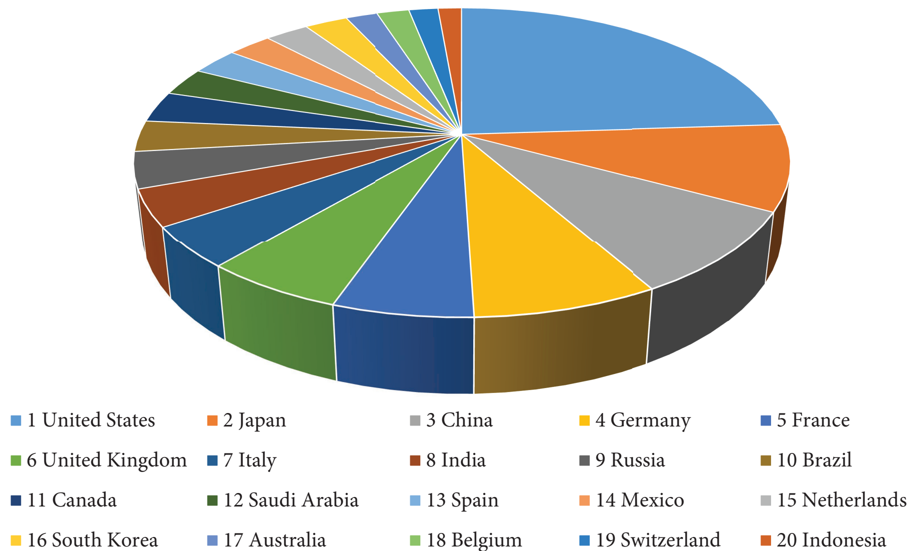
IMF Board of Governors is the highest authority in its hierarchy, which is officially responsible for approving quota increases, Special Drawing Right allocations, the admittance of new members, compulsory withdrawal of members, and amendments to the Articles of Agreement and By-Laws. The board comprises one governor and one alternate governor for each member country. However, in practice, the board of governors has delegated most of its powers to the IMF's Executive Board. Twenty-four executive directors represent all 189 member countries in a geographically based roster. Following the 2008 Amendment on Voice and Participation, eight countries each appoint an executive director: the United States, Japan, China, Germany, France, the United Kingdom, Russia, and Saudi Arabia. The remaining 16 directors represent the constituencies comprising 4-22 countries. The executive board is chaired by the managing director who heads the IMF staff as well. Historically, the IMF's managing director has been European, and the president of the World Bank has been from the United States. However, in 2011, the world's largest developing countries, the BRIC nations, issued a statement declaring that the tradition of appointing a European as managing director undermined the legitimacy of the IMF and called for the appointment to be based on merit.

The Special Drawing Rights (SDRs) are based on a basket of key international currencies. Each member has a number of basic votes that equal 5.502% of the total votes plus one additional vote for each SDR of 100,000 of a member country's quota. The basic votes generate a slight bias in favor of small countries. However, the additional votes determined by SDR outweigh this bias. The changes in the voting shares require approval by a supermajority of 85% of voting power.

The IMF continues to undertake reforms to ensure that its governance structure adequately reflects the fundamental changes occurring in the world economy. It was argued many times that to provide more effective

Table 1. Quota and Voting Shares for IMF Members.

Rank	IMF member country	Quota: millions of SDRs	Quota: percentage of the total	Number of votes	Percentage out of total votes
1	United States	82,994.2	17.68	831,396	16.73
2	Japan	30,820.5	6.56	309,659	6.23
3	China	30,482.9	6.49	306,283	6.16
4	Germany	26,634.4	5.67	267,798	5.39
5	France	20,155.1	4.29	203,005	4.09
6	United Kingdom	20,155.1	4.29	203,005	4.09
7	Italy	15,070.0	3.21	152,154	3.06
8	India	13,114.4	2.79	132,598	2.67
9	Russia	12,903.7	2.75	130,491	2.63
10	Brazil	11,042.0	2.35	111,874	2.25
11	Canada	11,023.9	2.35	111,693	2.25
12	Saudi Arabia	9,992.6	2.13	101,380	2.04
13	Spain	9,535.5	2.03	96,809	1.95
14	Mexico	8,912.7	1.90	90,581	1.82
15	Netherlands	8,736.5	1.86	88,819	1.79
16	South Korea	8,582.7	1.83	87,281	1.76
17	Australia	6,572.4	1.40	67,178	1.35
18	Belgium	6,410.7	1.37	65,561	1.32
19	Switzerland	5,771.1	1.23	59,165	1.19
20	Indonesia	4,648.4	0.99	47,938	0.96



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voice and representation for developing countries their share in voting power should be enhanced as in the present context the developing countries represent a considerably larger portion of world economic activity since 1944, when the IMF was created. Consequently, the following reforms were passed in 2010:

- Four emerging market countries (Brazil, China, India, and Russia) have been included among the 10 largest members of the IMF. Other members are the United States, Japan, Germany, France, the United Kingdom, and Italy.
- All members' quotas were increased from a total of approximately SDR 238.5 billion to approximately SDR 477 billion, while the quota shares and voting power of the IMF's poorest member countries will be protected.
- More than 6% of quota shares were shifted to dynamic emerging markets and developing countries and also from over-represented to under-represented members.

Quota subscriptions are a central component of the IMF's financial resources; however, its financial resources can supplement its quota component through borrowing if it believes that they might fall short of members' needs. The lending countries receive market-rate interest on most of their quota subscription, plus any of their own-currency subscriptions that are loaned out by the IMF, plus all of the reserve assets that they provide the IMF. At the end of 2016, the fund had SDR 477 billion (or $668 billion). Through quota contribution and borrowing, the IMF has created its two assets: Special Drawing Rights (SDRs) and gold reserves.

3.1. Special Drawing Rights

In 1969, the IMF has created "Special Drawing Rights (SDR), which is an international reserve asset, to supplement its member countries" official reserves. The SDR basket comprises the currencies that are issued by the IMF member countries or their monetary unions whose exports had the largest value over a 5-year period, and have been determined by the IMF to be "freely usable." The export criterion aims to ensure that the currencies that qualify for the basket are those issued by the member countries or their monetary unions that play a central role in the global economy. This criterion has been part of the SDR methodology since the 1970s. A "freely usable" currency indicates a currency that is widely used to make payments for international transactions and widely traded in the principal exchange markets. This concept is different from "free floating" and "convertibility." In 2016, the IMF adopted a new formula for determining the currency weights in the SDR basket to address long-recognized issues with the formula. Moreover, the Chinese Renminbi (RMB) has been included in the SDR's basket, because it met all conditions and operational requirements for being determined freely usable. The new formula assigns equal shares to the currency issuer's exports and a composite financial indicator. The financial indicator comprises, in equal shares, official reserves denominated in the member country's (or its monetary union's) currency that are held by other monetary authorities that are not issuers of the relevant currency, foreign exchange turnover in the currency, and the sum of outstanding international bank liabilities and international debt securities denominated in the currency. The weights of the five currencies in the new SDR basket based on the new formula are listed below:

Table 2. Weights in the SDR Basket.

Currency	Weightage	
	2016 Review	2010 Review
US dollar	41.73	41.90
Euro	30.93	37.40
Chinese Renminbi	10.92	00.00
Japanese Yen	8.33	9.40
Pound Sterling	8.09	11.30
	100.00	100.00

3.2. Gold

Despite the collapse of "Gold Standard," it remains an important asset in the reserve holdings of several countries, and the IMF is also still one of the world's largest official holders of gold. Currently, the IMF holds approximately 2,814.1 metric tons of gold at designated depositories. The IMF's total gold holdings are valued at SDR 3.2 billion (or $4.4 billion) on historical cost. However, at current market prices, their value is approximately SDR 83.0 billion (or $113.5 billion). The IMF had acquired its gold holdings through four main channels:

1. When the IMF was founded in 1944, it was decided that 25% of the initial quota subscriptions and the subsequent quota increases were to be paid in gold. This represents the largest source of the IMF's gold.
2. All payments of charges (interest on member countries' use of IMF credit) were normally made in gold.
3. A member wishing to acquire the currency of another member could do so by selling gold to the IMF. The major use of this provision was sales of gold to the IMF by South Africa in 1970-1971.
4. Member countries could also use gold to repay the IMF for the credit previously extended.

4. ROLE IN GLOBAL ECONOMY AND LENDING ACTIVITIES

All members of the IMF are also members of the World Bank (IBRD) and vice versa. Not all member countries of the IMF are sovereign states, and not all "member countries" of the IMF are members of the United Nations. Aruba, Hong Kong, Macau, and Kosovo are not the members of United Nations Organization (UNO), but they are members of the IMF. Cuba and Taiwan are the former members, which were ejected from the UNO. However, "Taiwan Province of China" is still listed in the official IMF indices. Apart from Cuba, the other UN states that do not belong to the IMF are Andorra, Liechtenstein, Monaco, and North Korea.

4.1. Surveillance of Global Economy

IMF members have to refrain from currency restrictions unless granted IMF permission, to abide by the code of conduct in the IMF Articles of Agreement, and to provide national economic information. Member countries of the IMF have access to information on the economic policies of all member countries, the opportunity to influence other members' economic policies, technical assistance in banking, fiscal affairs, and exchange matters, financial support in times of payment difficulties, and increased opportunities for trade and investment. IMF membership is not a difficult task; however, strict rules are imposed on the governments if they want to get monetary assistance from the IMF.

A particular concern of the IMF was to prevent financial crisis from spreading and threatening the entire global financial and currency system. Rather than maintaining a position of oversight of only exchange rates, its function became one of surveillance of the overall macroeconomic performance of member countries. The IMF oversees the international monetary system and monitors the economic and financial policies of its 189 member countries. As part of this process, which occurs both at the global level and in individual countries, the IMF highlights the possible risks to stability and advises on needed policy adjustments. The IMF oversees the international monetary and financial system and monitors the economic and financial policies of its member countries. This activity is known as surveillance, which facilitates international cooperation. The Fund typically analyses the appropriateness of each member country's economic and financial policies for achieving orderly economic growth, and assesses the consequences of these policies for other countries and for the global economy.

4.2. Capacity Development

In addition, the IMF provides technical assistance and training to its member countries to design and implement economic policies. It started the data dissemination work in 1995, with the view of guiding the IMF member countries to disseminate their economic and financial data to the public. The standards for dissemination of data were split into two tiers: The General Data Dissemination System (GDDS) and the Special Data Dissemination Standard (SDDS). The primary objective of the GDDS is to encourage member countries to build a framework to enhance the data quality and statistical capacity building to evaluate statistical

needs, set priorities in enhancing the timeliness, transparency, reliability, and accessibility of financial and economic data. Some entities that are not themselves IMF members (Palestinian Authority, Hong Kong, Macau, European Central Bank for the Eurozone, Eurostat for the whole EU including Cyprus and Malta) also contribute statistical data to the systems.

4.3. Lending

Most crucial and highly debated function of the IMF is the lending and the policy recommendations attached with it. Different from development banks, the IMF does not lend for specific projects. Its core responsibility is to provide loans to member countries that are experiencing problems related to balance of payments. This financial assistance enables countries to rebuild their international reserves, stabilize their currencies, continue paying for imports, and restore conditions for strong economic growth, while undertaking policies to correct underlying problems.

There are several types of lending facilities provided by the IMF:

- Low-income countries can borrow on concessional terms, which indicate that there is a period of time with no interest rates, through the extended credit facility (ECF), standby credit facility (SCF), and the rapid credit facility (RCF).
- No concessional loans, which include interest rates, are provided mainly through stand-by arrangements (SBA), the flexible credit line (FCL), the precautionary and liquidity line (PLL), and the extended fund facility.
- The IMF provides emergency assistance via the rapid financing instrument (RFI) to members experiencing urgent balance-of-payment needs.

At present, there are 189 member countries having 41 lending arrangements. The lending capacity of the IMF stood at US $ 1 trillion, while, since 2008, the IMF has provided 172 loans to member nations.

Under current lending arrangements, the IMF committed US$159 billion loans, of which US$144 billion have not been drawn. Portugal, Greece, Ukraine, and Pakistan are the biggest borrowers; whereas, the biggest precautionary loans were sanctioned to Mexico, Poland, Colombia, and Morocco.

In May 2010, the IMF participated, in 3:11 proportion, in the first Greek bailout that totaled €110 billion, to address the great accumulation of public debt, caused by continuing large public sector deficits. As part of the bailout, the Greek government agreed to adopt austerity measures that would reduce the deficit from 11% in 2009 to "well below 3%" in 2014. A second bailout package of more than €100 billion was agreed over the course of a few months from October 2011. As of January 2012, the largest borrowers from the IMF in order were Greece, Portugal, Ireland, Romania, and Ukraine. In 2013, a €10 billion international bailout of Cyprus was agreed by the IMF led consortium. At the end of March 2014, the IMF secured an $18 billion bailout fund for the provisional government of Ukraine in the aftermath of the 2014 Ukrainian revolution.

In 2010, the IMF could make loans to Greece in an unsustainable and political situation. The staff was directed to formulate an updated policy. The staff proposed that "in circumstances where a (Sovereign) member has lost market access and debt is considered sustainable, the IMF would be able to provide Exceptional Access on the basis of a debt operation that involves an extension of maturities," which was labeled a "reprofiling operation." These reprofiling operations would "generally be less costly to the debtor and creditors." Creditors will only agree if they understand that such an amendment is necessary to avoid a worse outcome: namely, a default and/or an operation involving debt reduction.

4.4. Rational Behind Conditionality and Policy Recommendations

The IMF negotiates conditions on lending. For this purpose, it legislated a "policy of conditionality" in the 1950s. Conditionality is associated with economic theory as well as an enforcement mechanism for repayment. Stemming primarily from the work of Jacques Polak (1957), the theoretical underpinning of conditionality was the "monetary approach to the balance of payments." Cutting expenditures (austerity), focusing economic output on direct export, devaluation of currencies, trade liberalization by lifting restrictions on import and export, increasing the stability of investment by supplementing foreign direct investment with the opening of domestic stock markets, balancing budgets, removing price controls and state subsidies, privatization, or divestiture of state-owned enterprises, enhancing the rights of foreign investors through

amendments in national laws, improving governance, and fighting corruption are included in the conditions for structural adjustment. It was hypothesized that these conditions ensure that the borrowing country will be able to repay the IMF and that the country will not attempt to solve their balance-of-payment problems in a way that would negatively impact the international economy. According to the IMF, the adoption of certain policies by the member will allow it to repay the IMF, thereby ensuring that the resources will be available to support other members. The borrowing countries have a very good track record for repaying credit extended under the IMF's regular lending facilities with full interest over the duration of the loan. It envisaged that IMF lending does not impose a burden on creditor countries.

5. OVER EMPHASIZE ON FISCAL POLICIES

The competitiveness, economic freedom, liberalism, globalization, and small governments are the popular slogans that support the popular supply-side economic policies. However, in this age of globalization and competitiveness, the IMF emphasizes on demand management policies. The development of physical and institutional infrastructure is the core ingredient of supply-side policies. The acceleration in economic growth is not possible in the absence of proper infrastructure, while IMF policies do not recommend the development of infrastructure, while ranking of infrastructure (World Economic Forum, 2011) does not show a correlation between infrastructure development and liquidity crisis that require funding from the IMF. Various studies have explored the priority of rebuilding the infrastructure in those countries that are provided the highest credit facilities by the IMF (Mehar, 2015). This type of development is necessary not only for economic growth, but also for the very survival of the country. It is most important to note that without developing the physical infrastructure industrialization and the flow of investment into commodity production and service sectors will dry up.

It is a well-known and established reality that, in its agreement, the IMF has been emphasizing on demand management policies that mainly belong to fiscal policy measures. The majority of its recommendation requires the upsizing of public financing and greater role of government in the economy. Contrary to this, it is also an established fact that people in the countries in problems do not have confidence in their public policies. They believe that corrupt practices and misuse of public funds are the major causes of economic miseries. It can be envisaged through the following tables that people do not have confidence in their government in case of those 10 top countries that have been provided the largest credit facilities by the IMF.

The history of public finance in those countries indicates the misuse of funds for the development of politically motivated projects: to offset the losses of commercial institutions in the public sector, to create inflated employment opportunities, to subsidize public services, and to finance unnecessary populist projects (Mehar, 2015). The cost of these bad decisions are ultimately paid by the middle and lower middle-class people in the form of direct or indirect taxes, while the majority of wealthy people do not contribute taxes, although they continue to consume and utilize public funds for their political objectives. In some cases, the IMF has over emphasized in enhancing the tax-to-GDP ratio despite the reality that business sector and common people are paying high taxes and those countries are included in the top most countries where tax rates are highest and people have to pay multiple taxes. In fact, the cause of lower tax-to-GDP ratio in those countries is the unequal burden of taxes as many sectors and segment are constitutionally exempted from taxes. However, the IMF does not recommend taxes on those segments because of political motivation. These powerful segments are supported by international forces. Moreover, it is a common intuitive that international forces do not allow the IMF to recommend any measures against the interests of those powerful elements. A report released by Fiscal Policy Department of IMF (Gupta, 2014) stated that "Some taxes levied on wealth, especially on immovable property, are also an option for economies seeking more progressive taxation. Property taxes are equitable and efficient, but underutilized in many economies and there is considerable scope to exploit this tax more fully, both as a revenue source and as a redistributive instrument." The IMF does not recommend measures to bring these sources in tax net.

Three decades of public policy failures, unfavorable monetary policies, a growing debt burden, a decreasing tax-to-GDP ratio, an uneven distribution of taxes, widespread feudalist landholding structures, and deteriorating business competitiveness indicate that the only option is to rebuild the economy by adopting supply-side policies.

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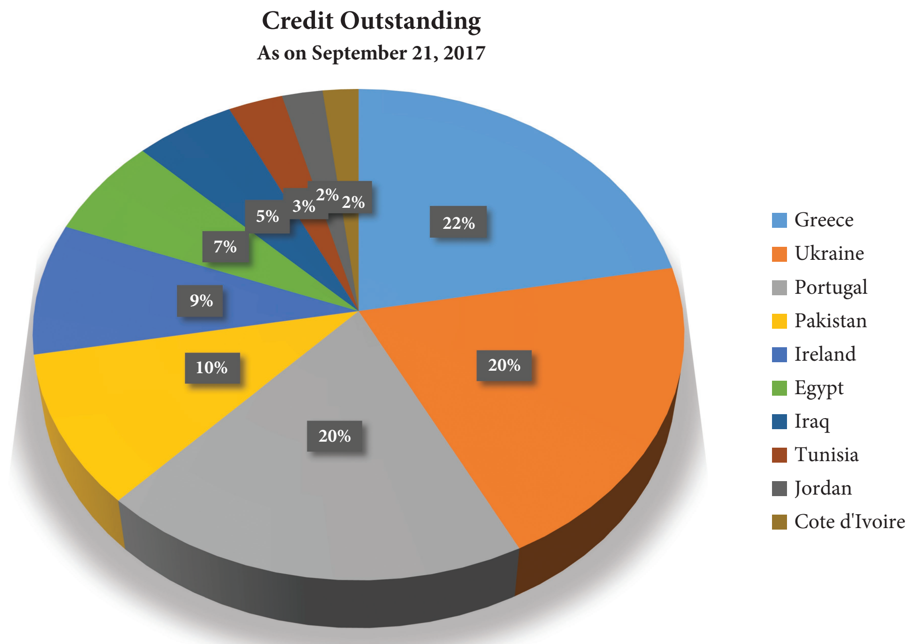
Table 3. Top 10 IMF Credit Outstanding Countries (Million US$): Tax Burden and Public Repute.

No.	Member	Credit outstanding (As on September 21, 2017)	% of global IMF credit outstanding	Overall taxes on businesses (% of Profits)	Quality of infrastructure (Ranked by WEF)	Public trust in politicians (Ranked by WEF)
1	Greece	9,641	18.27	44.7	58	137
2	Ukraine	8,893	16.85	43.0	70	40
3	Portugal	8,545	16.19	47.4	14	93
4	Pakistan	4,393	8.32	–	100	–
5	Ireland	3,772	7.15	26.5	69	65
6	Egypt	2,865	5.43	31.1	68	43
7	Iraq	2,385	4.52	31.6	–	91
8	Tunisia	1,295	2.45	42.9	30	57
9	Jordan	966	1.83	62.8	35	15
10	Cote d'Ivoire	846	1.60	57.2	77	122
Total (above 10)		43,601	82.62	–	–	–
Total (All 74 countries)		**52,774**	**100.00**	**–**	**–**	**–**



The scholarly consensus is that the IMF decision making is not simply technocratic, but also guided by political and economic concerns. The United States is the IMF's most powerful member, and its influence reaches even into decision making concerning individual loan agreements. Reforms to provide more powers to emerging economies were agreed by the G20 in 2010.

One view is that conditionality undermines domestic political institutions. The recipient governments are sacrificing policy autonomy in exchange for funds, which can lead to public resentment of the local leadership for accepting and enforcing the IMF conditions. Political instability can result from more leadership turnover as political leaders are replaced in electoral backlashes.

The IMF sometimes advocates "austerity programmers," cutting public spending and increasing taxes even when the economy is weak, to bring budgets closer to a balance, thus reducing budget deficits. Countries are frequently advised to lower their corporate tax rate. Joseph E. Stiglitz (2002), former chief economist and senior vice-president at the World Bank, criticizes these policies.

Table 4. The Global Competitiveness Index.

Country/factor of competitiveness	Overall index		Basic requirements		Efficiency enhancers		Innovations factors	
	Rank	Score	Rank	Score	Rank	Score	Rank	Score
Côte d'Ivoire	116	3.43	121	3.49	109	3.38	98	3.20
Egypt	70	4.04	78	4.21	80	3.87	71	3.51
Greece	71	4.04	56	4.49	57	4.13	66	3.59
Iraq	–	–	–	–	–	–	–	–
Ireland	25	4.84	37	5.06	22	4.87	20	4.63
Jordan	50	4.30	46	4.74	66	4.06	51	3.79
Pakistan	101	3.58	114	3.53	92	3.69	84	3.39
Portugal	43	4.40	39	5.05	43	4.40	41	3.98
Tunisia	40	4.50	35	5.09	56	4.14	45	3.94
Ukraine	82	3.95	94	3.96	68	4.05	80	3.42

Table 5. Total Tax Rate, Public Trust in Politicians, and Use of Public Money.

Country	Overall taxes on businesses		Diversion of public funds		Public Trust in Politicians	
	% of Profits	Rank	Score	Rank	Score	Rank
Côte d'Ivoire	44.7	83	2.0	132	1.6	137
Egypt	43.0	78	3.1	83	3.6	40
Greece	47.4	92	2.9	94	2.2	93
Iraq	–	–	–	–	–	–
Ireland	26.5	22	5.3	21	3.0	65
Jordan	31.1	32	4.3	41	3.5	43
Pakistan	31.6	37	3.0	92	2.3	91
Portugal	42.9	76	4.1	45	3.2	57
Tunisia	62.8	119	5.5	20	5.0	15
Ukraine	57.2	113	2.2	129	1.9	122

Diversion of public funds indicates the diversion of public funds to companies, individuals, or groups owing to corruption: 1 = very common; 7 = never.
Public trust in politicians indicates the level of public trust in the ethical standards of politicians in a country: 1 = very low; 7 = very high.

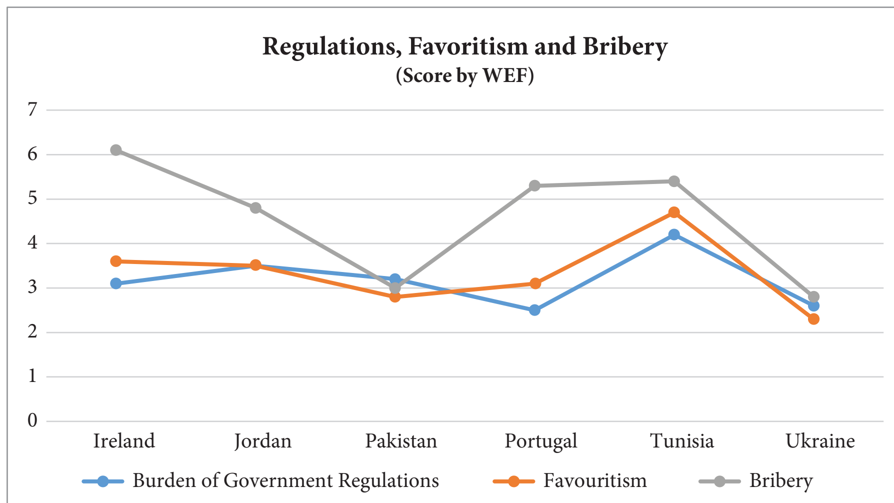
There has been persisting opinion that the IMF is constantly dominated by the developed countries. Accordingly, the developing economies had started raising voice for reforms in the IMF.

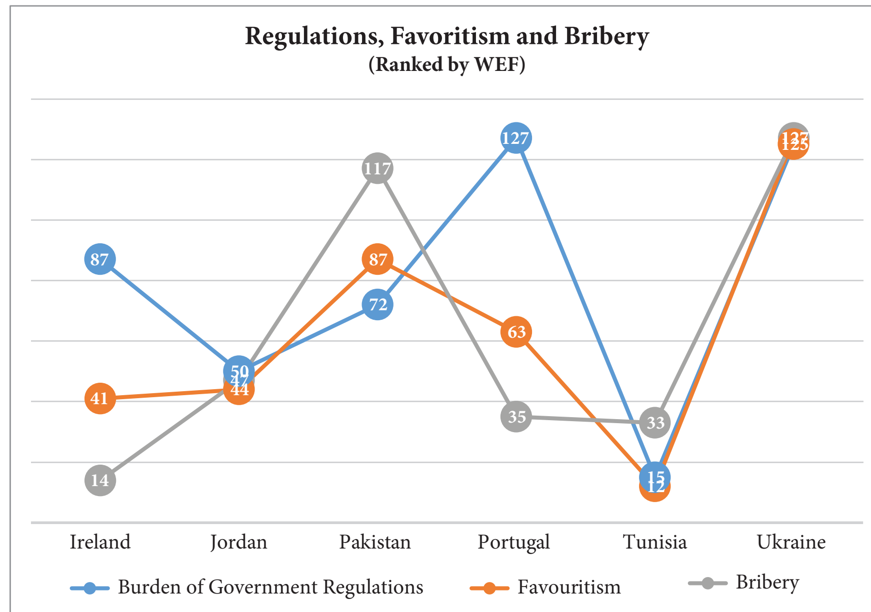
A study by Bumba Mukherjee (2008) found that developing democratic countries benefit more from the IMF programs than the developing autocratic countries. This is because policy making and the process of deciding where loaned money is used are more transparent within a democracy. Although earlier studies found little impact of IMF programs on the balance of payments, more recent studies using more sophisticated methods and larger samples "usually found IMF programs improved the balance of payments" (Jensen, 2004).

Table 6. Excessive Regulations, Favoritism, and Bribes.

Country	Burden of government regulations		Favoritism in decisions of government officials		Irregular payments and bribes	
	Score	Rank	Score	Rank	Score	Rank
Côte d'Ivoire	2.9	103	2.3	129	2.6	136
Egypt	3.1	79	2.7	95	4.1	64
Greece	2.4	129	2.6	105	3.6	89
Iraq	–	–	–	–	–	–
Ireland	3.1	87	3.6	41	6.1	14
Jordan	3.5	50	3.5	44	4.8	47
Pakistan	3.2	72	2.8	87	3.0	117
Portugal	2.5	127	3.1	63	5.3	35
Tunisia	4.2	15	4.7	12	5.4	33
Ukraine	2.6	125	2.3	127	2.8	127

Burden of government regulation: 1 = extremely burdensome; 7 = not burdensome at all.
Favoritism in decisions of government officials: 1 = always show favoritism; 7 = never shows favoritism.
Irregular payments and bribes: This indicator represents extra payments or bribes connected with imports and exports, public utilities, annual tax payments, awarding of public contracts and licenses, and obtaining favorable judicial decisions. 1 indicates very common, and 7 indicates never occurs.





The Group of 24 (G-24), on behalf of Least Developed Countries (LDC) members, and the United Nations Conference on Trade and Development (UNCTAD) complained that the IMF did not distinguish sufficiently between disequilibria with predominantly external as opposed to internal causes. Then, LDCs found themselves with payment deficits owing to adverse changes in their terms of trade, with the fund prescribing stabilization programs similar to those suggested for deficits caused by government over-spending. Experienced with long term, externally generated disequilibria, the G-24 argued for more time for LDCs to adjust their economies (Alexander, 1996).

6. OVERLOOKING MONETARY MECHANISM

Monetary policy is a part of overall economic planning and strategies, which are responsible to provide an environment to the public for their economic development and well-being. Surprisingly, the IMF do not pay considerable emphasize on the monetary measures in its recommended demand management policies. However, its primary objective was to safeguard the international monetary system and prepare devices to ensure monetary transactions without distortion in international money market. It has been observed that in IMF is limited only to suggest a devaluation for international transactions and rate of interest for domestic markets of borrowing countries. It does not consider the monetary policies in a broader sense, though such policies may create several problems in domestic and international markets. For instance, a monetary policy may be a most “regressive option” in the liberalization because of its drastic effects. There are several mechanisms that make monetary policy a regressive option to manage the economies. The most important is the interest rate spread. How a monetary policy can add economic miseries can be described in the following simplified model (Mehar, 2011).

In this study, it was hypothesized that growth in money supply affects the economic growth and inflation directly. This hypothesis has been established in the following equations of the model:

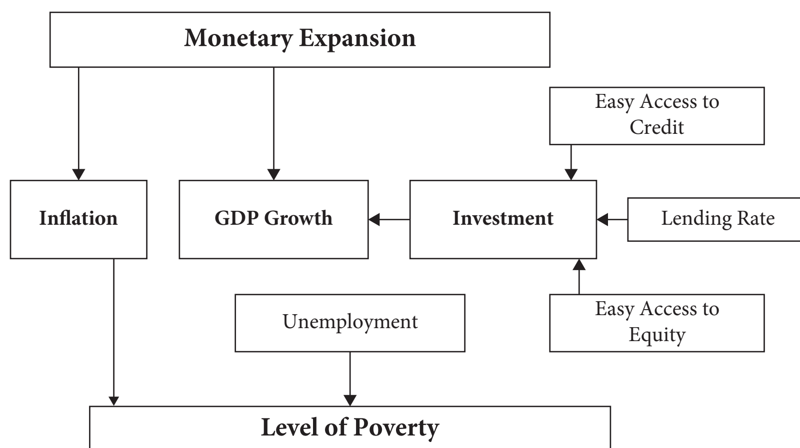
$$\text{GGDP} = \text{a0} + \text{a1 ITOGDP} + \text{a2 GM2} \tag{1}$$

$$\text{Infl} = \text{b0} + \text{b1GM2} \tag{2}$$

where GGDP is the annual growth in Gross Domestic Product in percentage, ITOGDP is the investment-to-GDP ratio, GM2 is the annual growth in Money Supply (M2), and Infl is the annual rate of inflation.

A higher spread indicates that depositors are receiving lesser return on their deposits as compared to the investors. If, in an economy, the larger part of bank deposits belongs to the lower income groups—such

Figure 1. The Simultaneity in the Model Effect of Monetary Expansion on Poverty.



as household savings, retirement money, pension funds, and endowments for orphans, old age peoples, non-working widows, and disable persons—the higher spread will make the monetary system regressive. Another common phenomenon in contemporary monetary and banking practices is the higher rate of return on the higher level of deposits. Evidently, it provides more earning opportunities to the well worthy peoples. The increasing (or constant) return to scale on the monetary assets may also enhance the rich–poor gap and poverty levels. The similar practice is the higher rate of return on the deposits of longer duration. There is no need to mention that only the rich people can afford the higher duration of fixed deposits, while lower income groups do not have either their bank accounts or they prefer to deposit their money on saving accounts where withdrawal of their money cannot be predictable. The IMF is a monetary institution, and it should consider the monetary policy-related recommendation in a broader sense.

A higher rate of interest may lead the cost push inflation in those economies where producers are used to obtain financing facilities for their production process and inventory holding through working capital loans from the banking sector. The industries—such as sugar, textile, tobacco, and food,—where availability of raw material depends on crop seasons, and the sales activities are spread over the year are likely to adopt working capital financing from banking sector; this situation will lead to higher inflation if interest rate increases. Again, the lower income groups will be the net looser, if the products are commonly used.

For desirable outcomes of monetary expansion, the rate of GDP growth should be greater than the rate of inflation. In case of lower rate of growth, the higher growth in investment is the only option to enhance the GDP growth. However, it is considerably difficult to determine the factors of investment in a common equation because of the complexity and variations in determining the investment in different economies. The lending rate of interest and the access to capital are the common factors in determination of the level of investment. Consequently, it was hypothesized in this study that investment is determined by the lending rate of interest and easy access to the capital. To test this relation, the following equation has been estimated:

$$ITOGDP = c0 + c1LRAT + c2EACR + c3EAEQ \qquad (3)$$

where ITOGDP is the investment-to-GDP ratio, LRAT is the rate of interest on lending, ECAR is the index that indicates easy access to credit, and EAEQ is the index that indicates easy access to equity.

The above-mentioned indexes have been constructed by the World Economic Forum (2011). The data on the above variables has been extracted from the World Economic Forum (2010a); whereas, its methodology is extracted from the study completed in Iqra University (Mehar, 2011). According to the models, growth in money supply (M2)—either by public sector or private sector credit—will affect the growth and inflation in the country. The growth and inflation jointly determine the effect of monetary policy on the level of poverty.

Table 7. Impacts of Monetary Policy.

Dependent variable	Average growth in GDP		Rate of inflation (CPI)		Investment to GDP ratio	
Independent variables	**Coefficients**	**T-statistics**	**Coefficients**	**T-statistics**	**Coefficients**	**T-statistics**
Intercept	0.203	0.251	0.242	0.360	23.063	4.762
Investment to GDP	0.097	3.010	–	–	–	–
Growth in M2	0.118	6.709	0.378	11.128	–	–
Lending rate	–	–	–	–	−0.203	−2.124
Easy access to credit	–	–	–	–	3.205	2.358
Easy access to equity	–	–	–	–	−2.137	−1.662
Adjusted R-square	0.3581		0.5320		0.1218	
No. of observations	109		109		36	

The credit expansion in both the cases—financing budget deficit and credit to private sector—will lead to growth in the money supply (M2); whereas, price acceleration because of shifting the demand of goods and services will be a natural consequence of this monetary expansion. However, a parallel increase in the supply of goods and service may lead to a higher economic growth. An increase in the supply of goods and services may lead to increase in the utilization of capital and labor in the economy. If the effect of monetary easing on inflation is stronger than its effect on growth, it will lead to a higher level of poverty in the economy, while a stronger effect on growth may lead to a reduction in poverty. It is a precondition that no obstacle should be involved in the tickle downing of the effect of growth on employment level. Here, it is noteworthy that sometimes credit easing and banking policies may create obstacles in the transformation of desirable effects of economic growth to the lower income groups. This situation will be discussed in the next section with details.

It was also hypothesized that investment is an important determinant of economic growth. The above-mentioned model explores that how growth in investment affect the growth of GDP. Here, it was proposed that growth in investment will lead to reduction in the unemployment. Consequently, if the desirable effect of monetary policy on GDP growth is less than its effect on inflation, the higher investment activity is the only option to increase the rate of growth.

Monetary policy is also a key determinant of investment. Equation III explains that the interest rate for lending from banks and the easy access to credit is the important determinant of investment. Both the lending rate of interest and the easy access to credit are the parts of monetary policy. Consequently, again monetary policy can affect the poverty by generating employment opportunities through boosting the investment activities in the economy.

It was further proposed that simultaneous investment activities are required in all sectors for overall economic development. It was commonly observed in case of developing countries that the access to capital by the smaller sectors is ignored by the planning authorities. Monetary policy should address this issue to develop the small and medium businesses to derive the demand of the large industrial products. The estimated results indicate that easy access to credit is an important and significant determinant of the investment, and the investment activities in isolation cannot be succeeded unless parallel investment activities are not available in the associated sectors. The qualitative easing is a required policy to make access of credit easy for the lower income people and small businesses. The small and medium businesses provide catalyst for the development of large-scale businesses. In most of the cases, small and medium businesses create demand of the products of large-scale businesses; they also provide raw material and services to the large-scale businesses. Consequently, they cannot be ignored in the monetary policy transformation mechanism. The qualitative tightening in monetary policy can adversely affect the small and medium businesses and ultimately the poor and lower income groups in the economy.

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The access of poor and small businesses to the bank financing shows a drastic picture in the global economies. In majority of cases, a negligible part of the poor people in a country can access to the banks for financing. Table 1 indicates that Bangladesh is an exceptional case, where financing to poor and small business has a significant portion. Morocco, Vietnam, Mexico, Indonesia, Peru, and Jordon are the other appropriate examples, and it has been observed by the country analysis that these countries have significant control over the poverty issue. Table 2 shows that majority of the business enterprises do not have a loan. The more important is that more than 87% business enterprises did not apply for loan.

The estimated results of the model have been shown in the above table. All the parameters are statistically significant except "Easy Access to Equity" in the determination of investment. It indicates that investment depends significantly on the rate of interest for lending and easy access to credit. Both the determinants are the parts of monetary policy, and they do not belong to quantitative easing. Therefore, it was concluded that for higher investment and for higher growth in GDP the credit easing is required. Particularly, it is a required policy when quantitative easing has been adopted, which may lead the higher inflation and consequently higher level of poverty. The results established the following corollaries:

Corollary I: "The creation of money—either to finance the budget deficit or credit to private sector—will always lead the inflation. This principle is not associated with the disbursement and utilization of debts without change in monetary expansion. A debt without monetary expansion will change the patterns of priorities of demand for goods and service. This situation may lead the changes in the prices of several commodities in both the directions. However, it will not be responsible for aggregate change in price level."

Corollary II: The upward changes in the prices of some goods may lead the changes in the prices of other goods in the same direction. The higher cost of inputs and maintaining the real profits are the causes of this type of price movement.

Corollary III: An upward change in the supply of goods and services may defuse the demand pull inflationary pressures; this is possible if growth in investment activities by utilization of capital and labor. The credit easing can attract the investment activities in the economy.

Corollary VI: A parallel Credit Easing Monetary Policy is always required with the Quantitative Easing for tuning the rate of GDP growth, investment, inflation, unemployment, and level of poverty.

Currently, even in the age of liberalization, the central banks provide a signal to the banks through announcing "discount rate" in its monetary policy statement. This discount rate influences the money market equilibrium, which limits the economic growth. It is surprising that the IMF becomes a part in this distortion by intervening in market mechanism through describing the changes in interest rates and the value of currencies.

7. CONCLUSIONS AND RECOMMENDATIONS

The discussion in previous sections derived some important conclusions, which indicate that in the present global economic scenario where world economies are following considerable openness and liberalization policies, IMF has to restructure its lending policies, while some modifications in its governance are also recommendable. The conclusion can be summarized in the following points:

7.1. Liberalism Requires Supply-side Approach

The end of a bipolar regime after the collapse of the Soviet Union diverted the world economies to globalization regime, where economic freedom and liberalization have been adopted as most powerful and popular philosophies of the economic welfare and development. The origination of a free trade regime, decentralization in public finance, and revival of the classical school of thought in economic policies are the natural outcomes of the global failure of centrally controlled economic planning experiences. Autonomy of the central banks, market-oriented exchange rates, convertibility of the currencies, privatization, deregulation, and free trade are the banners of classical economic thoughts in the present regime. The IMF came into force when the world was divided in left and right arms. The left-arm countries have been avoided from joining

the IMF system. Even the capitalism in those days widely recognized the Keynesian model to intervene in the economy through fiscal policies—subsidies, transfer payments, and taxation policies. The IMF conditionality and recommended measures are still based on demand management mechanism where most of the advices belong to the exchange rate mechanism (devaluation), increase in interest rate, increase in tax revenue, reduction in subsidies and transfer payments, etc. Evidently, these recommendations are based on the presumptions that national economic issues have emerged because of domestic policies. In today's world, every country has—willingly or unwillingly—adopted globalization. Where inflow of workers' remittances, foreign investment, foreign trade in goods and services, and official flows to public sector to finance global activities in its geographical boundaries. These global activities may belong to military operation against terrorists' activities, health improving and environmental activities, operation to perform MDGs, and capacity building for international trade. Global political and economic factors such as unpredictable increase in oil prices, wars, and political changes and tension in neighboring countries may become a major cause of the outflow of foreign investment, sudden increase in import bill, and drop in domestic outputs. In these situations, a demand management policy will further deteriorate the situation.

7.2. Market-based Interest and Exchange Rates—Not Devaluation

So far, as the recommendations of devaluation and fiscal measures by IMF are concerned, one can easily observe that all such measures are anti-liberalism and anti-economic freedom. The devaluation policy cannot enhance the exports of inelastic goods in an era of growing share of trade in services in world trade basket. For the developing countries, the devaluation causes a sudden increase in the burden of debt and badly hits the gearing ratio in terms of domestic currencies. Resultantly, the liability of repayment of debts' installment and the attached cost of interest increase without generating new debts, and push the governments to increase tax collection to finance the debt servicing. The increase in indirect taxes—particularly General Sales Tax (GST), which is evidently a regressive tax—seems the easiest in those countries. However, majority of goods and services are categorized as inelastic from the consumers' point of view. Oil and its products, medicines, foods, and edible items are included in those inelastic products. An increase in prices of these inelastic products will generate an inertia in the price determination of other commodities, which further accelerate inflation in the domestic market. This accelerated inflation not only increases the economic miseries of the people, but also increases the cost of exportable goods. Moreover, exports may become uncompetitive, which is against the primary objective of devaluation policy. Another drastic effect of devaluation policy is the increasing cost of capital goods that are imported from industrialized countries. The increasing cost of capital goods may adversely affect the investment activities and the employment in the country. Such situation leads to the increasing chances of bankruptcy.

7.3. Depart from Over Emphasized Fiscal Management

The IMF programs are designed to address excessive government spending, excessive government intervention in markets, and considerable state ownership. This assumes that this narrow range of issues represents the only possible problems. The proper way to enhance the economic health of sick countries is to promote economic freedom and liberalism. For this purpose, the IMF should emphasize of "small government" instead of increasing the tax-to-GDP ratio of collecting more taxes. To enhance the fiscal governance, the IMF should device a mechanism to support transparency in the monetary transactions. Particularly, it should address this issue in the age of growing use of e-money. The IMF should incorporate e-money and other medium of exchange in the broader definition of money to incorporate their effects on macroeconomic performance.

7.4. Coordination and Consistency with Other International Organizations

All the above-mentioned factors conclude that the only option available for the sustainable development is the development of infrastructure. The IMF funding does not address this issue; even public sector loans and lending agencies cannot resolve this issue in the present competitive age. It can be resolved with the help of foreign direct investment through globally recognized and well-established development firms in the private sector. Project financing, infrastructure bonds, and equity participation are all possible options to generate funds for development in the developing countries. In this manner, the inflow of foreign direct investment can rebuild the economy through the development of infrastructure facilities. The foreign companies in the energy, civil construction, telecommunications, and transportation industries can redevelop

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the economy, which would then lead to the development in the manufacturing and high-tech sector. To support the inflow of foreign investment in these mega-projects, legal and institutional support is required. Political governance and policy makers have to play an important role in the success of this policy. The IMF should develop its policy framework and recommendation in agreement with such developing agreements.

It is notable that the IMF is one of the many international organizations that are providing assistance to world economies. The role of the IMF is limited to provide assistance to manage liquidity crisis. WTO and WEF are the representatives of classical economic approach; they support liberalism and globalization. In the present scenario, the IMF should design its polices in harmonization of those institutions. Here, it is also mentionable that to enhance exports the devaluation is not an effective mechanism, which has repeatedly been suggested by the IMF. Currently, Non-Tariff Measures (NTMs) have become the most effective tool of trade barriers. The IMF should adopt the WTO policies to identify NTM, and it should suggest the measures for competitiveness in uniformity of WEF to develop the economies.

7.5. Creating Corporate Senate to Overcoming Borrower–Creditor Divide

It has been discussed in previous sections that rich countries provide considerable financial resources to the IMF, but it is used by poor countries. Meanwhile, decisions are made by the rich countries, as they have significant higher voting rights. Resultantly, the IMF's membership is divided into two groups with entirely different interests. Similar to the governance of corporate sector in some countries, it is recommended that the IMF should introduce a concept of "IMF Senate." The membership of IMF Senate should be based on one country one vote. It may be like "the Upper House" in Parliamentary systems in some countries. The decision that has been approved by the Executive Board must be approved and examined by the IMF Senate. A mechanism should be devised to balance the powers of the Executive Board and the IMF Senate.

Another important thing is the change in the way of classification of countries. In today's world, all countries are developing countries. In today's fast developing world, no country can be considered a developed country for long time. The development is a continuous phenomenon. Countries are compared on the basis of their relative economic strength. In relative term, every country is moving either forward or backward. Therefore, every country is a developing country (or "inversely developing country" if it losing its relative strength in global comparison). The present stage of development should not be compared with the past, while the responsibility of the IMF is not to intervene in the determination of the relative strength of the countries. Its role should be to monitor a fair game and provide assistance to the countries for preparing the fair game.

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Reforms in International Monetary Fund (IMF): Challenges and the Road Ahead

Niti Bhasin*, Surbhi Gupta
Department of Commerce, Delhi School of Economics, University of Delhi, New Delhi, Delhi, India.

***Correspondence:** nitisurydse@gmail.com

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Abstract

A prosperous and stable world economy is in the self-interest of every nation. The International Monetary Fund (IMF), which is a worldwide institution that facilitates prosperity and stability, was founded in 1944 to restructure the world economy ruined by the Second World War and to design the postwar international monetary system. Since its inception, IMF has been playing an important role in the promotion of world trade and solving Balance of Payments (BOP) difficulties of its member countries, especially the developing ones. Despite its significant contribution, the IMF has been severely criticized by academics, politicians, and public interest groups on the grounds that it is dominated by the developed nations, and hence better serves the interest of the wealthy nations as opposed to the world's poor majority. Even after several reforms introduced over a period of 70 years to improve and strengthen the representation of the developing countries, there are four critical issues that are yet to be addressed: dominance, governance, loan conditionality, and quota system. In this context, this paper aims to study the reforms introduced by the IMF over the years, analyze the key areas where reforms are still needed in the light of existing criticisms directed at the IMF's functioning and governance, and suggest the direction of reforms to address the prevailing challenges faced by the IMF.

Keywords: IMF; Reforms; Surveillance; Governance; Quota.

1. INTRODUCTION

The First World War and the subsequent events like the Great Depression of the 1930s and the Second World War deteriorated the international monetary system with detrimental effects on international trade and investment. During the interwar period of 1914–1944, every economy in an effort to recover used predatory devaluation of their currencies as a means of gaining advantages in the world export market and increasing the price of imports. Trade restrictions were also imposed to eliminate the impact on domestic income, leading to lowering of world trade and increase in unemployment. So in the cycle of competitive devaluations, no country could win. In a nutshell, the interwar period was characterized by economic and political instability, bank failures, deteriorating world trade, currency issues, capital flights across borders, the abolition of the gold standard as the system of international payments, and the emergence of dollar as the dominant world currency by gradually replacing the British pound.

In an effort to restructure the world economy and to discuss and design the post-war international monetary system, in July 1944, representatives of 44 nations gathered at Bretton Woods, New Hampshire, USA. The Bretton Woods Conference resulted in the establishment of two multilateral institutions, namely International Monetary Fund (IMF) and International Bank for Reconstruction and Development, popularly known as the World Bank, on July 24, 1944. The founding members signed the Articles of Agreement (AOA) of the IMF, which constitutes the core of the Bretton Woods System. Under this system, each country established a par value in relation to the U.S. dollar, which was pegged to gold at $35 per ounce, and then calculated the gold par value of the currency based on that selected dollar exchange rate. Dollar was the only currency to be convertible into gold. Each country was responsible for maintaining its exchange rate within −1% and +1% of the adopted par value. Countries were not allowed to use devaluation as a weapon of competitive trade policy or beggar-thy-neighbor policy. However, if a currency became too weak to defend, a devaluation up to 10% was allowed without any formal approval by the IMF.

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The primary objectives of the IMF, on its inception, were to promote international monetary cooperation, exchange rate stability, and orderly exchange arrangements by avoiding competitive devaluations; to provide financial assistance to countries facing short-term balance of payments difficulties; to facilitate the balanced growth of international trade; and to foster sustainable economic growth with enhanced productive capacity and employment levels globally. It also committed its members to move as rapidly as possible to current account convertibility, although it allowed them to retain restrictions on international capital flows.

Keeping in mind the above objectives, on March 1, 1947, the IMF began its financial operations, and on May 8, 1947, France became the first country to borrow from it. After the demise of Bretton Woods System in the year 1973 and introduction of floating exchange rate system, the IMF members amended the IMF's Charter and accordingly its operations were reduced. The role of the IMF became more active as a manager or surveillant of overall macroeconomic policy of its member countries rather than just maintaining an oversight of the exchange rates. During the 1980s, after the outbreak of the international debt crisis, the IMF reemerged once again with a new mandate to prevent financial crisis among the emerging market countries, particularly the middle-income countries, which are vulnerable to massive capital outflows. The IMF took a lead role when Mexico in 1982 and Brazil in 1987 announced that they would no longer be able to service their debt obligations. Also at the time of East Asian crisis in 1997-1998, the IMF held its influential role in the international financial system and lent unprecedented amounts of money to Thailand, Indonesia, and Korea to stop the contagion effect of the crisis in other Asian countries and elsewhere (Head, 2003).

During the early 2000s, the IMF faced another crisis of legitimacy and purpose owing to the declining demand for IMF loans due to the absence of large-scale financial crisis, increased availability from private international markets for middle-income emerging market countries, piling of large foreign exchange reserves by these economies, and growing dissatisfaction with the IMF's advice and loan conditionality. The IMF's financial woes were highlighted in May 2006 when its managing director Rogrido de Rato appointed an expert group to advise him on how to develop alternative sources of income for the IMF (Helleiner and Momani, 2007). Later on, the global financial crisis of 2007–2009 posed a deep challenge for many IMF members, especially the Euro zone area, and for the Fund itself. The Fund called for a comprehensive plan for greater European financial and fiscal integration. The major bailouts by the IMF post-global financial crisis include the first Greek bailout in May 2010 that totaled €110 billion, to address the ballooning government debt, caused by continuing large public sector deficits; a €10 billion international bailout of Cyprus on March 25, 2013; at the end of March 2014, the IMF secured an $18 billion bailout fund for the provisional government of Ukraine in the aftermath of the 2014 Ukrainian revolution.

Since its inception, the IMF has been playing an important role in the promotion of world trade and solving BOP difficulties of its member countries, especially the developing ones. A prosperous and stable world economy is in the self-interest of every nation—large and small, rich and poor, and the IMF is the worldwide institution that facilitates prosperity and stability. At present, 189 countries are members of the IMF, having 41 lending arrangements. The IMF is continuously working toward better financial sector regulation and supervision to ensure that the world does not return to the financial system that produced the crisis.

Although IMF has been persistently playing an important role in the promotion of world trade and investment, it has been severely criticized by academics, politicians, and public interest groups on the grounds that it is dominated by the developed nations and hence better serves the interest of the wealthy nations as opposed to the world's poor majority. Over the years, there have been many reforms relating to its governance, surveillance, and loan conditionality to improve and strengthen the representation of the developing countries. Even after several reforms introduced over a period of 70 years, IMF has been severely criticized by developing and least developing countries majorly on four critical issues relating to dominance, governance, loan conditionality, and quota system. In response of such allegations, the IMF is continuously striving to reform its activities and governance to ensure better growth and equity, particularly to ensure that the plight of poor and developing economies is recognized.

In this context, this paper aims to (i) study the reforms introduced by the IMF over the years, (ii) analyze the key areas where reforms are still needed in the light of existing criticism directed at the IMF's functioning and governance, and (iii) suggest how the reforms could take place to address the prevailing criticism/challenges directed at the IMF relating to dominance, governance, lending, and quota system. The paper is

divided into six sections. Section 2 presents an overview of the literature. Section 3 discusses in brief the organizational structure of the IMF comprising its internal governance mechanism, capitalization, voting system, and funding facilities of the IMF. Section 4 studies the major reforms introduced by the IMF over a period of 70 years since its inception in 1944. Section 5 proceeds to point out the major criticisms directed at the IMF and the areas where reforms are still needed. Finally, Section 6 concludes with suggestions to address the major issues/criticism directed at the IMF.

2. LITERATURE REVIEW

Head (2003) evaluated the key criticisms directed at the IMF, explaining their validity, which could form the basis for further reforms in the IMF. He suggested two types of initiatives: (i) structural reforms to make IMF more accountable for its operations and (ii) substantive reforms to strengthen the IMF's role in improving the national governments' competence to handle their economic challenges. Abouharb and Cingranelli (2009) examined the effects of four lending programs supervised by the IMF, namely Stand-by Arrangements, Extended Fund Facility, Structural Adjustment Facility (SAF), and Enhanced Structural Adjustment Faility (ESAF) on the governments' respect for the overall human rights' conditions in 131 developing countries between 1981 and 2003. They used two-stage Ordinary Least Squares (OLS) model and concluded that a longer period under an IMF program worsened the government's respect for economic, social, and human rights' conditions even after reforms in program lending of the late 1990s. Their findings support criticisms directed at the IMF that are common in the case study literature.

Moschella (2011) examined the factors that cause quick and deep changes in the IMF's surveillance policy soon after the global financial crisis of 2007-2009 despite the difficulties associated with the shift toward systematic surveillance. The IMF's surveillance policy was shifted from initial bilateral to multilateral surveillance post-global financial crisis, that is, from predominant one-country focus to detect the problems in domestic policies to a more systematic approach that requires the IMF to assess whether a country's domestic policies have a negative impact not only for its own financial stability but for the international financial stability as well. The author concluded that while the global financial crisis was an important catalyst, the causes that explain the rapid and substantive shift in the scope of surveillance are the incremental accumulation of knowledge and small transformation in policy instruments and organizational practices, especially lessons drawn from the 1994 Mexican crisis and the 1997–1998 Asian crisis.

Lavigne and Schembri (2009) assessed the potential impact of the IMF surveillance reforms introduced post–global financial crisis, namely the "2007 Decision on Bilateral Surveillance over Members' Policies" and the "Statement of Surveillance Priorities" (SSP). They concluded that these reforms if implemented properly have the potential to strengthen the effectiveness of surveillance by enhancing the IMF's ability to prevent crisis and maintain a stable international financial system. Also the surveillance reforms would be more effective if they were supported by changes to the surveillance review process and by governance reforms. Cottarelli (2005) pointed out that there exists potential trade-offs between legitimacy and efficiency, particularly for an international institution like IMF. Furthermore, designing appropriate governance structures for such institution is difficult, because steps to enhance the legitimacy of such an institution through constraints on its decision-making process may affect its operational efficiency. The paper has discussed the legitimacy-efficiency trade-offs with respect to three dimensions, namely Control of political power over the operational decisions of international "technocrats"; Transparency in the IMF decision making and Uniformity of treatment across countries. The paper underscored that the trade-offs are not absolute; however, they depend on the specific ways in which legitimacy is pursued—that is, on the specific constraints that are set. Strategic reforms should, thus, aim at improving the terms of the trade-off by exploring steps that are Pareto-improving in the dimensions of legitimacy and efficiency.

3. ORGANIZATIONAL STRUCTURE OF THE IMF

3.1. Internal Governance

At the top of the organization structure is the board of governors with whom the overall authority over the Fund's activities is vested. Each member country appoints one governor who is usually the finance minister

or the head of the central bank of the member country. The board of governors has delegated the power to an executive board, which is the Fund's major decision-making body and is responsible for the operations of the IMF. It has the power to discuss and decide on all aspects ranging from financial assistance programs to administration, surveillance, etc. The executive board comprises of 24 Executive Directors, out of which member countries having the largest IMF quota, such as the United States, the United Kingdom, China, Japan, Russia, Germany, and Saudi Arabia, appoint their own representative, and the remaining Executive Directors are elected by a group of countries that are grouped into multicountry constituencies, each of which has an executive director who casts the votes of all the countries in his or her constituency. The executive board, despite of the weighted voting system, makes its decisions largely on consensus among its members (Head, 2003). A third body, the International Monetary and Financial Committee (IMFC), was established much later to oversee the work of the Fund and make recommendations to the board of governors, the executive board, and the Fund's management.

3.2. Capitalization

The funding of the IMF comes from the members' subscriptions to the IMF capital. When a country joins the IMF, it has to deposit quota subscriptions measured in terms of Special Drawing Rights (SDRs). The quota is made up of two components: 25% of the quota is in the form of gold reserves, and the remaining 75% in the form of country's home currency. The size of the quota reflects the economic and financial importance of the member country relative to other members. A country's quota determines its borrowing power and voting power in Fund's two governing bodies namely its board of governors and its executive board. Currently USA has the largest quota in the IMF by virtue of its dominant economic power in the world (Table 1). Furthermore, the IMF is also empowered to borrow funds from the private markets.

3.3. Voting in IMF

A country's quota determines its voting power within the IMF. Voting in the IMF is based upon a "weighted voting system." Each member country has 250 votes plus an additional vote for each part of its quota equivalent to one lakh SDR (i.e., one vote per one lakh SDRs). The IMF uses a quota formula to help assess a member's relative position. The current formula is a weighted average of Gross Domestic Product (GDP) (50% weight), openness (30% weight), economic variability (15%), and international reserves (5%). This formula places most of the voting power in the hands of few powerful countries namely the United States, the United Kingdom, Japan, Germany, and France, which together control 40% of the total voting power in the IMF.

3.4. Funding Facilities

The IMF extends its loan facilities through various loan instruments that are tailored to different types of balance of payments need (actual, prospective, or potential; short term or medium term) as well as the specific circumstances of its diverse membership. The IMF provides non-concessional loans through the instruments like Stand-by Arrangements (SBA), Extended Fund Facility (EFF), Supplementary Reserve Facility (SRF), and Contingent Credit Line (CCL). Apart from these facilities, low-income countries may borrow on concessional terms through facilities available under the Poverty Reduction and Growth Trust (PRGT). This facility replaced the earlier Enhanced Structural Adjustment Facility created in the year 1987. Concessional loans carry zero or low interest financing. The IMF never offers its funds in a single lump sum. Extensive drawings from the IMF require a country to agree to its imposed restrictions on its economic policies known as "IMF Conditionality." If the conditions are not met, the funds are withheld and gradual disbursements are contingent on the implementation and results of policies suggested by the IMF. Some of the conditions for structural adjustment can include austerity measures to cut down public expenditure, devaluation of currencies, liberalization of trade and investments, removing price controls and state subsidies, privatization, and improving governance among other measures.

4. SIGNIFICANT REFORMS IN IMF

Although the IMF has been persistently playing an important role in the promotion of world trade and investment, it has been severely criticized by academics, politicians, and public interest groups on the grounds

that it is dominated by the developed nations. In response to such allegations, the IMF is continuously striving to reform its activities and governance to ensure better growth and equity, particularly to ensure that the plight of poor and developing economies is recognized. Some of the reforms introduced in the IMF over the years have been described below.

4.1. Surveillance Reforms

When the IMF was created in 1944, its primary role was to stabilize the exchange rates. However, after the demise of the fixed exchange rate system in 1973, its role became that of the surveillance of overall macroeconomic policies of its member countries. Initially, the IMF's surveillance was bilateral in nature with primarily one country focus, assessing the implication of each country's policies for its own economic and financial stability. Any spill-over of these policies on other member economies was not considered. Also, financial sector issues were not properly incorporated in the surveillance reports. However, during early 1990s, increasing globalization, integration of world financial markets, and financial crisis prompted the IMF to expand the scope of its surveillance to include financial sector crisis (Moschella, 2011).

Over the years, the scope of IMF surveillance was broadened, and the annual reports prepared by the IMF staff covered many issues, including those having little direct relevance to the primary objective of the Fund, putting an enormous burden on the executive board. Furthermore, the global financial crisis of 2007–2009 mooted the discussion of further reforming the IMF surveillance to minimize the likelihood of future financial crisis. Hence, the post-global financial crisis, following reforms, was introduced in the Fund's surveillance mechanism:

1. The objective of surveillance was clearly defined as the maintenance of external stability, that is, to ensure that member country's current and capital account balances are not in extensive disequilibrium and are not vulnerable to capital flights or exchange rates. Countries should avoid such exchange rate policies that cause external instability.
2. There was a shift from bilateral to multilateral surveillance, which is a system approach involving analysis of the impact of domestic financial policies on the international spill-over effects. Multilateral surveillance aims at achieving the mutual adjustment of country's policies to ensure that exchange rate and macroeconomic policies result in national as well as international stability, avoiding any abrupt correction of disequilibrium that could impact the entire world economy.
3. Introduction of even-handed surveillance taking into consideration specific circumstances of a country.
4. Examination of countries on a common set of core macroeconomic policies favoring equal treatment.
5. Expansion of the surveillance focus beyond exchange rates to domestic macroeconomic and financial policies while limiting the scope of Fund's analysis to core policies related to external stability (Lavigne and Schembri, 2009).

4.2. Quota Reforms

A member country's quota size determines its borrowing and voting power in the IMF. Higher quota simply means more voting rights and borrowing permissions under the IMF. The "weighted average voting system" is designed in such a way that it places most of the voting power in the hands of few powerful countries namely the United States, the United Kingdom, France, Germany, and Japan. The United States itself has approximately 17% quota, which is higher than the cumulative of several developing countries. As a result, the interests of the developed countries are put above the needs of the world's poor majority. To ensure that the plight of developing countries is properly recognized, the IMF's board of governors conducts general quota reviews at regular intervals (usually every 5 years). Two main issues addressed in a general quota review are size of an overall increase and the distribution of the increase among the members. Any changes should be approved by 85% majority of the total voting power. Also, a member's quota cannot be changed without its consent.

The first resolution to increase the overall quota size was adopted in the year 1958-1959, which resulted in 60.7% overall increase in the quota. Consequently, various quota reviews such as fourth quinquennial, fifth, sixth, seventh, eighth, ninth, and eleventh general quota review resulted in overall increase in quota to

30.7, 35.4, 33.6, 50.9, 47.5, 50, and 45%, respectively (Table 2). The distribution of quota and voting shares in the IMF is highly unbalanced and inappropriately reflects a nation's relative status in the world economy. In this context, in September 2006, the IMF countries promised that they would agree on a simpler and more transparent formula for rebalancing quotas and voting rights. In September 2006 in the IMF meeting held at Singapore, the voting share of the four emerging economies namely China, Korea, Mexico, and Turkey whose actual quotas were smaller than their economic weights saw an upward adjustment in their quotas and voting shares. However, India and Brazil who opposed the September 2006 changes did not get the first round upward adjustment. Also, even after many months of negotiations, the rebalancing formula proposed under the 2008 reforms was inadequate and far from being satisfactory. Formula did not achieve the stated goals of the 2006 Singapore resolution. However, on a positive side, the 2008 quota reforms strengthened the representation of the dynamic economies, many of them being emerging countries through an ad hoc increase for 54 member countries. The voice and participation of low-income countries through a near tripling of basic votes was also enhanced.

On the other hand, some developing countries were still under-represented and developed nations were overrepresented in the IMF even after their declining share in the world's GDP after the global financial crisis of 2007–2009. Due to this discontent with the IMF, the Brazil, Russia, India, China and South Africa (BRICS) nations established a new organization called the BRICS Bank to consolidate their position in the world as BRICS nations, which account for approximately one-fifth of the total world GDP. On December 15, 2010, the board of governors of the IMF completed the 14th General Review of Quotas which involved far reaching reforms of the IMF quotas and governance. These reforms became effective on January 26, 2016. These reforms resulted in an unprecedented 100% increase in the total IMF quotas; shifted more than 6% of quota shares from over-represented countries like the United States and European Union to under-represented member countries namely India, China, Brazil, and Russia; doubled the quotas from approximately SDR 238.5 billion to SDR 477 billion; preserved the quota and voting share of the poorest member countries; increased India's voting share from 2.44 to 2.75% and china's from 3.8 to 6%; voting share of Russia and Brazil was also increased. After the 14th General Review of Quotas, four BRICS countries are now among the top 10 shareholders in the IMF.

Furthermore, the 15th General Review of Quotas will provide an opportunity to assess the appropriate size and composition of the IMF's resources and to continue the process of governance reforms. Work on the new quota formula will also continue in the next 15th General Review of Quotas to be completed by 2019 spring meeting.

4.3. Loan Conditionality

Initially, when the IMF became operational, there was no conditionality attached to the loans. It was agreed by the executive board that several goals should be negotiated to secure the revolving character of the IMF resources and the borrowing country was free to decide which instrument it will follow to achieve those goals. Import substitution and export promotion to reduce current account deficit, few monetary and fiscal policies, and increase in international reserves were some of the few popular conditions in the beginning of Fund operations (Dreher, 2002). However, over the years, the IMF loan conditions became extensive especially after the Extended Fund Facility in 1974. The policies included in the programs were not preferred by the borrowing governments on the grounds that such extensive conditions were not commensurate to the small amounts of loan provided. Also, the developing countries alleged that the IMF conditions were not specific to a country's circumstances and developed countries received loans without conditionality. Although conditionality was formally introduced during the early 1970s, the era of 1970s was characterized by loose conditionality. At that time, partly as a consequence of the oil price shock, credit from private markets was abundantly available for developing countries at low interest rates without attached conditionality.

Faced with low demand for their resources, the IMF was willing to lend at low conditionality. However, as debt problems started to emerge in some Latin American countries, the flow of private money vanished. Now, for many developing countries, the only choice to get fresh money was to accept Fund and World Bank's conditionality. Consequently, faced with rising demand for their money, the IMF started to attach more conditions to their programs. As late as the 1970s, only 26% of the IMF loan disbursements involved substantial conditionality, but the Latin American debt crisis in the 1980s and the expansion of lending to Africa increased this figure to 66% by the end of the 1980s (Stone, 2008).

In 1986, with the introduction of its SAF, another kind of condition known as the structural benchmarks was established. Noncompliance with these benchmarks might lead to more stringent actions by the Fund's staff and could result to program interruptions. Since 1987, some other conditions that gained importance were privatization and liberalization in the trade systems as well as the financial sectors. Moreover, as a consequence of the Asian crisis, the IMF faced a rising demand for its money and governments were desperate enough to agree on virtually all kind of conditions to get the required international reserves. Again, they reacted with an increase in the number of conditions. In 1997, there were, on an average, 20 conditions included in programs with Asian countries, compared with an average of 16 conditions for all countries. Owing to such large number of conditions, it became increasingly difficult for borrowing countries to identify those conditions that were crucial for further Fund support, and it was criticized that that IMF programs were anti poor. The IMF was faulted for conditionality that sought to control too many policy variables, many of which extended beyond its traditional areas of competence. Also, it was criticized that conditionality did not help and may even worsened the economic prospects. Even though the Fund tried to consider this in more recent programs, it generally failed to establish pro poor measures under its conditionality. Over time, the IMF's conditions became more numerous and criticism of the authoritarian nature of conditionality increased. The IMF continues to be criticized for applying one-size-fits-all policy prescriptions without sensitivity to context, ignoring borrowers' domestic political constraints, and promoting the interests of major shareholding governments (or their elites) at the expense of borrowing countries' needs. Sympathetic insiders and the Fund itself have conceded that conditionality may, as a consequence of these shortcomings, have been superficially implemented, requiring a shift to greater "ownership" of reform by country authorities and "streamlining" of its content. (Stone, 2008).

4.4. Special Drawing Rights Reform

SDR is an artificial international reserve, which was created by the IMF in 1970 to partially alleviate the pressure on the dollar as the central reserve currency. SDR, which is a basket currency, comprising of major individual currencies was allotted to the members of the IMF who could then use it for transactions among themselves or with the IMF. Initially, the SDR was designed to be the weighted average of those 16 currencies whose share in the world exports were more than 1% and the percentage share of each currency in the SDR was about the same as the country's share in the world exports. In 1981, the SDR was greatly simplified to comprise only five major currencies, namely the U.S. dollar, German mark, Japanese yen, British pound, and France franc. Later, the SDR comprised four major currencies, namely the U.S. dollar, euro, British pound, and Japanese yen. However, effective October 1, 2016, the IMF added the Chinese renminbi (RMB) to the basket of currencies that make up the Special Drawing Right, or SDR. Renminbi joins the U.S. dollar, euro, yen, and British pound in the SDR basket. This change represents the important milestone for IMF, SDR, and China.

5. CRITICAL EVALUATION OF THE IMF

The IMF has been in existence for more than seven decades and over the years there have been many reforms relating to its governance, surveillance, and loan conditionality to improve and strengthen the representation of the developing countries. Even after several reforms introduced over a period of 70 years, the IMF has been severely criticized by academics, politicians, and public interest groups on several grounds. Some of the criticisms directed at the IMF, which need immediate resolution are presented in the following:

(i) The IMF continues to be criticized for applying "one-size-fits-all approach" to macroeconomic policy prescriptions, ignoring the borrowing countries' political and economic constraints at the expense of their needs (Stone, 2008). The conditionality measures of the IMF attached to the loans hamper the sovereignty of the borrowing countries. It is also alleged that the tight macroeconomic policies imposed by the IMF not only fail to cure but also make their economies sicker. Such policies also create distributional inequalities and ignore the social aspects of a country's well-being. For example, in South Korea, the government had been running a budget surplus for years (it was 4% of South Korea's GDP in 1994-1996) and inflation was low at about 5%. It had

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the second strongest financial position among the Organisation for Economic Co-operation and Development (OECD) countries. Despite this, the IMF insisted on applying the same policies that it applies to countries suffering from high inflation during the 1997 crisis. As a result, the IMF sparked a recession by raising the interest rates, which led to more bankruptcies and unemployment.

(ii) The second criticism directed at the IMF is that its bailouts create a problem of moral hazard. Moral hazard arises when people behave recklessly, because they know that they will be saved if things go wrong. The IMF conditionality requires the borrowing countries to deregulate their financial markets. Such deregulations have resulted in massive cross border flow of capital investments thereby providing an opportunity for speculation. The Mexican peso crisis of 1995 was partly the result of such policies. When the bubble popped, the IMF steeped in to bail out. The IMF's bailouts provide a signal to the governments engaging in poor economic management that their bad performance will not be penalized because the IMF would come to their rescue. It also encourages investors to continue making risky-speculative bets, thereby encouraging instability of the national economies.

(iii) The IMF has been criticized on the ground that it lacks any real mechanism for accountability. The IMF works with a selected staff to make policies and design loan packages without the deep knowledge of the borrowing country. The institution has resisted calls for public scrutiny and independent evaluation. To address the issue of accountability and conduct objective and independent assessment of the issues relevant to the IMF, it introduced Independent Evaluation Office (IEO) in July 2001. Although IEO has already undertaken several evaluation projects indicating IMF's willingness to provide increased public accountability, yet IEO falls short of being an external organ. IEO is an internal organ of the IMF as the director of the IEO is appointed by the IMF's executive board and may be dismissed at any time by the executive board. Also other IEO officers are hired as per the terms and conditions of the Board (Head, 2003).

(iv) Critics argue that the IMF is a closed, nontransparent organization that operates behind the veil of secrecy. Although IMF responded to this criticism in the past by undertaking impressive projects to provide more information on its operations such as publishing information on the use of its resources, reports on IMF programs, and posting information on its website about each member's financial position in the form of quarterly financial statements. However, further improvements in the IMF are still desirable.

(v) One of the major criticisms directed at the IMF is that it better serves the interests of wealthy countries as opposed to the world's poor majority. Controlled by a handful of rich nations, the IMF is an unaccountable autocracy in which the people most affected by its operations have no or very little chance to participate (Head, 2003). Unlike a democratic system wherein each member country would have an equal vote, rich countries dominate decision making in the IMF. This is reflected in its weighted voting system where powerful countries have more voting power because they pay more into the quota system. Although the 14th General Quota Review of the IMF has increased the voting share of four developing economies namely India, China, Russia, and Brazil placing them among the top 10 IMF shareholders; however, the current formula to determine the relative position of an economy in the world is flawed and overrepresent several developed nations despite their declining share in the world's GDP especially after the global financial crisis of 2007–2009. Hence, there is an urgent need for a simpler and more transparent formula for rebalancing quotas and voting rights to truly reflect the relative position of an economy in the world. Also it is impossible to make any reforms in the current quota system as more than 85% of the total votes are required to make it happen. With approximately 16.66% of voting power with the United States, it is impossible to reform quota without the consent of the United States.

(vi) Since its inception, the European members and the United States have conspired to allow Europe to nominate the head of the IMF. Throughout the history of the Fund, its managing director has been a European. Also, the IMF board is over-represented by the European chairs who play a major role in selecting 10 of the 24 executive directors. These arrangements are obsolete and should be replaced quickly. One of the most important ways to enhance the Fund's legitimacy would be to adopt a modern, open, and transparent procedure of selecting the Managing Director to include candidates selected on merit basis without citizenship restrictions.

(vii) Few other criticisms directed at the IMF are extension of its operations into areas in which it has no real authority such as microeconomic and structural issues (like corporate governance, political governance, etc.) and asymmetry in following the loan conditionality as the rich member nations are under no pressure to follow the conditionality attached to loans provided by the IMF as opposed to the poor and developed nations.

6. RECOMMENDATIONS AND CONCLUSION

In the light of the above criticisms directed at the IMF, urgent reforms are needed on four critical issues relating to the governance, loan conditionality, quota system, and dominance. Based on the analysis of the prevailing criticism, following are the proposals or suggestions to address the same for further reforming the IMF:

- Among those advocating IMF reforms today, the top priority should be given to address its governance structure particularly the reallocation of quotas (and thus votes) as well as the composition of chairs at the IMF's executive board. Governance structure should be such that it encourages participatory democracy and ensures that every member has a voice and its vote truly reflects its weight in the world economy. This will reinforce the faith of member countries in the functioning of the IMF.
- There should be voluntarily rebalancing of quotas within the existing total, from overweight countries to the most underweight emerging markets. Although the 14th General Quota Review of the IMF has increased the voting share of four developing economies, namely India, China, Russia, and Brazil, by placing them among the top 10 IMF shareholders, the current formula to determine the relative position of an economy in the world is flawed and overrepresent several developed nations despite their declining share in the world's GDP especially after the global financial crisis of 2007–2009. Hence, there is an urgent need for a simpler and more transparent formula for rebalancing quotas and voting rights to truly reflect the relative position of an economy in the world. Basic votes should also be increased to restore the degree of equality among the members. The formula could include shares in world population as an additional variable or more weight could be given in the formula to (Purchasing Power Parity) PPP-GDP with less weight to cross-border trade. Also the variables in the formula for the variability of international transactions and for cross-border trade could be redefined and measured more appropriately.
- The composition of the executive board should be adequately representative of current economic and political conditions in the world. The present distribution of seats in the executive board in favor of Europe may have reflected relative economic and political weight in the early years of the Fund's history, but today there is a clear economic shift away from Europe to emerging market economies that puts Europe's pre-eminence at the board into doubt. As proposed by Edwin Truman, consolidation of the European Union or perhaps just the euro zone into one seat would help to increase the relative voice of the emerging and developing member countries.
- The board of governors could revise the structure of the Independent Evaluation Office to make it more independent of the IMF's executive board.
- Most of the Fund's managing directors have been effective leaders of the institution. But equally effective leaders could come from other countries, including some of the emerging-market countries. A modern, open, and more transparent procedure should be followed for selecting the Managing Director to include candidates selected on merit basis without citizenship restrictions. Guidelines adopted for the selection of MD should be properly published. Kahler recommends "a process of restrained competition" where (1) minimum qualifications are agreed upon, (2) search committees establish a qualified long-list of possible candidates, and (3) national governments narrow down the long-list to a veto-proof nomination short-list. The entire process of selecting the MD should be democratized but clearly the hesitation of the United States and the European political capitals to forgo their "privileges" remains.
- The IMF's financial involvement in low-income countries has been less than expected. Hence, it should expand its lending facilities in relation to least developing economies. Peter Evans and

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Martha Finnemore note that the combined vote of all of the 80 low-income countries that qualify for the Fund's Poverty and Growth Reduction Facility is roughly 10% whereas G10 industrialized countries have 52%. Enhancing the developing members' voice in the IMF decision making will translate into better suited IMF loan conditionality that emphasizes long-term economic growth.
- The IMF should play a more active role in information dissemination. The IMF should provide timely and uncensored information on countries' financial health. It should rank countries' financial systems, and use modern risk management techniques to evaluate the degree of fragility of different economies (Edwards, 1998)
- The IMF should not expand its surveillance into areas in which it has no real authority such as microeconomic and structural issues (like corporate governance and political governance). The IMF surveillance activities should respect the domestic social and political policies of members. IMF should be more ambitious in its surveillance of exchange rate policies of its members.
- IMF staff should be trained in political economy as well apart from being trained as macroeconomists.
- Other suggestions include encouraging transparency, openness, accountability; promoting trade liberalization and free markets; and combating corruption and nepotism.

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APPENDIX

Table 1. Quota and Voting Shares of Top 10 IMF Members.

Rank	Member country	Quota: Million SDRs	Quota (% of total)	No. of votes	% of total votes
1	The United States of America	82,994.2	17.46	831,407	16.52
2	Japan	30,820.5	6.48	309,670	6.15
3	China	30,482.9	6.41	306,294	6.09
4	Germany	26,634.4	5.60	267,809	5.32
5	France	20,155.1	4.24	203,016	4.03
6	The United Kingdom	20,155.1	4.24	203,016	4.03
7	Italy	15,070.0	3.17	152,165	3.02
8	India	13,114.4	2.76	132,609	2.64
9	Russia	12,903.7	2.71	130,502	2.59
10	Brazil	11,042.0	2.32	111,885	2.22

Source: IMF members' quotas and voting power, www.imf.org

Table 2. General Quota Review of the IMF.

Quota review	Resolution adopted	% Increase in overall quota
First Quinquennial	No increase proposed	–
Second Quinquennial	No increase proposed	–
1958/59	February and April 1959	60.7
Third Quinquennial	No increase proposed	–
Fourth Quinquennial	March 1965	30.7
Fifth General	February 1970	35.4
Sixth General	March 1976	33.6
Seventh General	December 1978	50.9
Eighth General	March 1983	47.5
Ninth General	June 1990	50.0
Tenth General	No increase proposed	–
Eleventh General	January 1998	45.0
Twelfth General	No increase proposed	–
Thirteenth General	No increase proposed	–
Fourteenth General	December 2010	100

Source: IMF quotas factsheet, www.imf.org

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Has the IMF Outlived Its Usefulness or Gone Past Its "Use-by" Date?

Imad A. Moosa*
School of Economics, Finance and Marketing, RMIT University, Melbourne, VIC, Australia.

***Correspondence:** imad.moosa@rmit.edu.au

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Abstract

Since the advent of the Asian financial crisis of the late 1990s, a debate has ensued on whether the International Monetary Fund (IMF) should be reformed, abolished, or left as is because it is performing a good and useful job. In this paper, it is argued that the IMF should be abolished because its work, particularly in developing countries, has been useless at best and harmful at worst. Several reasons, as well as examples of how IMF operations have been detrimental to the welfare of people living in countries that the IMF is supposed to help, are presented to support this proposition.

Keywords: IMF; Bretton Woods System; Financial Programming; Conditionality; Austerity.

1. INTRODUCTION

The International Monetary Fund (IMF) was established in 1944 to supervise the Bretton Woods system of fixed but adjustable exchange rates. The system collapsed in 1971 when the convertibility of the dollar into gold, a pillar of the Bretton Woods System, was abolished. With the collapse of the system, the very reason for the existence of the IMF was no longer there, which makes it plausible to suggest that the Fund should have been abolished then. However, the IMF has reinvented itself as a development agency, assuming functions that were originally assigned to the World Bank. Since then, it has been in business as usual—actually, business as more than usual as the organization has become bigger and richer. This is how Kain (2011) describes the situation:

> Undeterred by the total disappearance of its purpose, the IMF—flush with continuing streams of subsidies, especially from American taxpayers—morphed into a "development" agency. The quotation marks around "development" are no mistake. There's no evidence that the IMF's efforts as a development agency have had any positive effects, unless by "positive effects" you include creating among many poor countries a culture of dependency upon foreign "aid," along with propping up authoritarian regimes.

Similarly, Friedman (1998) argued that "the IMF lost its only function and should have closed shop." Kain (2011) cites Leland Yeager as saying that "self-important international bureaucracies have institutional incentives to invent new functions for themselves, to expand, and to keep client countries dependent on their aid" (Yeager, 1998). He goes on to say that "the IMF is a tired old dinosaur of an institution, wholly under the thumb of European bureaucrats while largely reliant on U.S. tax dollars" and that "its mission seems to be little more than paving the way for international corporations entrance into various developing nations." He seems to accept the view that the IMF is an oppressor of Third World countries when he says that "the nations at the receiving end of the IMF's largesse are quickly placed under the iron thumb of the lender nations."

Naturally, the views expressed by Kain, Yeager, and Friedman are not shared by the IMF staff, and some observers believe that the IMF is still performing a good and useful job by boosting growth, dealing with financial crises, providing advice on economic and financial matters, and the provision of loans for countries short of liquidity. However, the facts and figures show that IMF operations are invariably detrimental to the health of the countries where it operates. The IMF's critics refer to inappropriate or dogmatic policy design (Babb and Carruthers, 2008; Babb and Kentikelenis, 2017; Kentikelenis et al., 2016; Stiglitz, 2002), adverse

effects on the economy (Dreher, 2006), negative social consequences (Abouharb and Cingranelli, 2007; Babb, 2005; Oberdabernig, 2013), and adverse effect on social spending, particularly government expenditure on health (Huber et al., 2008; Stubbs et al., 2017).

The objective of this paper is to highlight the aspects of this debate. Three different views are evaluated: (i) the IMF should be maintained because it is performing a good job, (ii) the IMF should be reformed, and (iii) it should be abolished, not only because the reason for which it was established no longer exists but also because its operations invariably hurt the countries where it operates.

2. THE TRANSFORMATION OF THE IMF

Following the Great Depression and World War II, there was a desire to create a new international monetary system that would serve the objectives of dealing with balance-of-payments problems, stabilizing exchange rates, and discouraging the 1930s-style "beggar-thy-neighbor" trade policies that involved competitive devaluation. Member countries should declare par values for their currencies in terms of the U.S. dollar, which was tied to gold at the fixed price of $35 an ounce. Exchange rates were allowed to move by one percentage point above or below the declared par values. However, currency devaluation was allowed for countries experiencing chronic or fundamental balance of payments deficits, only after consultation with, and approval by, the Fund.

For the purpose of granting loans to deficit countries, the IMF uses an "analytical framework" known as "financial programming," based on the work of Polak (1957). The underlying model is used to determine the amount of the loan and the macroeconomic adjustments essential to re-establish equilibrium. The macroeconomic adjustments are intended to reduce imports and boost exports to enable the deficit country to earn sufficient foreign exchange to meet its international obligations, including the newly incurred IMF debt. IMF loans, therefore, come at the price of "conditionality," the policy adjustments prescribed by the IMF as a precondition for granting the loan as outlined in a confidential "letter of intent." Conditionality typically involves tax hikes, monetary contraction, and cuts in government spending, the type of policies associated with painful austerity. With the passage of time, more intrusive measures were introduced as part of the conditionality package.

The Bretton Woods system suffered from a fundamental problem pertaining to the adjustment mechanism (of the balance of payments). Multilateral trade and currency convertibility require a real adjustment mechanism, something the system lacked. Governments had to demonstrate the existence of a fundamental disequilibrium in the balance of payments before they could adjust their exchange rates. The adjustable-peg system lacked the stability, certainty, and automaticity of the gold standard and the flexibility of the free-floating system. Another problem is that speculation can be extremely destabilizing because of the possibility of changing the fixed rates. When a currency is under pressure, it can only be devalued, by motivating speculators to sell it. An important loophole in the system was the defects in the liquidity creation mechanism. To avoid a liquidity shortage, the United States should run a balance of payments deficit, thus undermining confidence in the dollar. To avoid speculation against the dollar, the deficit must shrink, which would create a liquidity shortage. Consequently, it was a vicious circle.

By the late 1960s, central banks with abundant dollar balances saw gold at $35 an ounce as an irresistible bargain and began to exchange dollars for gold. On August 15, 1971, President Richard Nixon abolished the convertibility of the dollar into gold, and countries were given the right to choose the exchange rate regimes deemed appropriate for the underlying country. The collapse of the system, which the IMF was entrusted with the task of supervising, led the IMF to reinvent itself. According to Kain (2011), "the IMF skillfully used a series of global economic crises to increase its capital base and financing activities"—these crises include the oil crisis of the 1970s, the debt crisis of the 1980s, transformation of the former communist countries in the early 1990s, and the Mexican, East Asian, and Russian financial crises in the mid to late 1990s. With the upgraded status of the IMF, more intrusive policies, including the adoption of free-market policies, removal of subsidies, privatization of public assets, abolition of price controls and interest-rate ceilings, deregulation, reducing tariffs, eliminating quotas, removing export barriers, and maintaining adequate international reserves, were imposed on borrowing countries.

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Joseph Stiglitz, Nobel Prize winner and a former World Bank chief economist, was fired from the Bank in 1999 for questioning the Word Bank and IMF Policies. In an interview with Greg Palast, he outlines the IMF operations as follows (Gauding, 2011). The first step is the privatization of public resources, which he calls "briberization." According to Stiglitz, national leaders are required to sell off their electricity and water companies "with the promise of 10% commissions paid to their Swiss bank accounts if they are able to shave a few billion off the sale price of national assets" (that is, kickbacks). The second step is market deregulation, thereby causing what he calls the "hot money cycle," in the sense that "cash comes in for speculation in real estate and currency, then flees at the first sign of trouble, which drains a nation's reserves in days, hours." Step three is the elimination of subsidies to citizens, thereby causing the prices of food and fuel to increase and leading to what he calls "the IMF riot." Step four is the imposition of free trade agreements, according to the rules of the World Trade Organization (WTO) for the benefit of the multinationals. There is no wonder then that Salsman (1998) describes the IMF as a "destructive, crisis-generating global welfare agency."

Anderson (2005) argues that the Asian financial crisis of the late 1990s set the stage for the first genuine debate over the role of the IMF. Most analysts agree that IMF-prescribed policies to liberalize capital and financial markets in East Asia in the early 1990s aggravated the crisis at the very least. After rapid capital flight plunged Asian countries into an economic tailspin, the IMF imposed harsh economic measures on some countries that arguably made the impact of the crisis even more severe.

3. ARGUMENTS AGAINST ABOLISHING THE IMF

The opponents of the proposition calling for abolishing the IMF are of two types: (i) those who think that the IMF is performing a good and useful job, thereby helping countries in need; and (ii) those who believe that "reform" is what the IMF requires. Naturally, those who believe that the Fund has been performing a magnificent job include the staff of the Fund as this is an act of self-preservation—what has been termed as the desire to maintain jobs that pay tax-free, inflation-proof salaries. According to Anderson (2005), "the U.S. Treasury Department, arguably the principal influence on IMF policies, has offered a modest reform proposal that lacks a clear vision for change." Apart from the Fund itself, the U.S. Treasury Department has been the most enthusiastic advocate of the IMF, which is not surprising.

Most of the arguments put forward in favor of the Fund are mere rhetoric and counterfactual propositions. For example, the International Monetary Fund should not be abolished because the positive effects of its operations considerably outweigh any negative "side" effects. Another example is that the IMF serves the function of improving growth and boosting international trade. Yet another argument is that it is important to maintain the IMF because it serves a good purpose and does considerable work worldwide by helping out when there are global crises or potential global issues. One more argument in favor of the Fund is that it provides loans on a short-term basis to all countries with payment imbalances to balance them and works to enhance the economies of member countries. In a symposium about whether or not the IMF is obsolete, almost everyone expressed the opinion that all that is essential is some modification (International Economy, 2007). Examples are Ken Rogoff who said that "the IMF thrives by reinventing itself," Edwin Truman who declared that "we need a leaner and meaner IMF with a different kind of staff," Alan Meltzer, who suggested that "the IMF has lost a clear sense of purpose and must reorganize," and Jeffrey Frankel who expressed the view that the IMF is essential because "success in dealing with the China currency issue requires international cooperation and multilateral surveillance."

Those who put forward these views do not say anything about the human suffering caused by the conditionality associated with the loans and the IMF-ignited riots that erupt every time the Fund imposes austerity measures on poor countries. Reality is the exact opposite to what is suggested by the IMF enthusiasts as we have been moving from one crisis to a bigger one on the way to the age of dismal growth. What is important is not that the IMF thrives but that the countries it is supposed to help thrive, which has not been happening. If an international body has lost a clear sense of purpose and the reason for its establishment in the first place disappeared, then the solution is not to reorganize or making it leaner but to abolish it. It is bizarre to suggest that the IMF must exist so that China can be forced not to exercise its sovereign right of adopting the exchange rate regime it deems appropriate for its economy, which is what IMF rules dictate.

Anderson (2005) talks about the recommendations of the International Financial Institutions Advisory Commission, typically referred to as the Meltzer Commission, which was created as part of the 1998 legislation that increased the IMF's financial resources. The Commission's majority report calls for the IMF to be scaled back to serve only as a lender of last resort to solvent member governments facing liquidity crises. It would eliminate the IMF's power to impose conditions on developing countries in return for long-term assistance. However, it would still require that countries meet a list of rigid, free market-oriented preconditions in order to be eligible for short-term crisis assistance. Following the March 2000 release of the Commission's report, the then U.S. Treasury Secretary, Lawrence Summers, firmly denounced it, arguing that, if implemented, it would "profoundly undermine the capacity of the IMF…and thus weaken the international financial institutions' capacity to promote central U.S. interests." Summers even released his own proposal, which was not intended to change the status quo. According to Summers, the IMF is "among the most effective and cost-efficient means available to advance U.S. priorities worldwide." Commenting on the Fund's response to the 1997-98 Asian financial crisis, Summers claimed that without the IMF, "the crisis would have been deeper and more protracted, with more devastating impact on the affected economies and potentially much more severe consequences for U.S. farmers, workers, and businesses." This is a truly remarkable confession, which makes Summers honest in admitting that he defends the IMF because it serves U.S. interests.

There are also those who hold the view that if it is not feasible to abolish the IMF, big changes must be introduced. For example, Barro (2000) believes that the IMF's role in the collection and distribution of data has been useful and that an advisory role might also be satisfactory. However, Barro is more in favor of abolition as he argues that this function could be performed just as well by nongovernmental institutions. He also believes that the demand for the IMF's economic advice is likely to be low if it is no longer tied to its loans. We will see later that the IMF's advice brought havoc on the countries going by the advice as a condition for getting loans. Who wants this type of advice when even the countries that had to follow the advice found it tantalizing to get out of it?

4. ARGUMENTS FOR ABOLISHING THE IMF

Advocates of the elimination of the IMF come from both the right and the left of the political spectrum. Those on the right think that the IMF is a waste of public funds in an age when private capital flows to the developing world have dramatically increased and that IMF bailouts eliminate discipline (with respect to risk taking) in private markets. On the left, there are those who argue that the abolition of the IMF would, among other things, create more space for developing countries to pursue alternative economic policies that do not conform with the IMF's free market prescriptions. Let us consider the following arguments for abolishing the IMF.

4.1. Benefits for Borrowing Countries

Hanke (2000) argues that "the IMF's policies don't generate prosperity or alleviate poverty." Gauding (2011) suggests that the general public holds the vague idea that the IMF is a force for good, helping Third World countries with loans and other assistance to improve their economies. In reality, he argues, the IMF is the "prime cause of increased poverty and suffering around the globe." The IMF is out there to benefit bankers and multinationals by giving them access to markets and would-be-privatized public assets in the countries that are unlucky enough to get "help" from the Fund.

Khan (1990), who was for a long time a senior member of the Fund's staff, conducts a comprehensive assessment of the impact of IMF policies on macroeconomic variables such as the current account, inflation, and growth. After reviewing 13 studies covering the Fund's activities from 1963 to 1982, he concludes that (i) there is frequently an improvement in the balance of payments and the current account, although a number of studies show no effects of programs; (ii) inflation is generally not affected by programs; and (iii) the effects on the growth rate are uncertain. Johnson and Schaefer (1997) examine the relation between IMF loans and economic growth in less-developed countries from 1965 through 1995 and find that 48 of the 89 loan recipients were not better off in 1995 (as measured by real per capita wealth) than before they accepted their first loan, that 32 of those 48 countries were poorer, and that 14 of the 32 countries had economies that

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were at least 15% smaller than what they were before their first loan. For example, between 1968 and 1995, Nicaragua received $185 million from the IMF, yet its economy contracted 55% whereas Zaire received $1.8 billion between 1972 and 1995, and its economy contracted 54%. Therefore, the empirical evidence supports the proposition put forward by Hanke (2000) and Gauding (2011).

4.2. Long-Term IMF Dependency

Bandow (1994) examined the Fund's financing activities from 1947 through 1989 and found that six countries relied on IMF assistance for more than 30 years, 24 countries for 20-29 years, and 47 countries for 10-19 years. Among the 83 developing countries that used IMF resources for at least 60% of the years since they started borrowing, more than half have relied on the IMF every year. Bird (1995) concludes that "the image of the Fund coming into a country, offering swift financial support, helping to turn the balance of payments around, and then getting out, is purely and simply wrong." In effect, the Fund becomes something similar to a colonial force.

Ben-Ami (2011) argues that the IMF helps absolve politicians of their responsibility. One reason why politicians frequently opt for IMF bailouts in times of trouble is that it provides them with a way of evading responsibility for their actions. They can claim that austerity is imposed by an external institution, which they accept reluctantly for fear of losing access to the Fund's resources. Furthermore, corrupt politicians typically benefit from the work of the IMF at the expense of starving population. The abolition of the IMF would make the culpability of corrupt politicians more transparent.

4.3. Moral Hazard

The IMF's implicit guarantee of subsidized bailouts reduces the cost of fiscally irresponsible, yet rewarding policies that encourage even greater recklessness. This constitutes moral hazard, which was evident in July 1998 when Russia promised to implement key economic policies in exchange for an $11.2 billion IMF loan commitment. The Yeltsin government abandoned its commitments, devalued the ruble, defaulted on its debt, began printing money excessively, fired almost every reformer in the government, and failed to enact many of the promised reforms. However, Yeltsin was the darling of the "West," which is why IMF loans to Russia were pushed by the Clinton State Department. The same story goes for the 1995 IMF bailout of investors in Mexico.

4.4. Inappropriate Loan Conditions

IMF policy prescriptions are typically "off-the-shelf" remedies that are not adequately tailored to each country's unique circumstances—these conditions typically prolong and deepen financial crises. For example, the IMF failed to recognize that the East Asian crisis was a banking crisis, not a fiscal crisis, which made its traditional prescriptions inappropriate and exacerbated the problem. Hanke (1998) summarizes the debacle as follows:

> The International Monetary Fund failed to anticipate Asia's financial crisis. Then, to add insult to injury, the IMF misdiagnosed the patient's malady and prescribed the wrong medicine. Not surprisingly, the patient's condition has gone from bad to worse. Perhaps it is best, therefore, that governments seldom honor the terms of their loan agreements.

Gauding (2011) tells a story of how the IMF caused starvation in Malawi as presented by Johann Hari. During the 1990s, Malawi was experiencing severe economic problems owing to a terrible HIV-AIDS epidemic and a horrific dictatorship. When the Malawi government requested help, the IMF demanded the imposition of a "structural adjustment program." As a result, the government was told to sell off everything publically owned to private companies and speculators and to put an end to subsidies. Particularly, devastating was the abolition of fertilizer subsidies, even though those subsidies made it possible for farmers (who made up most of the population) to grow food in the country's depleted soil. Furthermore, the IMF demanded that available funds should be used to repay international bankers rather than help the Malawian people. In 2001, when the IMF found out that the Malawian government had built large stockpiles of grain in case of a crop failure, the government was ordered to sell those stockpiles to private companies so that the proceeds could be used to pay an IMF recommended loan from a large bank, a loan that carried a 56%

annual interest. In the following year, the crops failed, causing a starvation—yet, the IMF suspended $47 million in aid, because the government was not enacting free market adjustments fast enough.

In 2005, in the height of the starvation and economic wreckage caused by the IMF, Malawi ignored the Fund's instructions and re-introduced fertilizer subsidies, along with a range of other services to ordinary people. Subsequently, Malawi was not only able to feed its population, but it also began to provide food aid to Uganda and Zimbabwe. In her article, "Ending famine simply by ignoring the Experts," Dugger (2007) wrote the following:

> This year, a nation that has perennially extended a begging bowl to the world is instead feeding its hungry neighbors. It is selling more corn to the World Food Program of the United Nations than any other country in southern Africa and is exporting hundreds of thousands of tons of corn to Zimbabwe.

There is more where this came from. In Kenya, one of the countries worst affected by AIDS, the IMF insisted on the introduction of fees to see doctors, thus exacerbating the epidemic. In Ghana, the IMF insisted on the introduction of school fees, exacerbating illiteracy. In Zambia, the IMF insisted on slashing health spending, hence the number of babies who died doubled. All of this happened while those countries were required to keep foreign bankers and multinationals happy.

4.5. Conditionality Compliance and Enforcement

It is impossible for outsiders to monitor conditionality compliance routinely because loan terms and data are confidential and released only voluntarily. Edwards (1989) examined the degree of compliance by using the Fund's own data, looking at the compliance rate for 34 programs that were approved in 1983 in response to the debt crisis. He found that the median compliance rate with IMF loan conditions between 1983 and 1985 was only 46%. The compliance rate for government deficit never reached this level once and was 19% in 1984. Meanwhile, the median compliance rate for targets pertaining to the current account, inflation, and economic growth was only 41%. Sachs (1989) concludes that "the evidence presented in the IMF's 1988 review of conditionality … suggests that, since 1983, the rate of compliance has been decreasing sharply, down to less than one-third compliance with program performance criteria in the most recent years."

4.6. Discrimination and Opacity

Ben-Ami (2011) argues that "the IMF has functioned more like a medieval court than a modern organization." Owing to a long-standing agreement among "Western" countries, the IMF is typically headed by a European, while the World Bank is headed by an American. The appointees, according to Ben-Ami (2011), "have never been chosen by merit" and "will be chosen in a backroom deal between a few top politicians rather than going through a transparent or democratic process." Barro (2000) describes the appointment of the IMF's managing director as a "circus-like process." This is what he says in this respect:

> After a lengthy public debate, the leading countries settled on another German, Horst Köhler, to replace Michel Camdessus as the IMF's managing director. Unfortunately, the circus-like process began to resemble an affirmative-action procedure when it became clear that a particular nationality-German-was a prerequisite for the job.

Unfortunately, Barro's alternative to the "circus-like process" and "affirmative-action procedure" would have been to appoint Stanley Fischer, who was the deputy managing director at the time. Three years later, it was Stanley Fischer who insisted on privatization and the removal of subsidies in occupied Iraq. However, one has to be fair and acknowledge the fact that Barro is in favor of abolishing the Fund as he expressed his unfavorable opinion of the IMF's social value and his surprise that the Meltzer Commission did not advocate the abolition of the IMF.

Furthermore, the way the IMF is set up provides the United States a veto on any action of which it disapproves because it holds a big voting power. The prescribed policies are frequently discriminatory against developing countries—for example, the IMF granted rich countries considerable leeway to pursue fiscal stimulus in the aftermath of the global financial crisis, but immediate austerity was prescribed as a solution

to the Asian crisis of the late 1990s. Gauding (2011) argues that the IMF is "inconsistent," because it supports huge state-funded bank bail-outs in the rich world, while demanding an end to almost all state funding in the poor world.

4.7. Short-Termism

The IMF policies are characterized by short-termism, preferring short-term financial stability over long-term growth. This is one reason why the post-crisis world economy has been characterized by weak growth, with little attempt to address the problem. Ben-Ami (2011) argues that IMF bailout programs are aimed at rescuing troubled financial institutions, under the notorious pretext of too big to fail, rather than helping national economies return to growth. In a sense, the IMF programs resemble what Ben-Ami (2011) describes as a "kind of institutional welfare programme."

4.8. Interference in Domestic Politics

Hanke (2000) suggests that "the International Monetary Fund interferes too much in the domestic politics of the countries it seeks to assist." As an example, he tells the story of President Suharto who was not a popular man with the IMF or the Clinton Administration. When he wanted to stabilize the rupiah by establishing a currency board (on advice from Hanke), the IMF and the Administration mounted a massive counterattack, pressuring the Indonesian government to back off the board idea. On his retirement, a former IMF managing director, Michel Camdessus, boasted that "we created the conditions that obliged President Suharto to leave his job." In other words, Hanke argues, "they caused considerable human suffering in the course of trying to accomplish a political goal."

4.9. Depressing Effect on Social Expenditure

According to Rowden (2009), the IMF follows the "deadly ideas of neoliberalism," thus undermining public health. Stubbs et al. (2017) collected archival documents on IMF programs from 1995 to 2014 to identify the pathways and impact of conditionality on government health spending in 16 West African countries. Based on a qualitative analysis of the data, they found that IMF policies reduce fiscal space for investment in health, limit staff expansion of doctors and nurses, and lead to budget execution challenges in health systems. Overall, their findings suggest that IMF conditionality impedes progress toward the attainment of universal health coverage. Huber et al. (2008) declare at the very beginning that they expect the presence of an IMF agreement to be associated with lower levels of both social security/welfare and health/education expenditures. They obtain negative association with social security and welfare spending, which reduces the ability of people to pay for private healthcare. This issue is dealt with in detail by Moosa (2017).

5. CONCLUDING REMARKS

The IMF has inflicted significant damage on, and caused considerable misery to, the people of the countries it is supposed to be helping. In addition to the stories of Malawi and other countries mentioned earlier, the story of Iraq following the U.S.-led invasion and occupation of the country is more remarkable. Precisely similar to the case of Suharto's Indonesia, the IMF rejected a proposal to go for a currency board to put an end to hyperinflation and insisted on managed floating, which the Central Bank of Iraq was not familiar with. Even worse, the IMF delegation insisted on privatization (including the oil sector) and the removal of subsidies (for example, by charging market prices for petrol). That was the recommended recipe for a country under occupation and years of embargo. These events were witnessed by this author when he was an advisor to the U.S. Treasury in Baghdad in May-June 2003 (see, for example, Moosa, 2004). For the IMF, what matters is not the welfare of the masses but the financial interests of a few oligarchs. Certainly, the IMF should be abolished.

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The Consequences of IMF Conditionality for Government Expenditure on Health

Nisreen Moosa*
School of Commerce, University of South Australia, Adelaide, SA, Australia.

***Correspondence:** nisreen.moosa@mymail.unisa.edu.au

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Abstract

The International Monetary Fund (IMF) was established in 1944 to supervise the international monetary system that collapsed in 1971. Since then, the Fund has reinvented itself as some sort of a "development agency," providing loans with strings attached. Any country that wishes to obtain loans must follow the IMF-prescribed policies that reflect the neoliberal ideas of the Washington Consensus. As these policies are typically contractionary and involve austerity, the IMF has been accused of pursuing policies that exhibit a negative impact on health expenditure, with dire consequences for the population. Although the empirical evidence on this issue is mixed, it is well known that the IMF operations are more likely to exert a negative effect than a positive effect on government spending on health.

Keywords: IMF; Health Expenditure; Conditionality; Washington Consensus; Structural Adjustment.

1. INTRODUCTION

The International Monetary Fund (IMF) was established in 1944 as a constituent component of the Bretton Woods agreement to act as a supervisor of the international monetary system of fixed exchange rates. The Fund was entrusted with the task of helping (developed) countries suffering from balance of payments difficulties by providing loans and allowing currency devaluation only if the underlying country could demonstrate that it had a chronic deficit. Since the collapse of the Bretton Woods system in 1971, the Fund reinvented itself by acting as some sort of a development agency and an adviser on economic and financial stability. Its operations were extended to cover the developing world, which was at one time the jurisdiction of the World Bank. The operations of the IMF include the provision of loans, but these loans are not without strings attached—strings that come with the conditionality that involves measures of "reform." The conditionality clauses invariably include austerity measures to depress aggregate demand, including the removal of subsidies and the imposition of higher taxes. These policies have frequently led to popular revolt and austerity protests, taking the form of large collective actions that include political demonstrations, general strikes, and riots triggered by grievances over the policies of economic liberalization urged by the IMF. The policies may involve the reduction of government subsidies and/or higher prices of basic staples such as food, water, and domestic gas. Typically, the demonstrators demand lower prices, restored government subsidies, and wage increases to compensate for higher prices, or jobs (for example, the 1977 "bread riots" in Egypt as the IMF policies caused a quadrupling of bread prices).

These so-called "reforms" have adverse consequences for the well-being of people, including public spending on health, which takes a direct hit as a result of fiscal tightening and the retrenchment of social services. The IMF has been criticized severely for the conditionality associated with its operations. For example, Stiglitz (2002) refers to Thailand's "AIDS increase as a result of IMF-forced cutbacks in health expenditures," which the Director of the External Relations Department of the IMF responded to by accusing Stiglitz of dishonesty, claiming instead that its policies have led to higher levels of health spending (Dawson, 2003). The debate has been bipolar, as the IMF, its staff, and few supporters claim that a positive effect can be observed running from the IMF-prescribed policies to health care. For example, a study by the Fund staff reveals that the IMF's policies have a positive and significant effect on public health spending in low-income countries

(for example, Clements et al., 2013). The empirical evidence is mixed, but every study that involves IMF staff somehow detects positive effect running from IMF policies to public health expenditure.

The objective of this paper is to demonstrate that the nature of conditionality and the parameters that govern the operations of the IMF are more likely to be associated with a decline rather than a rise in health expenditure. The debate on this issue will be evaluated. Although the evidence is mixed, it will be argued that empirical research on this issue is motivated by the desire to support preconceived beliefs, and that self-preservation and ideology provide an explanation as to why studies involving IMF staff produce supportive evidence for the Fund's operations.

2. CONDITIONALITY, STRUCTURAL ADJUSTMENT, AND HEALTH SPENDING

The term "conditionality" refers to a set of "reforms" that borrowing countries must implement in order to obtain IMF loans, including reduction in public spending, currency devaluation (presumably to encourage exports), and changes to monetary policy (Toye,1994). In the mid-1980s, new and highly intrusive measures were introduced under the umbrella of the so-called "structural adjustment policies" (Woods, 2006), including privatization of state-owned enterprises and the liberalization of trade and finance (Summers and Pritchett, 1993; Toye, 1994). In this sense, the IMF has been acting for the benefit of multinationals and against the people of the countries it is supposed to help. In a sense, the IMF has been the conduit for the implementation of the neoliberal ideas envisaged by the Washington Consensus in countries around the world. Nooruddin and Simmons (2009) think that it is not a surprise that the increase in openness in the developing world corresponds closely with the increasing importance of the Washington Consensus. Moreover, they describe the consensus as follows: "the set of policies that often constituted the conditions countries were to follow to receive aid, an important component of which was lowering barriers to import competition."

This proposition is supported by Williamson (1990) who refers to a consensus (read the Washington Consensus) between governments and international financial agencies on general philosophy and the number of adjustment policies to be taken. Williamson suggests that the consensus is based on the three premises that policies should be market-friendly, outward-oriented, and macroeconomically stable. A typical policy package comprises 10 policy prescriptions including (i) fiscal discipline, (ii) reduction of general subsidies to finance human resources and infrastructure, (iii) tax reform, (iv) financial liberalization, (v) unified and competitive exchange rates, (vi) trade liberalization, (vii) abolishing barriers to foreign direct investment, (viii) privatization, (ix) deregulation, and (x) property rights. A country that does not meet the conditionality clauses will be deprived of IMF loans, which will in turn limit its access to development aid and international capital markets.

The IMF proposes three channels through which its programs are linked to strengthening of health systems. The first is that IMF-prescribed policies enhance economic growth and boost the tax revenues, thereby allowing governments to invest in public health (Clements et al., 2013; Crivelli and Gupta, 2016). Second, social spending floors shelter sensitive expenditures from austerity measures (Gupta, 2010; Gupta et al., 2000; IMF, 2015). Third, the implementation of the IMF's policy advice is conducive to foreign aid and investment (Clements et al., 2013; IEO, 2007). In contrast, the critics contend that adequate investment in health is hampered by pressure to meet rigid fiscal deficit targets and because funds are diverted away from the health sector to repay debt or boost reserves (Kentikelenis, 2015; Kentikelenis et al., 2015a, 2015b, 2016; Ooms and Schrecker, 2005; Stuckler and Basu, 2009; Stuckler et al., 2008, 2011). If, as the evidence indicates, the IMF-prescribed policies depress economic growth, the resources available to fund healthcare shrink (Barro and Lee, 2005; Dreher, 2006; Przeworski and Vreeland, 2000). Furthermore, these policies are not conducive to the attraction of health aid (Stubbs et al., 2016).

The IMF policies have both direct and indirect consequences for health expenditure, which can be construed to be positive and negative, depending on who is expressing the underlying view. The first of the positive direct effects, as mentioned earlier, is that the IMF operations are subject to conditions designed to protect social expenditures from the adverse consequences of adjustment policies (Gupta et al., 2000). In response, Kentikelenis et al. (2015b) argue that spending targets are frequently expressed as shares of gross domestic product (GDP), and as the IMF policies cause economic contraction, total expenditure declines.

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Furthermore, the extent to which these conditions are implemented and the importance the Fund provides to monitor them have been questioned (Goldsborough, 2007; Kentikelenis et al., 2014; Oxfam, 1995).

It is also claimed that the IMF policies frequently go beyond spending conditionality to foster a more active reshaping of the health sector, including the enhancement of the role of the private sector in healthcare provision (Benson, 2001; Gupta et al., 2000; Loewenson, 1995; Turshen, 1999), the introduction of cost-sharing for the use of health services (IEO, 2003; Pitt, 1993; Sen and Koivusalo, 1998), and decentralizing health services (Kentikelenis et al., 2014). Kentikelenis et al. (2015b) argue that while it is possible that public revenue generated from patients or hospital privatization may be reinvested in the health system (thus raising spending), the proceeds may be diverted to other areas of spending. The enhancement of the role of the private sector can hardly be a substitute for public health expenditure as private health care is beyond the means of the vast majority of people, particularly in low-income countries. Even in rich countries such as the United States, people die either because they do not have a private health cover or because they are denied a specific form of treatment for one reason or another. This is probably the reason why we frequently hear the terms "medical refugees" and "dental refugees" in reference to Americans seeking treatment in Mexico. The same criticism applies to the introduction of cost-sharing for the use of health services and the decentralization of health services.

Furthermore, it is claimed (on behalf of the IMF) that public health expenditure is subject to the "resource effect" arising from the low interest credit provided under its programs. The additional resources, as the argument goes, could be used to boost expenditure to meet health priorities. However, it is unlikely that this effect will materialize because the extra resources will be used to repay external debt (Gould, 2003). In addition, it is argued, on behalf of the Fund, that the IMF operations give the underlying country a "stamp of approval," which boosts aid flows (Clements et al., 2013). Although there is some evidence for the link between foreign aid and Fund programs (Bird and Rowlands, 2007), it is not necessarily the case that those funds will be directed to health (Rowden, 2009b; Stuckler et al., 2011) or that they will be channeled through the government (Lu et al., 2010; Sridhar and Woods, 2010).

The indirect effects of the IMF-prescribed policies are the unintended consequences of structural adjustment. To start with, the Fund's conservative projections, which form the basis of conditionality, frequently leave little space for fiscal maneuverability (de Renzio, 2005; Goldsborough, 2007; Kentikelenis et al., 2014; Rowden, 2009b). The IMF operations invariably involve the imposition of limits on the wage bill of the public sector, which can drive public health expenditure downwards, given that much of public health spending in low-income countries goes toward the payment of the salaries of doctors and nurses (Van der Gaag and Barham, 1998). Furthermore, currency devaluation and the removal of subsidies are bound to make medicine and medical technology more expensive and hence less available to the vast majority of people (Musgrove, 1987; Van der Gaag and Barham, 1998). The IMF policies typically involve the privatization of public assets, including hospitals. Even if the proceeds are reinvested in the health sector (which is not necessarily the case), this will only be a short-run phenomenon that will benefit private healthcare providers. It does not make sense to sell a public hospital and then use the proceeds to subsidize the cost of private health care—in any case, the IMF hates anything called "subsidies."

Although the IMF always claims that its programs strengthen health systems (Clements et al., 2013; Gupta, 2010, 2015), it has long been criticized for impeding the development of public health systems (Baker, 2010; Benson, 2001; Goldsborough, 2007; Kentikelenis et al., 2015a, 2015b; 2016; Stuckler and Basu, 2009; Stuckler et al., 2008, 2011). For example, a recent qualitative analysis of IMF programs in Guinea, Liberia, and Sierra Leone found that the IMF contributed to the failure of health systems to develop, thereby exacerbating the Ebola crisis (Kentikelenis et al., 2015a). The recent experience shows that the IMF's policy advice is associated with fewer public health resources, difficulties in hiring and retaining health workers, and unsuccessful health sector reforms. Van der Hoeven and Stewart (1993) suggest that "neither the IMF nor the World Bank recognized the need to take any special actions to protect the poor."

3. THE DEBATE

The debate between the IMF and its critics with respect to health care can be viewed clearly in an interview with two fund officials, followed by a criticism from Rowden (2009a), a reply from the IMF, and then another

reply from Rowden. There is also the exchange between Stubbs et al. (2017b) and Gupta (2017) who wrote in response to Stubbs et al. (2017a). The IMF defended its position with respect to issues related to health and social policy in an interview conducted by Glenn Gottselig (2009) with Sanjeev Gupta (Deputy Director of the IMF's Fiscal Affairs Department) and Catherine Pattillo (Advisor in the Strategy, Policy and Review Department). In this interview, the IMF officials were asked directly whether or not governments with IMF-supported programs are pressed to reduce social spending to meet prescribed economic targets. Gupta responded by declaring that "IMF-supported programs have been very flexible by accommodating larger fiscal deficits and higher inflation, and by continuing to protect priority social expenditures" and that "the programs have placed considerable emphasis on strengthening social protection for the most vulnerable." He attributed constraints on health expenditure to "administrative capacity constraints," rather than excessively tight macroeconomic policies—specifically, he mentioned "poor national coordination," "shortcomings in the health care system," and "absorptive capacity." If these factors mean anything at all, they are bound to be affected by tight policies designed primarily to meet debt repayment and boost creditworthiness, albeit at the expense of starving people.

When asked if IMF-supported policies require countries to cut spending on social programs so that inflation can be contained, Pattillo answered in the negative, arguing that "in a number of crisis-affected countries, programs were also flexible in adapting high inflation targets as food and fuel prices increased." Gupta then rejected the proposition that social spending in general, and health spending in particular, have declined in countries with IMF-supported programs, arguing that "the IMF's Independent Evaluation Office did not find any evidence of a decline in social spending in IMF-supported programs." He referred to the IMF studies showing that social spending—including health and education spending—has increased by 0.6% of GDP relative to preprogram levels and that spending increases have been higher for education, at 0.35% of GDP compared to health at 0.25%. These numbers conceal the unpleasant truth that these programs are contractionary, and when GDP shrinks, the level of health expenditure per capita declines in turn. Then a big question mark must be put on the word "independent" in the name of a body that is a constituent part of the IMF.

Another issue that was raised in the interview was whether or not the IMF's policies deter countries from using available donor aid for health spending and whether or not the IMF's position on aid intended for the health sector is diverted to repay domestic debt or boost reserves. Gupta responded by suggesting that "IMF-supported programs play an important role in mobilizing donor support around country-owned poverty reduction strategies" and referred to an IMF study concluding that social spending (including spending on health and education) in 51 countries was generally unaffected by aid flows during the period 1990-2004. It is not surprising at all that studies conducted by the IMF produce results that tell us what a wonderful job the IMF has been performing.

When confronted with the proposition that IMF programs typically involve public sector wage-bill ceilings, which are bound to have a negative impact on health expenditure, Gupta responded by saying that "IMF program conditionality has never included any wage-bill ceilings, or hiring freezes for that matter, specifically on the health sector." However, he added that "a new policy on wage ceilings was put into effect in July 2007" under which "ceilings can be used only in exceptional circumstances where they are crucial for macroeconomic stability, and should be of limited duration, periodically reassessed, and sufficiently flexible to accommodate spending of scaled-up aid in priority social sectors." For the designers and implementers of the IMF programs, all circumstances are exceptional and macroeconomic "stability," which is achieved by economic contraction, is always the primary objective. Moreover, even if wage-bill ceilings do not exist, governments adopting austerity measures are bound to impose these ceilings.

In response to this interview, Rowden (2009a) raised several points as to why the IMF is likely to reduce spending on health, which triggered a response and a response to the response. In particular, he asserts that "the IMF is not a development organization per se, but acts to ensure that sovereign debt payments are made on time to external lenders and that creditworthiness is maintained," which means that "its short-term priority for borrowers to generate increased exports and earn foreign exchange which may be used to repay creditors." He suggested that "by looking to the IMF for its assessment of the adequacy or 'soundness' of a recipient country's macroeconomic policies before giving out foreign aid each year, bilateral and multilateral aid donors have wrongly afforded tremendous leverage and power to the IMF." The "soundness" of macroeconomic policy typically means keeping inflation in check, which is inconsistent with currency devaluation that leads to imported inflation.

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The IMF is an ideologically driven organization, adopting the neoliberal ideas of *laissez faire* and the Washington Consensus. Rowden (2009a) refers to the IMF's "ideological disposition that prioritizes short-term financial sector variables in macroeconomic policy to the subordination or neglect of real sector variables, such as long-term developmental goals, industrialization, higher employment or increased public investment," arguing that "such a position is associated with the school of monetarism within neoclassical economics." It is these types of policies that induce a long-term trend of low-growth, low-employment and low-public investment that has been characterized by chronically insufficient health budgets and dilapidated health infrastructure.

Typically, the IMF-imposed macroeconomic targets include an annual inflation rate at or below 5-7% per year and to keep budget deficits below 3% of GDP. The restrictiveness of these policies, according to Rowden (2009a), "undermines the ability of domestic industries to generate higher levels of productive capacity, employment, and GDP output—and thus, tax revenues—than otherwise could be the case under more expansionary fiscal and monetary policy options." As a result, the government is deprived of higher levels of tax revenue for recurrent expenditures and for long-term public investment as a percent of GDP. A report published by the General Accountability Office (2001) on IMF loans suggests that "policies that are overly concerned with macroeconomic stability may turn out to be too austere, lowering economic growth from its optimal level and impeding progress on poverty reduction." Similarly, Pollin and Zhu (2006) contend that "there is no justification for inflation-targeting policies as they are currently being practiced throughout the middle- and low-income countries." The Center for Global Development (2007) found that "the empirical evidence does not justify pushing inflation to these levels in low-income countries." On November 14, 2007, the House Financial Services Committee of the U.S. Congress sent a letter to the Managing Director of the IMF, expressing concern about "the IMF's adherence to overly-rigid macroeconomic targets," suggesting that "it is particularly troubling to us that the IMF's policy positions do not reflect any consensus view among economists on appropriate inflation targets" (Financial Services Committee, 2007). It is true that high inflation can be damaging for investment and growth, but how high is high? Controlling inflation should be looked upon in terms of costs and benefits. Rowden (2009a) refers to the "empirically unjustifiable tight fiscal and monetary targets in non-transparent meetings with central bank and finance officials behind closed doors."

Gupta and Pattillo replied to Rowden (2009a) by identifying three principal criticisms that require a response: (i) IMF policies keep budget deficit targets below 3% of GDP; (ii) the IMF has very little empirical evidence to justify pushing inflation down to the 5-7% level, and (iii) the IMF's policies for borrowing countries are primarily designed for achieving short-term priorities, which could be in conflict with longer-term successful economic development strategies or health goals. On the first point they respond by citing some IMF reports claiming that "the evidence does not support the view that IMF-supported programs adopt a one-size-fits-all approach to fiscal adjustment" and that "there was no evidence that IMF-supported programs were overly tight." As far as point (ii) is concerned, they pick selective evidence to claim that 5% is the beginning of the inflation-related death zone, without mentioning what costs are involved. For point (iii) they claim that the statement is false because "Fund-supported programs are framed in the context of a medium-term macroeconomic framework that incorporates longer-term development objectives." Ironically, they claim that "the objective of IMF-supported programs is to promote high and sustained growth, which will improve the well-being of the poor and create fiscal space for increasing priority spending, including on health." Tell that to the people of Egypt who revolted violently against the IMF programs in 1977.

Rowden (2009a) replies by referring to biased sampling covering the period 1993-2001 (well after deficit targets had already been dramatically lowered under the original IMF stabilization loans of the 1980s) and suggests that the results would be different if the sample went back to 1980. Furthermore, he suggests that Gupta and Patillo do not address a central concern—the fall in public investment as a percent of GDP, neither do they explain how and under what conditions the targets may be raised. Furthermore, Rowden notes that Gupta and Pattillo do not address the concerns raised in a number of studies, including Government Accountability Office (2001), Pollin and Zhu (2006), Center for Global Development (2007), and the letter to IMF from the Financial Services Committee (2007).

Another exchange was initiated by Stuckler et al. (2011) who suggest that "IMF macro-economic policies, which specifically advise governments to divert aid to reserves to cope with aid volatility and keep government spending low, could be causing the displacement of health aid." They attempt to determine

whether aid displacement was greater when countries undertook a new borrowing program from the IMF between 1996 and 2006 and conclude that "health system spending grew at about half the speed when countries were exposed to the IMF than when they were not." Glassman (2011) comes to the rescue of the IMF by describing as a "controversial conclusion" (of Stuckler et al.) that IMF policies could be causing the displacement of health aid and showing her dislike to the fact that this article was picked up by The Guardian (2011). In particular, she argues on the basis of econometric grounds by suggesting that "the paper fails to document the econometric strategy used to reach their conclusion" and that "comparisons of health spending in countries with and without programs are subject to statistical biases in different directions, which are again influenced by the same factors that affected a country's decision to enter an IMF-supported program in the first place."

In a comment on Glassman's defence of the IMF, Rowden attributes the observation that various studies have inconsistently found differences or no differences between IMF program and non-IMF program countries to "the ideological biases that underpin them," arguing that "many current finance ministry and central bank officials who have gone to school in the last 20-30 years have largely been taught one thing—and one thing only—that the only 'prudent' and 'sound' option for fiscal and monetary policies is the very conservative one favoured by the Reagan and Thatcher governments steeped in the school of monetarism within neoclassical economics." According to this line of thinking, all other viable options have subsequently been dismissed as "imprudent" and "unsound." Rowden concludes that "it should not matter if a country has an IMF program or not, as its fiscal and monetary policies are likely subject to the same sharp right-wing turn taken in the economics profession 30 years ago, from which it has yet to recover." This means that IMF-like policies may be implemented, on ideological grounds, without the IMF demanding that.

In another comment on Glassman's piece, a commentator (who was unimpressed by Glassman lecturing everyone on the difference between causation and correlation) likens the IMF's role of a lender of last resort to the behavior of colonial powers in the 17th-19th centuries. During that period, whenever a country in Latin America, the Middle East, North Africa, and Southeast Asia defaulted on its debt, the creditors (almost always the British, French or Dutch) would typically invade the country, take over their public finances, and devote them to paying down the debt, regardless of the consequences for public health (and everything else, for that matter). When or if the debt was paid off, the creditors would either set up a permanent colonial administration, or a loyal, dependent client state.

4. THE EMPIRICAL EVIDENCE

Few studies examine empirically the relation between structural adjustment and health expenditure. Some of these studies are based on descriptive statistics only, including van der Hoeven and Stewart (1993), Thiesen (1994), van der Gaag and Barham (1998), and Gupta et al. (1998, 2000). Two of these studies found increasing expenditure on health, using as the dependent variable either the share of GDP or the share of total government expenditure. By using a sample of 118 developing and transition countries, Gupta et al. (1998) find that since the mid-1980s real per capita spending on education and health has increased, on average, in developing countries but decreased in the transition economies. They observe comparable increases in countries that had IMF-supported adjustment programs during the same period despite the fiscal consolidation often required by those programs.

Other studies employ formal econometric modeling, including the use of ARIMA models, OLS, the generalized method of moments, and Prais-Winsten regression (Clements et al., 2013; Huber et al., 2008; IEO, 2003; Kentikelenis et al., 2015b; Nooruddin and Simmons, 2006; Stubbs et al., 2017a). Four of these studies found an unambiguous result of increase in health expenditure, while two show mixed results of increase for some countries and decrease in others. Interestingly, among the 10 studies employing summary statistics or formal modeling, the four that show unambiguous increase in health expenditure involve staff of the IMF or other international financial institutions. The IMF has claimed that its programs enhance government spending for health, and that a number of innovations have been introduced to enable borrowing countries to protect health spending from broader austerity measures (Kentikelenis et al., 2015b). This is the risk of combining preconceived ideas or the urge to provide supportive evidence for a claim by using (dodgy) econometrics. Let us examine some of these studies.

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Kentikelenis et al. (2015b) investigate the effects of Fund programs on government health expenditures in low-income countries using data for the period 1985-2009. They find that Fund programs are associated with higher health expenditure only in Sub-Saharan African countries, which historically spent less than any other region. This relation turns negative in other low-income countries. They argue that examining the link between IMF programs and public health spending provides partial accounts of how health outcomes are affected because different economic and structural adjustment policies can impact population health in various ways.

A study conducted by the Independent Evaluation Office of the IMF (IEO, 2003) addresses the following question: What is the impact of the presence of an IMF-supported program on the level of social spending (other factors being held constant) relative to a situation without a program? The study attempts to determine what happens to public sector social spending under IMF-supported programs using a broad sample of 146 countries in the 1985-2000 period. Four different indicators were used for each type of spending: as a share of GDP, as a share of total government spending, and as an index of real spending at domestic prices and in U.S. dollars per capita. The empirical results reveal that, on average, the presence of an IMF-supported program does not reduce social spending and that the presence of a program is associated with increased public spending in health and education measured as either a share of GDP, total spending, or in real terms compared with a situation without a program. However, they find the positive effects attributable to the program to be short-lived—for these effects to be durable, they would have to be followed by further policy actions in these sectors beyond the program period.

Nooruddin and Simmons (2006) argue that a central component of the IMF's programs is reducing government budget deficits. Hence, they wonder how domestic political considerations shape the distribution of cuts made by governments participating in IMF programs. Their central finding is that the role played by domestic politics shrinks as a result of participation in IMF programs. Although democracies allocate larger shares of their budgets to public services in the absence of IMF programs, the difference between democracies and non-democracies disappears under IMF programs.

Huber et al. (2008) declare at the very beginning that they expect the presence of an IMF agreement to be associated with lower levels of both social security/welfare and health/education expenditures. They use a dummy variable to indicate obligations to the IMF in a given year—the variable takes the value of 1 for each year a country has repurchase obligations with the IMF and 0 for each year it does not, cumulative since 1970. The coefficient on this variable turns out to be significantly positive, implying a higher level of health expenditure in association with IMF programs. However, it is not clear why they obtain negative association with social security and welfare spending. This in itself reduces the ability of people to pay for private health care.

Clements et al. (2013) find that education and health spending has increased during IMF-supported programs at a faster pace than in developing countries as a whole. The analysis is based on the most comprehensive data set assembled thus far for this purpose, with data covering 1985-2009 for 140 countries. Controlling for other determinants of education and health spending (including macroeconomic conditions), the results confirm that IMF-supported programs have a positive and significant effect on social spending in low-income countries. Over a 5-year period with IMF-supported programs, spending on health increased by about 1% of GDP. IMF-supported programs are in addition associated with increases in the share of government spending allocated to education and health.

Stubbs et al. (2017a) argue that the most important international institution setting the fiscal priorities of low-income countries is the IMF. They collect archival documents on IMF programs from 1995 to 2014 to identify the pathways and impact of conditionality on government health spending in 16 West African countries. Based on a qualitative analysis of the data, they find that IMF-prescribed policies reduce the potential for investment in health, put a limit on the numbers of doctors and nurses, and lead to budget execution challenges in health systems. Furthermore, they use cross-national fixed-effect models while adjusting for confounding economic and demographic factors and for selection bias. Their results reveal that IMF conditionality impedes progress toward the attainment of universal health coverage.

In his response to Stubbs et al. (2017a), who tried to draw a causal link between IMF programs and government health expenditure, Gupta (2017) raises several broad methodological issues: drawing causal inferences from qualitative methods, addressing endogeneity when the counterfactual is almost never observed

in reality, and interpreting findings from qualitative and quantitative methods. Specifically, Gupta raises the following questions: (i) is the qualitative method adopted by the article suitable for drawing causal inferences?, (ii) are all potential pathways covered by the qualitative method adequately and transparently?, (iii) are endogeneity issues addressed adequately?; (iv) are the findings from qualitative and quantitative methods interpreted accurately?, and (v) are the findings of the article consistent with those of the literature? Thus, he declares the following: (i) the qualitative method is based on a systematic search of document archive, the nature of the description in these documents suggests that the findings from the qualitative methods are mostly selective and anecdotal; (ii) there are other important pathways that the qualitative methods may have failed to identify with the list of key words used in the document search; (iii) addressing the endogeneity problem, otherwise the wrong conclusion may be drawn; (iv) the interpretation of the findings from the quantitative analysis appears to be incomplete and may lead to misunderstanding; and (v) it is important for the article to cast its findings in terms of the relevant literature that has studied the impact of IMF programs on public health spending in developing countries. He concludes that "while the proposed new methodology by the authors represents an improvement, the results derived from it are inaccurate and misleading." Stubbs et al. (2017b) reply meticulously to Gupta and conclude that that structural adjustment programs should be judged by their effects on the human condition. They argue that "in an era of global uncertainty and important challenges to international organizations, the IMF could best address criticism by reforming its practices, thereby living up to its own standards on social protection, rather than continuing to deny evidence."

It seems, therefore, that the evidence on whether the IMF-sponsored programs have a positive or negative impact on health expenditure is mixed. However, it is quite evident that somehow, the studies conducted by the IMF's staff or supporters show unequivocally that the IMF has performed a wonderful job in promoting health expenditure, which is counterintuitive, to say the least. These results are engineered for the purpose of self-preservation. Let us not forget that the IMF should have been abolished in 1971, when the original purpose for its establishment was no longer there.

5. CONCLUSION

The problem with the empirical studies of the relation between health expenditure and IMF-prescribed policies is that they depend on regression equations that contain a large number of explanatory variables representing empirical models that have no corresponding theoretical models. This methodology, predominantly based on cross-sectional and panel data, produces results that are highly sensitive to the selected set of explanatory variables, model specification, and variable measurement. It is this problem that prompted Edward Leamer's article "Let us Take the Con out of Econometrics" (Leamer, 1983). The Leamer critique revolves around the proposition that a regression model with a large number of potential explanatory variables can be used to prove almost anything and produce results (after extensive data mining) that support prior beliefs. For example, Moosa (2012, 2017) demonstrates that the same data set can be used to show that either of the two theories of capital structure is superior to the other, simply by changing the set of explanatory variables.

With respect to the issue under consideration in this paper, the proponents of either of the two views (that is IMF operations are good or bad for health expenditure) have produced contrasting evidence. Unfortunately, empirical work in economics and finance has been all about proving prior beliefs, which can be easily performed by playing around with model specification, variable definitions and measurement, and estimation methods. This is why a trend has emerged recently to deal with the sensitivity of the results with respect to variations in the model. However, if we combine the empirical results with common sense, intuition, and what happens on the ground, we will reach the conclusion that the IMF operations depress health expenditure. After all, the IMF is not a development agency—it is out there to allow multinationals to acquire public assets without paying considerably in the countries where it operates and to make sure that those countries pay their debt. The last thing the IMF cares about is the health and well-being of the people in those countries. After all, and as Rowden (2009b) puts it, the IMF follows the "deadly ideas of neoliberalism," thus undermining public health.

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IMF, BIS, and World Bank: On the Intra-institutional Articulation of the International Financial System

Maria de Fatima Silva do Carmo Previdelli*, Luiz Eduardo Simões de Souza
Economic Science Department, Post Graduation Program on Social and Economic Development, Universidade Federal do Maranhao, Brazil.

***Correspondence:** fatprevi@gmail.com

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Abstract

The international financial system could be organized into three groups. According to this classification, the first group includes the organizations that exercise the functions of regulation and supervision. In the second, we have those that are regulated and supervised by the former, and in the third, we find the organizations that do not follow such rules or supervision, forming the so-called shadow banking system. This article seeks to examine the first group, and, more specifically, how the International Monetary Fund articulates with the primary elements of such a group.

Keywords: International economy; International Monetary Fund; International financial system; Bank for International Settlements; World Bank.

1. INTRODUCTION

The current configuration of the international financial system (IFS) can be classified into three groups of organizations. In the first group, we can include those that exercise functions of regulation and supervision. In the second group, we can include the ones that are regulated and supervised by the former. In the third, we find the organizations that do not follow such rules or supervision, also known as the shadow banking system. In our view, this configuration of the international financial system reflects a characteristic of its evolution from capitalism to the most recent stage, known in a broader sense as financial globalization (Hirst *et al.*, 2009).

At the same time, the structure of the International Financial System and its functioning carry an apparent contradiction between expansionist vision and widespread competition. This contradiction would be inherent to capitalism itself, as an economic system.

Therefore, this paper aims to examine how the International Monetary Fund fits in and relates to the primary members of the first group—that of the regulatory organizations—because, in order to think about IMF reform, it is essential to examine their interrelation with the other representatives of such a group and their joint objectives. This is justified because, in order to verify how the IMF can play a new role in the face of the challenges of an increasingly interconnected and interdependent international scenario, the actions that such an organization has in the financial system as a whole cannot be ignored. Thus, in order to make some sort of change, one should first identify the objectives of the group of regulators as a whole.

In order to attain such goal, this article is organized into four parts. In addition to this introduction, we have the first section, which presents the contradiction inherent in capitalism, which, in our view, extends to the structuring of the financial market, in any scope. A second section describes the current configuration of the international financial system. A third part sets out the history of the major organizations involved, their objectives, structure, and who the decision makers are in each of them. Next, the articulations of these organizations with the IMF are analyzed. Some considerations are made at the end of this paper, through conclusion.

2. FREE TRADE AND COMPETITION IN CAPITALISM AND THE FINANCIAL SYSTEM

The contradiction between the ideology of free trade and the real conditions of capitalist competition has been evidenced in economic theory since the mid-nineteenth century and finds its primary critical points in David Ricardo, Karl Marx, and Friedrich Engels.

Ricardo in his *Principles of Economic Policy and Taxation* (1817) initiates, through an interesting critique of the Smithian vision of infinite expansion of markets, the formulation of the "law of diminishing returns." This would serve as a subsidy to the theory of neoclassical production, presented by Alfred Marshall in *Principles of Economics* (1891), which is adopted to the present day in the mainstream of economic theory, one way or another.

The exposition of the law of diminishing returns did not prevent Ricardo from making free market apology along the lines of classical laissez-faire liberalism, extending an inverse relationship between cost and income, what Marshall would later call "opportunity cost." This extension would be the rationale of the Theory of Comparative Advantages of Foreign Trade, the theorem so questioned in theory, as used as the foundation for economic policies. In any case, it is reiterated that Ricardo was the first in the history of economic thought to formulate the law of diminishing returns as a consequence of the expansion ad infinitum of production and of market forces.

Friedrich Engels, in his 1841 *Umrisse einer Kritik der politischen Ökonomie (Outlines of a Critique of Political Economy)*, is, in turn, the first to effectively check the collaborative character of international trade, classifying it as the "stylized war" between nations. The recognition of the capitalist expansion worldwide with a historical process, not as an extension of wealth and opportunity but as a fierce competition between companies in search of the monopoly situation, was often achieved in the form of oligopolistic agreements, centralization, and concentration of the capital.

Karl Marx's critical analysis of Capitalism, in *The Capital* of 1867, most clearly exposed this antinomy. The discourse of the free market, of free competition, would not find real effect in the face of the cumulative need of the cycle of capital between money and commodity, or even in its usurious or abbreviated form (the form M-M′, in which M′ > M). The expansion of productive social relations of capitalism would thus lead to concentration and centralization, which implies the pauperization of the workers for the enrichment of the owners of the productive methods, in stamental, organizational, and even geographical (territorial) terms.

This configuration of the dynamics of capitalism would pass through not only by its organizations—in terms of the constitution of the economic environment and its effective rules—but also by the directives of its related organizations. Thus, it is not difficult to deduce that between the free-trade discourse and the cumulative need of the members of the "bureau of bourgeois interests," organizations linked to the structuring and regulation of an international financial system would adopt the second path, as a real goal for the routing of their actions. The contributions of Rudolf Hilferding (1910) and Vladimir Ilitch Lenin (1917) on the extension of capitalism at its simplest stage complement the earlier formulations of Marx and Engels.

After the "golden age" (Hobsbawm, 1995), in the early 1970s, the articulation between national states and markets reached a point where the shifting of the former toward internationalization and financialization of the latter went from an objective necessity to reality, in what was called the globalization of capital. In this sense, organizations created in the "era of catastrophe" (Hobsbawm, 1995) have fulfilled the role of promoting, through their related organizations, precisely this scouring of national states through the coordination and integration of local financial markets. The ultimate purpose of these organizations is to seek not to perpetuate the accumulation of usurious capital, in spite of the implications of the law of diminishing returns, by promoting the movements of centralization and concentration characteristic of capitalism in any of its historical phases.

In this manner, the apparent contradiction between the free-trade ideology and the real conditions of capitalist competition occurs only insofar as its discourse of its practice is not dissociated. Thus, both commercial companies and international financial system organizations should not be observed from their "mission" or manifest proposal, but from their effective action, which is to ensure continuously increasing returns to capital, in margin and scale, or, in more direct terms, the perpetuation of capital accumulation.

3. THE INTERNATIONAL FINANCIAL SYSTEM

The international financial system (IFS) can be conceived as the space that allows the relations of exchange or business between currencies, activities, monetary and financial flows, loans, payments, and international financial investments between companies, banks, central banks, governments, or international organizations (Persaud, 2012, 219).

Thus, organizations that regulate such a space should, in the first place, facilitate international trade and investment but, above all, guarantee the necessary stability for the transit of capital, both productive and speculative.

However, in order for the aforementioned objective to be achieved, there is a need for well-defined rules and adjustment criteria, accepted by all agents, private or public, who negotiate in it. Thus, we are going to start from the end of World War II to see how the attempts to create a regulated space were made, emphasizing, however, that some organizations that would become part of the regulatory group, existed even before the 1940s.

After World War II, state representatives began to worry about the needs of a more stable international business environment. Fear of a new international crisis along the lines of that of the 1930s led the newly victorious national states of the war to seek regulatory measures for the financial system of the period. The objective was to achieve full employment and the stability of international prices, while at the same time, allowing for an external balance without restraining international trade. Many believed that if there was a new crisis on a global scale, domestic measures would no longer be sufficient. Therefore, it was necessary to create organizations and rules of behavior that would strengthen the power of rulers also at the international level. The domestic prosperity of each country would thus be attained. Therefore, international cooperation would help countries to achieve their external balance and financial stability without sacrificing their internal objectives (Gonçalves, 1997, 279-286).

Thus, in 1944, representatives of 44 countries met in Bretton Woods to plan and sign the articles of the agreement that won the same name of the locality. The agreed system required fixed exchange rates against the U.S. dollar, and a constant dollar gold price of $35 per ounce. Member countries had to maintain their international reserves largely in the form of gold or dollar assets and had the right to sell dollars to the Federal Reserve in exchange for gold at the official price. It was therefore a gold-exchange standard, with the dollar as the primary reserve currency, because the floating exchange rate in the period was considered highly detrimental to the progress of international trade (Krugman and Obstfeld, 2005, 408-414).

This agreement was unilaterally disrupted in 1973 as a result of the increase in the international mobility of capital in previous years. Such increase was due to the recovery of financial markets and the increase in international transactions that made it difficult to isolate transactions in current and capital accounts. The maintenance of parity required high intervention levels in the foreign exchange markets and led to doubts about how to intervene based on the confidence of a given government to be able to eliminate the imbalances in its balance of payments (Eichengreen, 2002, 183-185).

The 1970s were characterized not only by floating exchange rates and high inflation, but also by the rapid growth of international financial markets and of cross-border money flows. As a result, financial stability issues came once again to the fore and in 1974, the collapse of Bankhaus Herstatt in Germany and of Franklin National Bank in the United States highlighted the lack of efficient banking supervision of banks' international activities, and prompted the Group of Ten (G10) central bank governors to create the Basel Committee on Banking Supervision (BCBS) under the Bank for International Settlements (BIS).

Furthermore, the Latin American debt crisis of 1982 highlighted the danger of undercapitalized banks being overexposed to sovereign risk and justified a new form of free markets operating under regulation and supervision of supranational organizations (BIS, 2017).

The execution of the international aid to the countries in debt were mainly performed by the International Monetary Fund (IMF) but followed the decisions of the above-mentioned group. From the 1970 decade onward, after the Jamaica Agreement in January 1976, the decisions of any action that would affect the IFS were to be discussed first by the G10 and the Board of Central Bank Governors (BCBG) at BIS as well as IMF. Consequently, it becomes essential to examine some of the characteristics of the primary organizations acting in the supervisory and regulatory role of IFS.

4. MAIN IFS REGULATORY ORGANIZATIONS

The international financial system comprises three groups of organizations. In the first group are those that regulate and supervise the functioning of the system. Moreover, this is the focus of our article, as it is in this group that the IMF is inserted. Most of such organizations have a supranational role. In the second group,

we have regulated institutions, which, in general, have an area of activity linked to national spaces. Finally, in the third group, we have the shadow banking system that includes those who do not have to follow the determinations of the first group.

We next examine some of the history, the structure, and characteristics of operation of the primary organizations of the first group by order of date of foundation, in order to verify the common points between such organizations.

4.1. Bank for International Settlements

The Bank for International Settlements (BIS) was established in 1930 by the Hague Agreements, in Basel, Switzerland. It was created in the context of the Young Plan,[1] adopted on January 20, 1930 at the Hague Conference. BIS replaced the Agent General for Reparations and assumed the role of managing the collection, administration, and distribution of the annuities payable as reparations. The Bank's name is derived from this initial role. In addition, the BIS was appointed as agent to the trustees and trustee, respectively, for the German government international loans of 1924 and 1930 (the so-called Dawes and Young Loans issued to help finance reparations). In execution of the Young Plan, the BIS reinvested part of the Young Loan proceeds in German bonds (Backer, 2002).

The names behind the foundation of BIS were Charles G. Dawes,[2] Owen D. Young,[3] and Hjalmar Schacht.[4] Moreover, the funds that allowed its functioning were provided by the central banks of Belgium, France, Germany, Italy, Japan, and Great Britain and three private banks in the United States: J.P. Morgan & Company, First National Bank of New York, and the First National Bank of Chicago. The central bank of each country subscribed to 16,000 shares, and the three private American banks had 16,000 shares each. Thus, the American representation in the BIS was three times greater than that of any other country. (Lebor, 2014)

As a consequence of the Great Depression of the 1930s, the reparations issue quickly faded, and the German financial and banking crisis of the summer of 1931 led first to a one-year moratorium on reparation payments (Hoover Moratorium of July 1931) and subsequently to their complete cancellation (Lausanne Agreement of July 1932). With the reparations issue out of the way, the BIS focused its activities on the technical cooperation between central banks (including reserve management, foreign exchange transactions, international postal payments, gold deposit, and swap facilities) and on providing a forum for regular meetings of central bank governors and officials. The BIS board consisted of the governors and their alternates of the National Bank of Belgium, the Bank of France, the German Reichsbank, the Bank of Italy, the Netherlands Bank, the Swedish Riksbank, the Swiss National Bank, and the Bank of England, as well as representatives for the Bank of Japan (Lebor, 2014).

After the end of World War II, according to the BIS official homepage (www.bis.org), during the Bretton Woods Conference it was decided to abolish the BIS "at the earliest possible moment," because it was considered that the BIS would have no useful role to play once the newly created World Bank and International Monetary Fund were operational. European central bankers held a different opinion, and

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[1] The Young Plan was intended to deal with the question of reparation payments imposed on Germany (and to a lesser extent on other central European countries) by the Treaty of Versailles following the end of the First World War.

[2] Charles G. Dawes was director of the US Department of the Budget in 1921 and served on the Allies Reparation Commission from 1923. His later work on "Stabilization of the German Economy" secured him the Nobel Prize in 1925. After being elected vice president to President Calvin Coolidge from 1925-1929 and appointed ambassador to England in 1931, he returned to his personal banking career in 1932 as chairman of the board of directors of the City National Bank and Trust in Chicago, where he remained until his death in 1951.

[3] Owen D. Young was an American industrialist. He founded the RCA (Radio Corporation of America) in 1919 and was its president until 1933. He also served as President of General Electric from 1922 until 1939. In 1932, Young sought nomination as presidential candidate for the Democratic Party but lost to Franklin Delano Roosevelt.

[4] Hjalmar Schacht was a German economist, banker, center-right politician, and cofounder in 1918 of the German Democratic Party. He served as the currency commissioner and president of the Reichsbank under the Weimar Republic and served in Hitler's government as president of the Reichsbank (1933-1939) and minister of economics (August 1934-November 1937). As such, Schacht played a key role in implementing the policies attributed to Hitler (Backer, 2002).

successfully lobbied for maintaining the BIS. By early 1948, the liquidation resolution had been put aside, and it was agreed that the BIS would focus foremost on European monetary and financial matters (BIS, 2017).

As a matter of fact, the BIS board meetings resumed in December 1946, and the priority was in stabilizing the different European national currencies before trade and foreign exchange restrictions could be gradually lifted. As a result, in September 1950, 18 European countries set up a European Payments Union (EPU) and appointed the BIS as its agent. The primary goal of the EPU was to restore the free convertibility of European currencies in line with the Bretton Woods agreements. To achieve this, each country reported its bilateral trade deficits or surpluses with each of the other participating countries to the BIS on a monthly basis where the aggregate deficit or surplus of each country was then calculated as part of the EPU as a whole. At first, these deficits and surpluses did not have to be settled immediately, but were instead largely converted into debits and credits within the EPU. With time, the ratio of debits and credits granted by the EPU was gradually reduced until the end of 1958, when it was dissolved (BIS, 2017).

With the signature of the Rome Treaties in 1958 and the starting process of creating the European Economic Community, BIS continued its role as a mentor for the countries of Europe who had signed such treaties. Therefore, both The European Monetary Cooperation Fund (EMCF, 1973) and the European Monetary System (EMS, 1979) were operated from Basel, with the BIS acting as technical support. In 1988-1989 the Committee for the Study of Economic and Monetary Union, chaired by Jacques Delors, was once again based in Basel where the technical groundwork for the European Council's decision to move toward full European monetary union was also provided by BIS and was approved in the 1992 Treaty of Maastricht. With the implementation of the first phase of the monetary union process at the end of 1993, the Committee of Governors was replaced by the European Monetary Institute (EMI), and moved from Basel to Frankfurt where, in 1997, the EMI became the European Central Bank (ECB, 2017).

In the 1970s, the Group of Ten (G10) also created the Basel Committee on Banking Supervision (BCBS) as a committee of banking supervisory authorities of the central bank governors of the Group of Ten countries in order to provide a forum for regular cooperation on banking supervisory matters. In the next decades, the Basel Committee issued the Basel Capital Accord, introducing a credit risk measurement framework for internationally active banks that became a globally accepted standard. This capital accord was further refined in the Basel II (2004) and Basel III (2010) frameworks with the goal to increase control and transparent measurement of the various risks incurred by internationally active banks, limiting the possibility of contagion in case of a crisis within the IFS (Lebor, 2012).

Besides the Basel Committee, there are other BIS-based committees such as the Markets Committee (since 1964), the Committee on the Global Financial System (CGFS, since 1971), and the Committee on Payment and Market Infrastructures (CPMI, since 1990—until 2014 the Committee on Payment and Settlement Systems).

Nowadays, BIS states that its mission is "*(...) to serve central banks in their pursuit of monetary and financial stability, to foster international cooperation in those areas and to act as a bank for central banks*." Regarding the way of its operation, it states as follows:

> BIS pursues its mission by: fostering discussion and facilitating collaboration among central banks; supporting dialogue with other authorities that are responsible for promoting financial stability; carrying out research and policy analysis on issues of relevance for monetary and financial stability; acting as a prime counter party for central banks in their financial transactions; and serving as an agent or trustee in connection with international financial operations. (BIS, 2017)

Owing to the 2007-2008 financial and banking crisis, the structure of BIS was modified in order to gain more speed in the decisions that were taken so that, at the present moment, the main structures and groups working at BIS are the board of directors, and the main committees are the Basel Committee on Banking Supervision (BCBS), the Committee on the Global Financial System (BGFS), the Committee on Payment and Settlement Systems, and the Central Bank Governance Forum (BIS, 2017).

According to the BIS official page (http://www.bis.org/about/board.htm), the board of directors meets every two months and may have up to 21 members, including six ex officio directors, comprising the central bank governors of Belgium, France, Germany, Italy, the United Kingdom, and the United States. Each

ex officio member may appoint another member of the same nationality. Nine governors of other member central banks may be elected to the board. The board of directors elects a chairman and may elect a vice chairman from among its members—each for a three-year term. In addition, BIS is part of several other organizations such as the Financial Stability Board (FSB), the International Association of Insurance Supervisors (IAIS), and the International Association of Deposit Insurers (IADI).

4.2. International Monetary Fund

The International Monetary Fund (IMF) was conceived in July 1944, at the meeting of Bretton Woods, in the United States of America and came into formal existence in December 1945, when its first 29 member countries signed its Articles of Agreement and began operations on March 1, 1947. The IMF's primary mission was to ensure the stability of the international monetary system, by operating mainly in the system of exchange rates and international payments. In order to maintain stability and prevent crises in the international monetary system, the IMF monitors member country policies as well as national, regional, and global economic and financial developments (IMF, 2010).

According to its official web page, every country that joins the IMF accepts the obligation to subject its economic and financial policies to the scrutiny of the organization and the international community. The IMF's mandate is to oversee the international monetary system and monitor economic and financial developments in and the policies of its 189 member countries. In order to perform that, the surveillance process assesses whether domestic policies promote countries' own stability by examining risks they might pose to domestic and balance of payments stability and IMF technicians' advises on policy adjustments and propose policies' alternatives when the countries' decisions could affect global stability (de Vries, 1986).

By the early 1960s, the U.S. dollar's fixed value against gold, under the Bretton Woods system of fixed exchange rates, was observed as overvalued. A sizable increase in domestic spending on President Lyndon Johnson's Great Society programs and an increase in military spending caused by the Vietnam War gradually worsened the overvaluation of the dollar. The system dissolved between 1968 and 1973. In August 1971, U.S. President Richard Nixon announced the "temporary" suspension of the dollar's convertibility into gold. Although the dollar had struggled throughout most of the 1960s within the parity established at Bretton Woods, this crisis marked the breakdown of the system. An attempt to revive the fixed exchange rates failed. Moreover, by March 1973, the major currencies began to float against each other (IMF, 2010).

Since the collapse of the Bretton Woods system, the countries that were IMF members were free to select any form of exchange arrangement they wish, which allowed the currency to float freely, pegging it to another currency or a basket of currencies, adopting the currency of another country, participating in a currency bloc, or forming part of a monetary union (IMF, 2010).

As part of the first amendment to its articles of agreement in 1969, the IMF developed new reserve instruments called special drawing rights (SDRs), which could be held by central banks and exchanged among themselves and the Fund as an alternative to gold. SDRs entered service in 1970 originally as units of a market basket of 16 major vehicle currencies of countries whose share of total world exports exceeded 1%. The basket's composition changed over time and presently consists of the U.S. dollar, euro, Japanese yen, Chinese yuan, and British pound. Beyond holding them as reserves, nations can denominate transactions among themselves and the fund in SDRs, although the instrument is not a vehicle for trade. Special drawing rights were originally equivalent to a specified amount of gold, but were not directly redeemable for gold and instead served as a surrogate in obtaining other currencies that could be exchanged for gold. The Fund initially issued 9.5 billion SDRs from 1970 to 1972 (Somanath, 2011).

In January 1976, the IMF members signed the Jamaica Agreement, which ratified the end of the Bretton Woods system and officially embraced the flexible exchange rate regimes, thus formalizing the end of use of gold as a reserve instrument. The IMF gold reserves were then returned to members or sold to provide poorer nations with relief funding. Developing countries and countries not endowed with oil export resources enjoyed greater access to IMF lending programs as a result.

After the agreement, IMF continued assisting nations experiencing balance of payment deficits and currency crises, but began imposing conditioning on its funding that required countries to adopt policies aimed at reducing deficits through spending cuts and tax increases, reducing protective trade barriers, and contradiction on monetary policy (de Vries, 1986).

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In 1978, a second amendment to the articles of agreement was signed, and it legally formalized the free-floating acceptance and gold demonetization achieved by the Jamaica Agreement. Additionally, it required members to support stable exchange rates through macroeconomic policy. The post-Bretton Woods system was decentralized in that member states retained autonomy in selecting an exchange rate regime (de Vries, 1986).

Post 2007-2008 financial and banking crisis, the IMF states that its mission is as follows:

> The IMF's primary purpose is to ensure the stability of the international monetary system—the system of exchange rates and international payments that enables countries (and their citizens) to transact with each other. The Fund's mandate was updated in 2012 to include all macroeconomic and financial sector issues that bear on global stability. (IMF, 2017)

In order to attain that goal, the IMF states in its official web page that it works with a management team and 17 departments. The staff has a managing director, who is the head of the staff and chairperson of the executive board. He is appointed by the executive board for a renewable term of five years and is assisted by a first deputy managing director and three deputy managing directors. The resources for IMF loans are provided by member countries, primarily through their payment of quotas. Each member country of the IMF is assigned a quota, based broadly on its relative position in the world economy.

The primary decisions of IMF are made by the board of governors formed by one governor and one alternate governor for each member country. The governor is appointed by the member country and is typically the minister of finance or the governor of the central bank. This board normally meets once a year (IMF, 2017).

Table 1 shows the quota and voting shares of IMF members since the Board Reform Amendment on January 2016 as a percentage of the total.

It is important to note that over 50% of the quotas are held by the United States, Japan, China, Germany, the United Kingdom, France, Italy, and India. In order to attain over 50% of the voting power, Russia is included in the group. These nine countries, in case of mutual agreement, may decide by vote, any question in the board of governors.

4.3. World Bank

Founded in 1944 at the Breton Woods Conference, the International Bank for Reconstruction and Development (IBRD) became most known as the World Bank (WB). The purpose of this organization was to provide loans to help rebuild countries devastated by World War II. In time, the focus shifted from reconstruction to development, with a heavy emphasis on infrastructure such as dams, electrical grids, irrigation systems, and roads. With the founding of the International Finance Corporation in 1956, the institution became able to lend to private companies and financial institutions in developing countries. Moreover, the founding of the International Development Association in 1960 puts greater emphasis on the poorest countries, part of a steady shift toward the eradication of poverty becoming the bank broup's primary goal. The subsequent launch of the International Center for Settlement of Investment Disputes and the Multilateral Investment Guarantee Agency further rounded out the bank group's ability to connect global financial resources to the needs of developing countries. Therefore, today, the bank has five branches as we shown in Table 2 (World Bank, 2017).

To become a member of the World Bank, a country should first join the International Monetary Fund (IMF). To become a member in IDA, IFC, and MIGA, a membership in IBRD is mandatory. The member countries, or shareholders, are represented by a board of governors, who are the ultimate policymakers at the World Bank. Generally, the governors are member countries' ministers of finance or ministers of development. They meet once a year at the annual meetings of the boards of governors of the World Bank Group and the International Monetary Fund. The voting policy follows the same characteristics as the IMF. So that each member votes on a system of share votes (one vote for each share of the bank's capital stock held by the member) plus basic votes (calculated so that the sum of all basic votes is equal to 5.55% of the sum of basic votes and share votes for all members). The exception is MIGA where each member votes based on share votes (one vote for each share of MIGA's capital stock held by the member) plus parity votes, calculated so that the aggregate number of votes of category 1 and category 2 members is the same. Members select the category they want to join at the time of membership. The category 1 has members that were

Table 1. Quota and Votes of the Countries Members of IMF as a Percentage of the Total.

	Country	Quota (%)	Votes (%)
1	USA	17.60	16.70
2	Japan	6.54	6.21
3	China	6.46	6.14
4	Germany	5.65	5.37
5	UK	4.27	4.21
6	Frane	4.27	4.07
7	Italy	3.20	3.05
8	India	2.78	2.66
9	Russia	2.74	2.35
10	Saudi Arabia	2.72	2.31
11	Brazil	2.34	2.24
12	Canada	2.34	2.24
13	Spain	2.02	1.94
14	Mexico	1.89	1.82
15	Netherlands	1.85	1.78
16	Coreia	1.85	1.72
17	Australia	1.39	1.35
18	Belgium	1.36	1.31
19	Switzerland	1.22	1.19
	Total	***72.49***	***68.66***
	Other 169 member	***27.51***	***31.34***

Source: Elaborated by the authors using official data provided by IMF at: https://www.imf.org /external/np/sec/memdir/members.aspx#top, accessed May 16, 2017.

originally defined as developed countries, and category 2 has members defined as developing countries (Persaud, 2012).

The World Bank operates under the leadership of the president, and the vice presidents in charge of global practices, cross-cutting solutions, areas, regions, and functions. The five largest shareholders appoint an executive director, while other member countries are represented by elected executive directors. The governors also delegate specific duties to 25 executive directors, who work on-site at the bank. The executive directors make up the boards of directors of the World Bank. They normally meet at least twice a week to oversee the bank's business, including approval of loans and guarantees, new policies, the administrative budget, country assistance strategies, and borrowing and financial decisions. (World Bank, 2017).

4.4. Group of Ten

The Group of Ten or G-10 refers to the group of countries that agreed to participate in the General Arrangements to Borrow (GAB), an agreement to provide the International Monetary Fund with additional funds to

Table 2. World Bank Structure.

Foundation date	Name		Mission
1944	International Bank for Reconstruction and Development (IBRD)	World Bank (WB)	Provides loans to governments of middle-income and credit worthy low-income countries.
1956	International Development Association (IDA)		Provides interest-free loans and grants to governments of the poorest countries (per capita annual income less than US $ 925)
1960	International Finance Corporation (IFC)		Private sector financing of developing countries.
1966	International Center for Settlement of Investment Disputes (ICSID) * 140 Member States.		Reconciliation and arbitration of international investment disputes (investors × States).
1988	Multilateral Investment Guarantee Agency (MIGA) *180 member countries with 25 lenders		Ensure private foreign investment in developing countries.

Source: The World Bank Official Home Page at: http://www.worldbank.org.

increase its lending ability. The GAB was established in 1962, when the governments of eight International Monetary Fund (IMF) members—Belgium, Canada, France, Italy, Japan, Netherlands, United Kingdom, and the United States of America—and the central banks of Germany Federal Republic and Sweden, agreed to make resources available to the IMF with an additional $6 billion of their own resources. The Group of Ten signed the Smithsonian Agreement in December 1971, replacing the world's fixed exchange rate regime with a floating exchange rate regime owing to the end of the Bretton Woods agreement (Black, 2009).

Nowadays the G-10 is made up of 11 industrial countries (Belgium, Canada, France, Germany, Italy, Japan, the Netherlands, Sweden, Switzerland, the United Kingdom, and the United States), which consult and cooperate on economic, monetary, and financial matters. The ministers of finance and central bank governors of the Group of Ten meet as needed in connection with the meetings of the International Monetary Fund (IMF) and the World Bank (WB) in order to produce joint documents or reports that express the joint view and decisions of the group regarding the subject that motivated the meeting (BIS, 2017).

4.5. Financial Stability Forum (FSF) and Financial Stability Board (FSB)

In February 1999, the G10 Finance Ministers and Central Bank Governors created the Financial Stability Forum (FSF)—which became the Financial Stability Board (FSB) in 2009—to coordinate the emerging international standards regime by bringing together in the same place the representatives of important organizations of the International Financial System such as the BCBS, IAIS, IOSCO, IASB, IMF, WB, BIS, and OECD, and the central bank, finance ministry, and regulatory and supervisory authorities from each G7 country (along with the European Central Bank (ECB). As one of its first tasks, the FSF compiled a compendium of existing international prudential standards (Porter, 2009).

More specifically, the FSB was established to assess vulnerabilities affecting the global financial system as well as to identify and review, on a timely and ongoing basis, the regulatory, supervisory, and related actions required to address these vulnerabilities, and their outcomes. In addition, it aims to promote coordination and information exchange among authorities responsible for financial stability monitoring and to advise on market developments and their implications for regulatory policy. In order to perform the action, FSB undertakes joint strategic reviews of the international standard setting bodies and coordinates their respective policy development work to ensure this work is timely, coordinated, focused on priorities and addresses gaps. In order to do so, FSB collaborates with the International Monetary Fund (IMF) to conduct Early Warning Exercises in order to promote member jurisdictions' implementation of agreed

commitments, standards, and policy recommendations, through monitoring of implementation by peer review and disclosure (Helleiner, 2010).

According to the FSB official page (www.fsb.org), the plenary is the sole decision-making body of the FSB and is governed by the FSB charter, Articles of Association, and procedural guidelines. The countries that are represented in it are Argentina, Australia, Brazil, Canada, China, France, Germany, Hong Kong, India, Indonesia, Italy, Japan, Korea, Mexico, Netherlands, Russia, Saudi Arabia, Singapore, South Africa, Spain, Switzerland, the United Kingdom, and the United States. Important organizations such as International Monetary Fund (IMF), the World Bank (WB), Bank for International Settlements (BIS), Organization for Economic Cooperation and Development (OECD), European Central Bank (ECB), European Commission, Basel Committee on Banking Supervision (BCBS), International Association of Insurance Supervisors (IAIS), International Accounting Standards Board (IASB), and Committee on the Global Financial System (CGFS) are represented in the SFB.

Embedded in the FSB's structure is a framework for the identification of systemic risk in the financial sector, for framing the policy sector policy actions that can address these risks, and for overseeing implementation of those responses. The FSB's structure comprises the plenary as the decision-making body, a steering committee to take forward operational work in between plenary meetings, and three standing committees: (1) the Standing Committee on Assessment of Vulnerabilities (SCAV), which is the FSB's primary mechanism for identifying and assessing risks; (2) the Standing Committee on Supervisory and Regulatory Cooperation (SRC), which is charged with undertaking further supervisory analysis or framing a regulatory or supervisory policy response to a material vulnerability identified by SCAV; and (3) the Standing Committee on Standards Implementation (SCSI), which is responsible for monitoring the implementation of agreed FSB policy initiatives and international standards (Helleiner, 2010).

The FSB's decisions are not legally binding on its members. As obligations of membership, the members commit to pursue the maintenance of financial stability, maintain the openness and transparency of the financial sector, implement international financial standards, and agree to undergo periodic peer reviews, using IMF/World Bank public Financial Sector Assessment Program (FSAP) reports. They also commit to implement international financial standards (Porter, 2009).

5. IMF AND THE IFS REGULATORY ORGANIZATIONS

In this section, we discuss how BIS, IMF, and WB work together regarding the interaction with countries that have problems in their balance of payments or experience debt issues.

Regarding practical logistics, the International Monetary Fund (IMF) interacts with governments while the Bank for International Settlements (BIS) interacts only with central banks. The IMF lends money to national governments of countries experiencing some fiscal or monetary crisis. In addition, the IMF produces money by receiving contributions from the quotas of its member countries. Although member countries can borrow money to make their contributions, they actually come from taxes paid by taxpayers. It is curious that this characteristic of the IMF relationship with its member countries is exactly the basis of economic policy consolidated in capitalist democracies in the last decades and that it engenders, in its apparent hydraulic logic of equilibrium, a contradiction between the taking of the social product generated by national economies and the policies of money emission. Through it, wealth is exchanged for credit, quite distinct categories within economic theory.

The World Bank also lends money to governments. Within the World Bank, there are two separate entities for this purpose—the International Bank for Reconstruction and Development (IBRD) and an International Development Association (IDA). As explained before, the IBRD targets middle-income countries and countries deserving credit, while the IDA caters to the poorest countries in the world. The World Bank is self-sufficient for internal operations, lending money from direct bank lending and floating bond issues, and then lending this money through IBRD and IDA to countries in difficulty.

BIS, like the central bank of the others banks, facilitates the movement of money. It does "bridge loans" to the central banks of countries where IMF or World Bank money has been promised but not yet released. These bridge loans are then returned by the respective governments when funds are released that have been pledged by the IMF or the World Bank.

The IMF is the last resort of the BIS when a monetary crisis occurs. For instance, in the 1998 crisis with the Brazilian currency, caused by the country's inability to pay excessive accumulated interest on loans made over an extended period of time; the original loans were made by banks such as Citigroup, J.P. Morgan, Chase, and FleetBoston, and they could suffer the loss of an immense amount of money if payment did not happen. Therefore, the IMF lent money to Brazil to pay the banks and to be able to borrow again from them. In exchange for this new loan, the government had to accept the policies advised by IMF and speed the cut of expenses, the selling of governmental actives, and adopt a floating exchange rate. It is important to note that (1) this is the route of action characteristic of these institutions in the case described, such as a currency crisis in a peripheral country; and (2) the circumstances of the articulation and performance of the organizations inherent to the system also depended on the internal environment of economic policy, marked by the apologetics not only of institutionally dominant economic policies but by its practice in the form of "hegemonic knowledge."

In addition, it is also important to note that IMF and BIS, as well as the committees, commissions, forums, and other organizations created from both, have their decisions centered on a small group of nations. When crossing the structures of decision inside these organizations, the names of such countries get highlighted.

Consequently, we can observe that, in the case of BIS, 12 of the 21 board members that actually make decisions are the governors of Belgium, France, Germany, Italy, the United Kingdom, and the United States central banks. These countries own, together, 35% of the voting power of the IMF and, consequently, of the World Bank. These are also six members of the Group of Ten (G10), and along with the other countries in this group, they hold approximately 47% of the total votes in the IMF, and the World Bank.

On the other hand, organizations created to increase the participation of developing countries such as the G20 and even the Financial Stability Forum (FSF) and Financial Stability Board (FSB) do not have the power to determine or confront the decisions made by the select group of the countries mentioned earlier.

6. CONCLUSION

The articulation between the largest organizations of the International Financial System (IFS) follows a logic and purpose that are not exactly what they advertise on their official web pages. We can argue the case in three instances.

First, there is the concern, both in protection and development of the IFS, which holds the highest priority, that the primary goal is the creation of an effective crisis protection instrument. However, this does not necessarily void its intrinsic characteristic vulnerability.

Second, the issue of preserving the movement of capital accumulation has increased its power in the last half of the twentieth century. The economic and financial health of companies, external and domestic to national economies, is a second concern of this form of articulation in the IFS.

Third, there is the clash of these priorities with the doctrine of free trade and laissez-faire, as indicated in the previous section. On this basis, the apparent contradiction between the free-trade discourse and the institutional network of protection of the financial capital created during the twentieth century appears much more like a strategy of systemic perpetuation.

BIS, World Bank, and IMF, in their genesis and coordination, as well as their changes and permanencies over time, indicate a practice of "trial and error" in the sense of managing the financial crises, with the security not of the real assets of the economy or of the productive factors in its efficiency but of the financial capital. On the other hand, the permanence of strict interests linked to the preservation of the latter in the hands of its holders suggests a fairly linear consistency over time. The very evolution of organizations originally and formally designed to "promote economic development" in order to establish safeguards and protections for investors, as opposed to structural permanence, both in operations and in the representativeness of strictly financial bodies, such as the BIS, show the fact for which the international financial system is oriented.

Through the structure created, the interconnected functioning of the IMF, BIS, World Bank, and G10 has cohesion, speed, and decision-making power centralized in a few countries, the main world economic

powers and to discuss a reform of the IMF in order to reduce domination of developed economies; modify IMF's existing activities; expand lending facilities in relation to least developing economies; and providing governance, passes, therefore, for its necessary discussion and reorientation of the entire IFS.

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A Critical Evaluation of IMF History and Policies

Syed Ahmed*, Abdulhamid Sukar
School of Business, Cameron University, 2800 W. Gore Boulevard, Lawton, OK 73505, USA.

***Correspondence:** syeda@cameron.edu

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Abstract

The International Monetary Fund (IMF) was originally mandated to maintain exchange rate stability and adjustment of external imbalances in member countries and to act as a lender for countries facing short-term balance-of-payment crises. With the breakdown of the fixed exchange rate system, the IMF had to adjust its role in exchange rate management. The international banking crisis in the 1980s required a recalibration of IMF policies. Most of the policies in the 1980s and 1990s were driven by "Washington Consensus," a doctrinaire view of economic development that called for structural adjustment through market liberalization and privatizations. However, critics indicate that the IMF, by failing to consider the unique conditions in developing economies and lumping them under a "one size fits all," category may have caused more damage than good. In addition, it was alleged that IMF loans imposed unrealistic conditions on borrowers. All these policies are under review now in a quest for appropriate policies that will address some of these concerns and aid economic development. This paper provides a brief review of IMF policies from a historical perspective and a critique of IMF policies over the last few decades.

Keywords: Capital control; conditionality; financial crisis; financial reform; global institution, reserve asset, structural adjustment.

1. INTRODUCTION

The establishment of the International Monetary Fund (IMF) at the conclusion of the Bretton Woods agreement heralded a new era in the international economic landscape after the stalemate of interwar years. The Bretton Woods agreement was the brainchild of two protagonists. Representing the British side was the world renowned economist, John Maynard Keynes, who revolutionized macroeconomics with his General Theory. Representing the US side was a Harvard economist, John Dexter White, then treasury secretary. These two prodigies had two different, sometimes, opposing visions about the emerging international monetary order. Keynes, being the reputed economist, wanted to maintain UK interests in the postwar era, whereas White wanted to ensure that the emergence of the United States as the mightiest economic power was recognized. Another complicating issue was that British and other European powers needed immediate financial aid to recover from their prewar losses.

Keynes envisioned a truly multilateral system, based on a single international central bank that would serve as an international clearing union (ICU). The ICU would be structured in a way so that no single currency and, therefore, no single country could dominate the system and also to prevent a crisis in the foreign exchange market similar to the one in 1928-1932 (D'Arista and Erturk, 2013). In Keynes' vision, the ICU would create an international reserve currency, Bancour, which would supplement gold and dollar. Similar to Keynes, White also believed that a multilateral institution would be far more effective than a bilateral institution in helping countries ravaged by the war. He suggested the formation of an international credit cooperative, which would provide loans to banks, the size of the loan to be determined by the amounts paid by other member countries. At the end, neither of the two proposals saw the light of the day in their original forms, but the final deal incorporated parts of both proposals.

This paper provides a brief review of IMF policies from a historical perspective and a critique of IMF policies. Section 2 delineates the evolution of IMF from a historical perspective. Section 3 provides a critique of IMF governance and policies. Section 4 demonstrates some evidence between IMF loans and economic growth. Section 5 provides some concluding thoughts.

2. EVOLUTION OF IMF POLICIES—A HISTORICAL PERSPECTIVE

We can divide the evolving history of the IMF into three phases.

2.1. Phase I: IMF Policies during the Fixed Exchange Period, 1944-1971

The mandate of the IMF at its creation was to govern and support the new international economic order in the postwar world (Kenen, 2007). The IMF was created to maintain exchange rate stability and adjustment of external imbalances in member countries and act as a lender for countries facing short-term balance-of-payment crises (Minton-Beddoes, 1995). In the initial years, the overriding objective of the IMF was to support and maintain the multi-currency parity rate based on the fixed price of dollar in terms of gold. During the fixed exchange rate system, the US dollar was pegged to gold at $35 per ounce of gold and other major currencies were linked to the US dollar at a fixed rate. The IMF would advise a country to devalue its currency if it considered the currency to be overvalued, hurting its balance-of-payment position. Exchange rate misalignment and balance-of-payment difficulties were the main preoccupation of the IMF during the period from 1944 to 1971.

During the 1950s and 1960s, IMF lending mostly comprised short-term loans to advanced economies to facilitate moderate exchange rate adjustments (Reinhart and Trebesch, 2015). Western developed nations such as the United Kingdom, France, Iceland, Italy, Spain Portugal, and the United States borrowed from the IMF in the initial years after the formation of IMF. Later, the IMF assistance was provided mainly to developing economies of Asia, Africa, and Latin America and emerging market economies in Eastern Europe. Membership expanded from 28 in 1945 to 188 in 1990s. Membership experienced two growth spurts, one in the 1960s because of independence of former colonies of Africa and the other in the 1990s after the breakdown of the soviet empire and the independence of eastern European countries (Broughton, 2009).

Since its inception, the Bretton Woods system suffered from problems of liquidity, confidence, and adjustment. In the post-World War II world economy, the dollar emerged as the key currency and a major reserve asset. Dollars held by the official institutions (mainly non-US central banks) were freely convertible into gold. However, the problem was, as Triffin (1960, 1968) indicated, the inherent unsustainability of the system. This is because a growing supply of world liquidity of reserve assets (US dollar) depended crucially on a growing US trade deficit. However, a large balance-of-payments deficit, relative to the supply of gold, undermines confidence in the reserve currency and could trigger a crisis. The pressure on the US dollar mounted, as the US trade balance worsened in the 1960s owing to Vietnam, a huge international aid program, and other commitments.

When some European central banks began to convert US dollars into gold, US gold reserves at Fort Knox began to fall at an alarming rate. President Nixon declared a moratorium on the convertibility of dollar into gold on August 15, 1971, ending the era of fixed exchange rate.

2.2. Phase II: Oil Price Shock and International Banking Crisis, 1972-2007

After a turmoil in the foreign exchange market upon the collapse of the Bretton Woods agreement in 1971, dust started to settle around 1973 when the Jamaica agreement was reached. The era of floating exchange rates began with the exchange rates of developed countries determined by free forces of demand and supply and exchange rates of most developing economies linked to major convertible currencies of the west.

The oil price shocks of 1973-1974 unleashed a new set of dynamics both on the demand and the supply side in the foreign exchange market, which also provided new challenges for the fund. On the demand side, oil-importing countries were in need of dire financial help for high costs of oil imports. On the supply side, oil-exporting countries ended up with a sudden bonanza of reserves from the oil price hike. Much of the oil revenues found their way into European financial markers as petrodollars. To meet the challenges of the oil price shock, the IMF created an oil facility (Broughton, 2009).

On the heel of the international banking crisis in the early 1980s, the IMF had to reinvent itself to meet new challenges and recalibrate its policies to deal with the crisis that unfolded with default on sovereign debt by some Latin American countries. The focus shifted from exchange rate management issues and balance-of-payment problems to sovereign default and international banking issues. The scope of IMF expanded to structural reform and financial stabilization management of member countries. The international institution

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was expected to provide a new public good in the form of financial market stability (Bordo and James, 2000). In view of recurring banking crises, the IMF adopted a two-pronged policy of financial sector stability and prevention of liquidity crisis (Papi *et al.*, 2015). These issues reemerged during the global financial crisis of 2008. Since the early 1980s, term loans were replaced with long-term loans on projects that would span over decades with precautionary credit lines provided to prequalified countries. Loans became more of developmental assistance. Following the lead of World Bank and based on the Washington consensus, IMF loans were also tied to structural reforms. Loans were made conditional upon implementation of structural adjustment policies and successful reforms in the economy. Close surveillance, constant monitoring, and policy recommendations became part of the new policy. Since 1990s, IMF loans have been tied to financial reform measures and capital account liberalization measures (Joyce and Noy, 2008). An important lesson learned from the financial crises of the 1990s in Mexico, Southeast Asian counties, Russia, and Turkey is that financial sector liberalization, without tight banking supervision in place, may lead to banking sector fragility.

2.3. Phase III: Global Financial Crisis and New Challenges, 2000

During the Asian financial crisis in 1997, many Southeast Asian countries could not get IMF loans because of highly stringent conditions attached to the loans. Consequently, the IMF reserves continued to grow. Countries such asThailand, Hong Kong, Korea, and Singapore learned a valuable lesson from their experiences of financial crises. Not taking any more chances, some of these countries gathered over $100 billion war-chest funds to ride over any possible financial storm (Eraseder, 2015). Consequently, around 2003, income from the IMF loan portfolio shrunk alarmingly as countries started taking fewer loans from the IMF.

The global financial crisis of 2007-2008 changed the international financial landscape for the IMF again, as it regained its status as international lender of last resort (Ban and Gallagher, 2014). The IMF started providing more loans to countries that suffered financial crises, opening the spigot of money to distressed countries. During the global financial crisis, the IMF provided loan arrangements of $225 billion as of October 31, 2009, whereas it had provided only $36 billion in loans to distressed countries in Southeast Asia in 1997-1998. Thus, according to Rose (2010), the IMF emerged as the lead international financial institution in charge of dealing with financial crises. The IMF received additional resources in the form of Special Drawing Right (SDRs) worth $250 billion. Its lending capacity increased to $750 billion through an expansion of "New Arrangements to Borrow" (Rose, 2010). Within 18 months of the unfolding of the crisis, 18 countries received loans as part of the crisis management. After the global financial crisis, the IMF loan exceeded any previous record in terms of sheer volume of loan provided to Greece and other PIIGS (Portugal, Italy, Iceland, Greece, and Spain) countries (Eraseder, 2015). According to Rose (2010), the IMF rose to the occasion in the aftermath of the global financial crisis, as leaders of developed countries stood by their IMF commitments. As a result, the IMF was not criticized as badly about handling the global crisis as it was in the aftermath of the Asian financial crisis.

Since the financial crisis of 2008, the IMF started emphasizing the importance of fiscal balance and consolidation to borrower countries with reduced emphasis on structural reforms that characterized the IMF policies in the 1980s and 1990s (Broome, 2014).

3. REVIEW OF IMF POLICIES

The original framework of the Bretton Woods system had international development content and was formulated in consultation with developing countries. The Bretton Woods discussion generated many innovative proposals to create a development-friendly international financial order, some of which found their way into the agreement (Helliner, 2014). The content was dramatically watered down when many of the original architects of the system lost influence and those who assumed power were skeptical about the development goals and urged free trade and the acceptance of foreign investment in the region (Helliner, 2017).

Countries of Latin America and India expressed strong frustration with the lack of international development content in the existing system and together with Africa and other developing countries demanded a "New International Economic Order" (NIEO) that would support their development goals. They demanded greater access to financial resources in the North to meet development needs and an increase in the overall participation in the decision-making process of the fund.

In early 1970s when interest rates were low, developing countries borrowed heavily to invest in infrastructure and other large-scale development projects. When interest rates increased sharply in 1980s, heavy debt loads seriously affected their ability to repay and forced them to borrow more to finance their debt. As a result of this, the push for the NIEO order collapsed, developing countries lost their voice in the decision making, state-level development policies were dismantled, and multilateral governance became mainly centered around G7 (Helliner, 2017).

As mentioned above, the World Bank and IMF introduced structural adjustment programs (SAP)—long-term loans to countries experiencing recurrent balance-of-payment problems. These loans emerged with a variety of conditions based on what is termed as "Washington Consensus." The Washington consensus maintained that market liberalization, privatization, and fiscal responsibility would spur economic growth in less-developed economies as it did in developed economies. Restructuring comprised reducing public expenditure, liberalizing trade, investment, and capital controls; deregulation; and privatization of state-owned enterprises. Frequently, the terms of conditionality were attached with IMF loans without due consideration for borrower countries' individual circumstances and their perspectives.

According to critics, the IMF imposed the Washington consensus upon developing economies with considerably many restrictions. Stiglitz (2002) contends that requirements of conditionality imposed by international institutions such as the IMF or World Bank have been used as policy tools frequently without considering the best interests of the economics concerned. In some cases, the IMF may have provided wrong recommendations to developing economies in terms of monetary and fiscal policies. For example, Stiglitz provided an example of Korea where during the Asian financial crisis, the IMF urged the central bank of Korea to focus on inflation although monetary policy did not cause any problem there. Stiglitz also suggested that the "one size fits all" approach did not recognize the distinct characteristics and dynamics of different countries and the policies might have caused more harm than good.

Critics argue that the IMF policies were applied all at once than sequentially—for example, careful regard was not taken to determine whether appropriate Institutional framework was present for implementation of such policies. For example, privatization of utility companies was recommended without consideration for the impact on unemployment. Large-scale privatization was conducted without creating an appropriate institutional framework to deal with unemployment problems that would result from the massive layoffs by the newly created private firms who took over public companies, leading to immense economic and social problems.

Critics of IMF were also apprehensive about the role of the Bretton Woods institutions in shaping the development discourse through their research, publishing activities. Many of the top positions of the IMF were held by University of Chicago graduates who were strong supporters of free market economy and advocated privatization, deregulation, and cuts on social spending (Klein, 2007). As the World Bank and the IMF staff were regarded as experts in the field of financial regulations and economic development, their view and prescriptions undermined or eliminated alternative perspectives on development. Even within the Chicago boys, those who tried to introduce these ideas with democratic debate were overwhelmingly rejected (Klein, 2007).

There is a slew of critical literature on the conditionality with a general focus on the distributional aspect of the reform. Criticisms of IMF policies include the failure of reforms to take social and environmental issues into account and the failure to ensure sustained growth. Another point of criticism of the IMF was that the conditionality impinged upon the sovereignty of borrowers. Thus, there were not only economic repercussions of conditionality but the inflexibility in negotiations alienated governments from the measures they were supposed to implement. The overlap of IMF and the World Bank policies also swamped governments of borrowing countries with policy conditions (Kellick, 1993).In response to the critique, the IMF became more flexible in ways it engaged with countries in issues related to structural reform. In 1999, it replaced SAP with poverty reduction and growth facility (PRGF). The PRGF was intended to be based more on participation and country ownership, be more selective in the use of terms of conditionality, and include stronger analysis of social issues (Bull *et al.*, 2006).

The guidelines on the conditionality were revised in 2000. The new guidelines state the key principles of conditionality are to ensure that fund resources are used to assist members in solving their balance of payments, which is consistent with the original intent of the fund (IMF, 2002). The new guidelines emphasize five interrelated principles that the fund believes are relevant for the success of fund-supported programs: 1)

National ownership of reform program, 2) Parsimony in the application of program-related conditions, 3) Tailoring programs to members circumstances, 4) Effective coordination of policies with other multilateral institutions, and 5) Clarity in specific conditions (IMF, 2002).

Cooperation among governments of member countries is of paramount importance to address a global economic crisis. The IMF is criticized for not being adequately equipped to ensure such cooperation (Woods, 2006). It is a global institution, but it is dominated by a few major industrialized countries who pay little heed to the views of developing countries. Advanced economies provide the bulk of IMF resources but do not use the facilities while developing countries provide a small share but draw upon the fund's resources for financial assistance, which makes them subject to conditionality. This situation created tension around governance issues. Developing countries make up 85% of the total membership and believe they have an inappropriately small voice within the organization (Bloomberg and Broz, 2006). Jha and Saggar (2000) mentioned that the Bretton Woods agreement did not provide a clear raison d'être for the quota system. Moreover, the quota system is inherently biased against developing economies. According to them, despite impressive growth, some non-oil-exporting countries experienced a decline in their quota shares. Under the existing quota structure, members should vote to approve or disapprove policy proposals before they are implemented. In most cases, a majority of 70% votes are required to make a decision. In certain cases, such as admitting a new member, it would require 85% of the votes (Woods, 2006). Because of the way the governance of the IMF is structured, few industrialized countries dominate their votes. For many years, there has been an effort to reform the IMF through changing vote. In December 2010, the board of governors of the IMF approved a package of the fund's quotas and governance, and the reform became effective only in January 26, 2016 (IMF, 2017). The reform reflects the increasing importance of emerging market countries. The voting shares of China, Russia, Brazil, and India were increased. The United States is the largest member of the IMF currently accounting for 17.46% of the quota and 16.52% of voting shares (IMF, 2017). With such a big chunk of the quota, the United States along with other G7 countries dominates decisions in the IMF. The fifteenth review of quotas, scheduled for 2019, is expected to show further increased share of dynamic economies of emerging markets. Reforms also envisage an increase in permanent capital resources. In fact, the IMF resources doubled to SDR $477 billon (approximately US$659 billion) in recent years.

The IMF was created with limited lending ability, because it was overtly reliant on the US dollar. It did not develop an effective method for dealing with trade imbalances. Consequently, imbalances among countries continued to grow. "Lack of an effective mechanism to deal with trade imbalances ultimately undermined the system's ability to provide flexible monetary reserves and simultaneously safeguard its integrity" (D' Arista and Erturk, 2013, 235). Currently, Germany, Japan, and China are sitting atop a huge amount of international reserves, whereas, the United States is running with a huge trade deficit with no automatic adjustment in place.

Another concern is the role of unrestricted movement of capital across national boundaries in financial crises including the ones in Mexico in 1994, East Asian financial crisis in 1997, and the global financial crisis in 2007-2008. The IMF stance on capital control has changed drastically over the years. In the initial years after its inception, the IMF supported capital control, consistent with the views of the academic circles then, namely, Keynes and White. Capital control allows a country to pursue an independent macroeconomic policy and maintain financial and currency stability. However, this view changed with the onset of the liberal era in the 1980s. The IMF started supporting capital account liberalization and, for example, did not, in particular, support Malaysia imposing capital control in the wake of the financial crisis in 1994. However, in the aftermath of the Asian financial crisis in the late 1990s, the IMF started supporting a limited capital control. However, there was considerable ambivalence about capital control. The pendulum swung to capital control as all doubts about it evaporated after the global financial crisis of 2008.

The IMF has made a significant progress over the years including adaptation of lending facilities, streamlining reforms, and helping countries to have control over their own reform (Helliner, 2017). The changes, however, have been very slow and considerably little to have any significant impact on IMF decision making. Dissatisfied with the decision-making process and policies of the IMF, the developing countries started to look for alternative sources of funding. In particular, China's influence in developing countries has been increasing. Moreover, it has become an important source of both development funds and foreign exchange. New institutions such as New Development Bank and Asian Infrastructure Investment Fund pose

further challenges to the IMF. Unless, the fund reforms its quota system to reflect the changing economic dynamics of the world, its credibility and influence will be further eroded.

4. EVIDENCE ON ASSOCIATION BETWEEN IMF LOAN AND ECONOMIC GROWTH

The evidence on the impact of IMF loans on the economic growth of developing economies is mixed. The IMF reviews typically report a positive relationship between IMF loans and economic growth. For example, in a study of 36 countries that received support under structural adjustment facility (SAF) and enhanced structural adjustment facility (ESAF), the IMF study finds that most of them became more market oriented and economically stronger after receiving IMF loans IMF (1997). The living standards of the people in these countries improved, and substantial progress was made toward external viability. The IMF study also recognized that the progress was uneven, thereby reflecting policy weakness, and a number of ESAF countries are still poor. Easterly (2003) finds no systematic effect of adjustment lending on growth. Papi *et al*. (2015) covered 113 low- and medium-income countries from 1970 to 2010 and found that countries who participated in the IMF-supported programs were less likely to have banking crises. Eichengreen *et al*. (2008) also found that countries with strong fundamentals who take IMF loans are less likely to have financial crises.

Dreher and Walter (2010), in a study of IMF programs in 68 developing countries that spanned five years, found that the IMF aid reduced probability of a currency crisis. They also indicated that it was the terms of the lending agreement that made a difference. Since 1990s, IMF loans have been tied to financial reform measures and capital account liberalization measures (Joyce and Noy, 2008). An important lesson learned from those days is financial sector liberalization without tight banking supervision may lead to banking sector fragility. Przeworsky and Vreeland (2000) and Barro and Lee (2003) found that the IMF loan participation had a negative effect on economic growth.

5. CONCLUSION

Since the inception of the IMF in 1944, it has come a long way in meeting new challenges of international finance and international monetary order. During the first few decades of the IMF's formation, major clients of the IMF were advanced economies of the west. Since the 1980, banking crises and sovereign default problems in Latin American and African economies dominated the IMF agenda and focus shifted from balance-of-payment problems of advanced economies to debt sustainability problems of developing economies.

In recent years, the IMF has conducted major reforms in terms of quota and governance of loans. The IMF's fourteenth general quota review, which was conducted in 2010, reflected a major shift in quota governance policy. The reforms entailed a major shift in quota share toward dynamic emerging market economies. Another remarkable development is the elevation of four emerging market economies, Brazil, India, China, and Russia, to the group of 10 largest members of IMF. According to some quarters, the changes, however, have been very slow and considerably little to have any significant impact on IMF decision making. Dissatisfied with the decision-making process and policies of IMF, developing countries started looking for escaping the IMF orbit by seeking alternative source of Funds (Ocampo, 2013). In particular, China's influence in developing countries has been increasing. Moreover, it has become an important source of both development funds and foreign exchange. New institutions such as New Development Bank and Asian Infrastructure Investment Fund pose further challenges to the IMF. Unless, the fund reforms its quota system to reflect the changing economic dynamics of the world, its credibility and influence will be further eroded.

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Developing Economies and Global Governance: Will IMF Rethink Its Orthodox View?

Manjula Jain*, Himanshu Gupta
School of Business Management, IFTM University, Moradabad, India.

***Correspondence:** manjulajain@iftmuniversity.ac.in

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Abstract

It has been constantly viewed that the developed economies unevenly ruled the governance structures in the international organizations such as International Monetary Fund (MF). The continuous development in Emerging and Developing Economies (EDEs) over the last 20 years witnessed their growing importance in the world economy, but at the same time little increase in their voice in the IMF. There are reasons for the discontent of the EDEs in the present structure such as the increase of regional monetary arrangements, uneven distribution of quota shares, IMF quota reforms, and IMF voting structure. The world economy is witnessing a tremendous growth of these EDEs and is now at the verge where Asian economies are capable of leading, rather than the North Atlantic economies. This issue should be acknowledged properly and must be responded adequately. This paper makes an attempt to understand the prime issues that should be fixed in the current quotas system and voting structure in the IMF.

Keywords: Developing economies; Governance; International Monetary Fund; Reforms; Quotas.

1. INTRODUCTION

The last few years have seen a number of heated arguments over the long-awaited changes in economic governance across the globe. These arguments draw their roots from the fact that despite the approval of the board of governors in 2010, implemented in 2016, least has been done in the direction of economic reforms by the International Monetary Fund (IMF). The United States (US), being the largest member of the IMF, enjoys an effective veto with a current quota (as of March 2017) of Special Drawing Right (SDR) 82.99 billion (about US$113 billion), which accounts for 17.7% of the quota share (and 16.7% of the vote share), therefore making any reform in the current quota system impossible without the consent of developed countries, as more than 85% of total votes are required to make it happen (IMF, 2016c). The biggest irony is that the reforms are delayed due to the failure of the U.S. administration to obtain approval from the U.S. congress despite the fact that the US was the main architect of the 2010 agreement (Truman, 2015), which emphasized the need to increase the share of EDEs by marginally reducing the share of European countries.

The quota reviews in the IMF, which should be implemented in a period not exceeding five years, have been delayed unprecedently. This is mainly due to the resistance of the so-called advanced economies (AEs) and the obscurity of the U.S. administrations in getting the essential approval of the Congress. Keeping in mind the fragile nature of the global economy and the repercussions of the North Atlantic financial crisis (NAFC), such as sovereign debt, the indisposition of IMF management and its members is difficult to comprehend.

Despite the fact that the world economy is facing ongoing substantial modifications in the dissemination of economic power, this reluctance of the AEs group has great importance, as they don't want any changes in the present structure of global governance. The current framework has been in place since World War II end, when the conception of the IMF and the World Bank took place in the Bretton Woods Conference (BWC). Subsequently, many international organizations, such as the World Trade Organization (WTO) in 1942, Regional Development Bank in 1960, and Asian Development Bank in 1966, were formed. However, the only noteworthy change to the present structure was the formation of Financial Stability Board (FSB) in year 2009 as a result of the NAFC.

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The problem at present is the unceasing dominance of these global bodies by the AEs regardless of the significant modifications that are now happening in the present global economic framework. The formation of BRICS Bank (a $100 billion New Development Bank) by the BRICS countries (Brazil, Russia, India, China, and South Africa) and the Asian Infrastructure Investment Bank (hereafter AIIB) majorly led by China is a sign of the dissatisfaction of EDEs with the present structure of global governance.

Here, the question is, why these issues are now brought out with more focus rather than two decades back? We are continuously debating that we are now at the verge where Asian economies are capable of leading the world economy that has not been viewed over the past two centuries. Moreover, the stability in the world economic framework can be viewed from World War II end till the twentieth century. Although in the same period the AEs were having 60-70% share of the world gross domestic product (GDP), owing to postwar economic changes in Japan and Germany, the AEs' relative weights themselves vary. However, during the period, the continuous dominance of the US was seen in the global economy. Since the twentieth century, the rapid shift in the world economy weight from the North Atlantic economies to Asian economies has been observed. The evidence of this historical development over the past 15 years is the root cause of today's vigorous debate. With the hope of such change hastening the current scenario over the next two or three decades or so, the present incremental change in global governance will not suffice; rather it will have to be more indispensable.

This paper is an attempt to draw attention to the major problems that are being faced by developing economies, specifically related to global economic governance by the IMF. The rest of the paper is outlined as follows. Section 2 details the historical perspective of the modifications that took place in the world economy over several periods and the need for the same at present. Section 3 highlights the changes in the IMFs global governance framework in the last seven decades. In addition, this section describes why there is a need for IMF to rethink its orthodox view particularly in reviewing the quota formula as to cater the present changes going on in the world economy. Section 4 assesses the importance and role of EDEs in governance of various international platforms while the final Section 5 concludes by conferring the necessities of changes on the regular interval so as to make the IMF more effective and trustworthy institution.

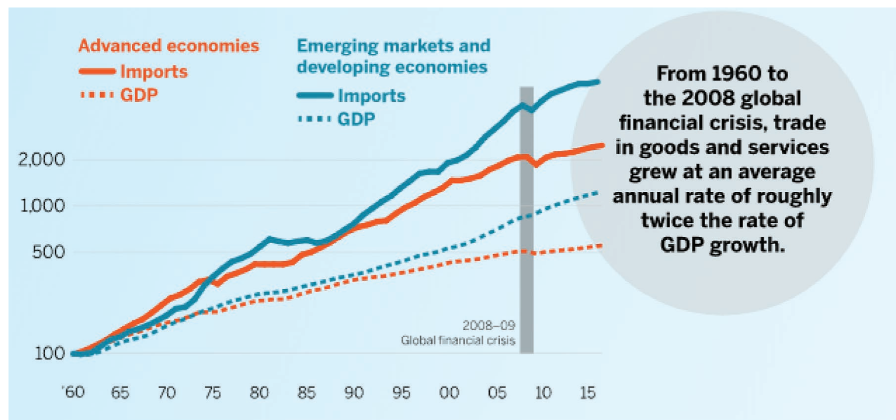
2. ECONOMIC SHIFTS AND NEED FOR GOVERNANCE

The world witnessed a dramatic change in the global economy in the eighteenth and nineteenth centuries with the industrial revolution that took place in Europe, which later gathered pace in the US and Japan as well. This marked the advent of colonialism and imperialism classifying the developing countries as groups of European powers. However, the constitutional repercussions of First World War and the subsequent Second World War undermined the European control and led to the emergence of the US as the central economic, political, and military power.

Another shift in the global growth rate took place in the 1950s with the rapid emergence of Asian and Latin American economies causing a shift in the economic power in favor of developing countries. Despite a rapid growth recorded in Japan in the 1950s, which ignited a growth trend in other Asian countries as well, the Asian tigers continued to have lower economic weight in the world economy because of small share in world GDP. According to the IMF report, the EDEs long-term GDP growth will be higher than that of AEs (Figure 1). Due to these noteworthy and substantial developments in the economies of developing countries and their repercussions for world economic governance that arouse the need for a paper that highlights on the importance and the role of these economies, a change in the quota reforms so as to have increase in the quota share and voice in the IMF.

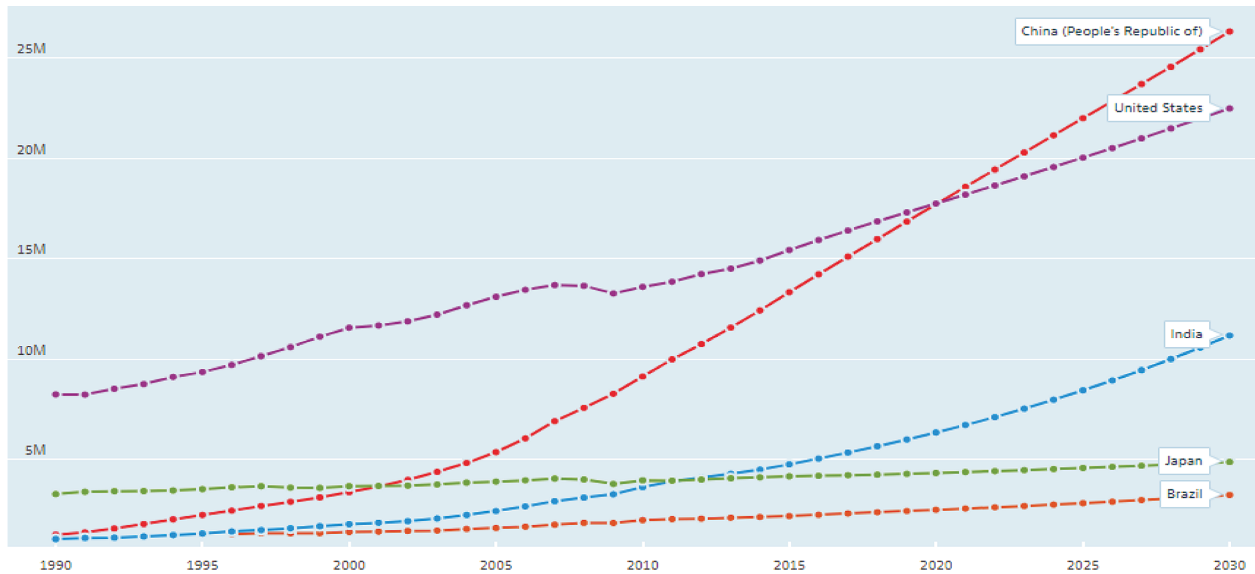
The world had started witnessing the growth of two Asian largest economies namely India and China during the late 1970s. But this growth surprisingly became more noticeable, with the commencement of fundamental reforms by these two economies—China started in the 1980s and then India in the early 1990s. Thereafter, almost for the next three decades, both economies recorded high growth, specifically China. According to Organization for Economic Cooperation and Development (OECD) report, during 1980-2014, India recorded over 6% average change in the annual real GDP growth than that of China, which recorded nearly close to 10% (Figure 2). Further in the same phase (1990s and 2000s), the Latin American region,

Figure 1. Real Trade and Real GDP Growth, 1960-2016.



Source: Author's elaboration based on data extracted from IMF (2017a).

Figure 2. GDP Long-term Forecast.



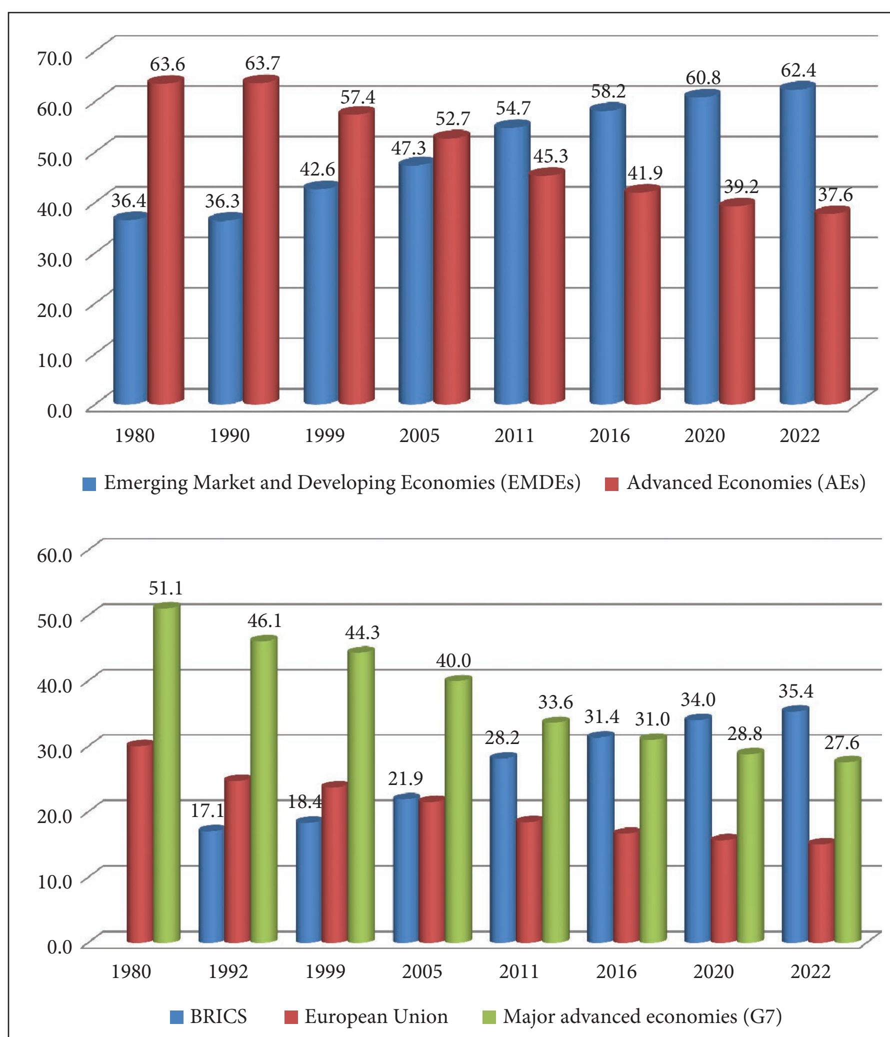
Source: Author's elaboration based on data extracted from OECD (2017).

particularly Brazil, witnessed the high growth due to comparative macroeconomic stability in that region (Figure 2).

The rapid, continuous, and sustained growth in the economies of the BRICS countries has led to increase their combined share in the global world economy (more than 31% of the share of world GDP) and hence become major players today. Furthermore, the IMF estimates (source: IMF, 2017b) the BRICS members share in the global GDP (PPP basis), which is expected to increase to 34% and 35.4% by 2020 and 2022, respectively. The year 2016 witnessed the increase in share in the world GDP of BRICs than that of the G-7 economies. Moreover, the same can be inferred from Figure 3, where the share of G-7 economies in the global GDP (PPP basis) decreased from about 46% in 1992 to about 31% in 2016 and further expected to decrease to about 27.6% by 2022, with a comparable rise in the BRICS' share from 17% in 1992 to 31.4% in 2016 and further expected to increase to 35.4% by 2022.

What is noteworthy is that in spite of sustained and high growth in Asia in almost past five decades, the overall economic weight of EDEs did not change in that ratio, and merely 10% increase concerning global GDP (PPP basis) has been observed in between 1970s and 1999. It can be noticed that in the same time span

Figure 3. Share in Global GDP (PPP Basis).



Note: BRICS data are accessible after 1992. Data for 2020 and 2022 are IMF predictions.
Source: Author’s elaboration based on data extracted from IMF (2017b).

their share concerning global GDP (MER basis) recorded a 5% downfall (Table 1) whereas the share of AEs remained constant during that period. Hence, it can be argued that these advanced economies had their dominance, and they themselves (with in G7 or G10) could easily decide the world economic framework and the contours of governance.

Nevertheless since 2000 the very rapid increase in the economies of the AEs at one side and the BRICS at the other is histrionic. Furthermore, the increasing role of EDEs in the world economy and involvement in deciding governance necessitates more accountability. With finer economic institutions and research centers, the US and Europe continue to rule the global economic power as compared to developing countries that are way lacking the essential sophistication. However, one thing is for sure that this gap can soon be bridged.

As we talk about EDEs and their relative weight in the world economy, we should first question the existence of the IMF as a coordinating institution and have an analysis of global economic policy. Until the 1970s, the IMF financial flows were basically meant for trade financing until the collapse of the Bretton Woods system that instigated the mechanism to the use of IMFs resources to be augmented significantly.

Table 1. GDP and Quota Shares of Emerging and Developing Economies vis-à-vis Advance Economies.

Item	1980	1990	1999	2005	2011	2016	2020	2022
Share in global GDP (PPP basis)								
Emerging and Developing Economies	36.4	36.3	42.6	47.3	54.7	58.2	60.8	62.4
Emerging and Developing Asia	9.0	12.5	16.5	20.0	26.7	31.6	35.2	36.9
Advance Economies	63.6	63.7	57.4	52.7	45.3	41.9	39.2	37.6
Share in global GDP (MER basis)								
Emerging and Developing Economies	24.2	21.8	19.6	23.7	36.6	38.8	42.4	44.3
Emerging and Developing Asia	6.8	4.8	6.6	8.7	15.9	21.4	24.3	26.0
Advance Economies	75.8	78.2	80.4	76.3	63.4	61.2	57.6	55.7
Share in IMF Quota								
Emerging and Developing Economies	35.1	34.5	36.0	35.5	36.6	42.4	n.a.	n.a.
Advance Economies	35.7	35.2	37.0	37.5	63.8	57.6	n.a.	n.a.

Note: Data for 2020 and 2022 are IMF predictions.
Source: Author's elaboration based on data extracted from IMF (2017b).

A number of financial crises occurred between 1970 and 2011 (Boorman, 2015), mostly in EDEs, which led to the classification of two different groups among the IMF member countries: first, creditor countries (mainly AEs); second, debtor countries (mainly EDEs). While most of the creditor countries were AEs, the dawn of the NAFC viewed 20 systematic banking crises in the AEs as well since 2008. This led to the need of an institution that could lend a helping hand to the stressed economies and play a leading role in the economic governance worldwide, thus the critical role of the IMF.

There has always been a need for an institution such as the IMF, which could bring stability in times of significant global economic changes such as the introduction of fixed but modifiable exchange rates of gold/dollar standard, since Bretton Woods arrangements collapsed. This need was further accentuated with the introduction of floating exchange rates and free flow of capital, which led to more frequent banking, exchange rate, and sovereign debt crises. Adding to this is the NAFC, which forced European economies to increase their access limits as high as 1000% of quota in the 1990s (IMF, 2016a).

Technological changes in the 1990s and till date have brought a mammoth change in the role of IMF. Free flow of capital and the simultaneous introduction of financial liberalization policies in AEs and EDEs both brought ever bigger sizes of rescue programs. The credit need of even developing countries increased significantly so that the IMF funds have to be supported by European organizations. With the increasing size of EDEs, the probability of the financial crisis in future and growing financial dependence of economies on each other, whether of developing or developed countries, the importance of the IMF cannot be ruled out.

The IMF played a vital role in the resolution of many crises: primarily, the 1980s debt crises in Latin America and then the 1990s Asian crisis brought stillness in the global economy. The level of contentment increased, and there was an oversight in the observation of the world economy that led to the NAFC. As a result, the IMF alternatively arranged huge borrowings through the New Arrangements to Borrow (NAB) and subsequently from Bilateral Arrangements (Mohan and Kapur, 2015).

It is therefore clear that the role of the IMF increasingly will become more dominant in the near future with the rapid changes in the world economy. Equally important is the fact that the EDEs should be provided more powers in the IMF; it can be in terms of quota or in voice in the executive board. However, despite the fact that developing countries should be provided their due share, the U.S. dominance will continue with respect to economic weight owing to its superior institutions leaving the Europe way behind.

3. IMF QUOTA HISTORY AND GOVERNANCE REFORM

The history of Quota system started when the founding fathers of IMFs intended to include involvement so that the world economic structure might be monitored more effectively in the unbiased method. Nevertheless, it took almost six decades to achieve this purpose of inclusive membership. In 1944, 40 members were the members of the IMF, which increased to more than triple fold in the late 1970s, with the continuing dominance of the established nations and the joining of autonomous African nations. Hence, the significant growth in membership had been witnessed till early 1990s making IMF a globally known institution with worldwide membership, but there was no proportionate change in the institutional overall governance.

The quota system in the IMF works in a fashion that a specific quota is allocated to each member of the fund that later defines the borrowing capacity and voting power of that member. In addition, the fund is managed in a manner that the allocated quotas are likely to offer enduring and adequate resources for granting. Since its commencement, formulae have been used while assigning quotas to members and have been constantly revised periodically. Moreover, the formulae are generally worked as initial ideas, and the value of real quota differs from the allocated one. Meanwhile, for subsets of members, the system also implemented selective and ad hoc increases. The quota formulae used in allocating funds become cumbersome over the period of time because of the increased number of formulae in the next three to four decades. In 1983, the formulae count reduced to five, thus, reducing the complexity of the quota system up to some extent. This complication continued till the IMF board agreed to apply new comparatively modest formula in 2008 (source: author’s elaboration based on data is extracted from Box 2, IMF, 2000, pp. 15-16 and Box 2, IMF, 2016a, p. 22). Although, the current formula is easy and simple to understand, it still suffers from major flaws that have been highlighted later in this paper.

The quotas initially in 1944 were assigned through ex ante mechanism rather than based on original formula (Mirakhor and Zaidi, 2006) and the ex post mechanism where the quota formula was established to justify the assigned quotas (Virmani and Patra, 2011). The current U.S. President Roosevelt instructed his treasury staff to modify the formula in such a way that the formula favors the US in grabbing the largest quotas from its three major allies (United Kingdom (UK), Union of Soviet Socialist Republics (USSR), and China).[1] One of the primary purposes of the quota formula was basically to weaken the influence of the US in the global economy and thus ensuring that the quota limit must be allocated broadly so as to make IMF more appealing in the global platform (Mohan and Kapur, 2015). Despite this, many equally positioned countries have different quota shares which in turn created dissatisfaction among the delegations regarding the allocation done and *hence, a need for revision in the present structure of quota formula is warranted.*

As the borrowing limits and the withdrawal needs were connected to the members’ quota shares, their relative importance was increased over time. In the late 1960s, the noteworthy change assumed in the quota shares was when SDRs were introduced and connected to the quotas (de Vries, 1976). More essentially, the continuing determined change in the economy, in particular GDP) among the members of the fund, led to claim for a further strong modification in the relative members quota shares. It can be observed that earlier in 1960s the rapidly developing countries such as Japan and Germany had contributed more in the global GDP and had more quota shares earlier rather than the slowly developing countries such as India and China. Nevertheless, the scenario has now been witnessing the reverse with EDEs, in particular Emerging and Developing Asia (EDAs), growing rapidly and outperforming the AEs (Table 1).

[1] “In mid-April 1943, shortly after the White plan was made public, White called me to his office and asked that I prepare a formula for the ISF [International Stabilization Fund] quotas that would be based on the members’ gold and dollar holdings, national incomes, and foreign trade. He gave no instructions on the weights to be used, but I was to give the United States a quota of approximately $2.9 billion; the United Kingdom (including its colonies), about half the U .S. quota; the Soviet Union, an amount just under that of the United Kingdom; and China, somewhat less. He also wanted the total of the quotas to be about $10 billion. White’s major concern was that our military allies (President Roosevelt’s Big Four) should have the largest quotas, with a ranking on which the president and the secretary of state had agreed. I was surprised that White did not mention France, which was usually regarded as being third in economic importance among the Allied powers. He said he did not care where France ranked, and its ranking did not need to be an objective in the exercise.” (Mikesell, 1994, p. 22)

Furthermore, besides the allocation of members' quota shares, all the fourteen general reviews held had a healthy discussion on the amount of the quota resources. Necessity for the increased quotas resources has been warranted as the world economy perceiving enormous growth since the last two decades. In addition, it has been suggested in every successive reviews that the AEs preferred a very less increase (say 20-40%) in the overall amount of the quota resources allocated for multiple causes: worldwide presence of private markets; restrictions on ability to be responsible for resources by their own, and they may be the cause for any inflationary part in the world economy. In contrary, the EDEs favored a comparatively more increase in the overall amount of the quota resources (say 80-95%) as the developing economies require more external financial assistance if they suffer from any possible crisis from increasing trade and economic interdependence (de Vries, 1976, 1985). It can be well said with respect to quota resources in the IMF that the potential borrower economies normally sought large amount whereas the creditor economies tried to resist them.

During almost two decades of its existence, there was generally no increase in the quotas of the Fund. Some modest changes that occurred in the 1960s were also distributed in proportion to the existing quotas. With countries such as Japan and Germany gaining relative weight in the global economy, it was demanded to reflect this in the form of increase in quotas during the 1959. The mammoth task ahead of the IMF in the fifth general review was to strike a balance between the demands of EDEs and that of fast growing economies.

The sixth general review witnessed the 33.6% increase in the quota share, much demanded from the developing economies to protect their shares. This led to a more improvised methodology in quota allocation and moved the attention toward quota formula and its variables (de Vries, 1976). The US has always been a dominant power in the quota share. However, during the 1970s, its share had dropped from 33.5% in 1946 to 23% but that did not affect in any way its veto power over key fund decisions. "U.S. officials argued that the United States needed some margin to retain at least 20 percent of voting power. U.S. officials argued, too, that lowering the voting power of the United States to below 20 percent of the total might well lower the commitment to the Fund by the U.S. government and even by the U.S. public at large, which would be contrary to the interests of the Fund itself" (de Vries, 1985, p. 521). This led to augment the majority required for special voting from 80 to 85% in the Second Amendment to the Articles in 1978, thus empowering veto at 15%.

The seventh review witnessed 51% increase in the quotas mostly in proportion to their present status with selective increase of 1% for only 11 EDEs who had a fewer shares as compared to their calculated quota shares (CQSs). The eighth review with 48% increase in the overall quota was tilted more regarding selective growth (29%) rather than an equiproportionate growth (19%). After that the ninth review in June 1990 also noticed a 50% increase in the overall quotas slanted more toward equiproportionate increase (30%) than the selective one (20%). After that, there had been no change in the overall quota share in the tenth general review conducted in 1995. The eleventh review (1998) also led to an equiproportionate distribution of an increase of 45% in the quotas. Despite the rapid growth in the EDEs after 2000, there had been no change in the overall quota as well as relative quota positions in the two successive reviews—twelfth in 2003 and thirteenth in 2008.

The rapid growth in the EDEs brought into light the mismatch between their quota shares and economic weight (Table 1), and thus 54 countries had an ad hoc increment in their quota shares in 2006 and 2008. This trend also continued in the fourteenth review, where, as a result of NAFC, the IMF's total quota resources for the first time increased by 100% after a lag of 13 years. However, unfortunately even with prominent increase in gross capital inflows and outflows and a notable increase in trade, the increase in Fund's quota resources did not fare well in relation to global economy. Adding onto this, the delays in the implementation further nullified its effect.

After the enforcement of the fourteenth review in January 2016, the marginal increase of 3% (39.6-42.4%) has been observed in the EDEs' member quota share. The fourteenth review marks a change in representation in the governance board and the initiation of quota reviews in a comprehensive manner (January 2013). Hopefully, the fifteenth Review expected to emerge in 2019 will witness a new quota formula with the executive board working expeditiously on it in accordance with its understandings and the guidance provided by the IMFC (IMF, 2016b).

There is an ever increasing gap between the relative weight of EDEs in the world economy and their state in the global governance, almost 15% points to be specific (IMF, 2017b). Hence, the conservative

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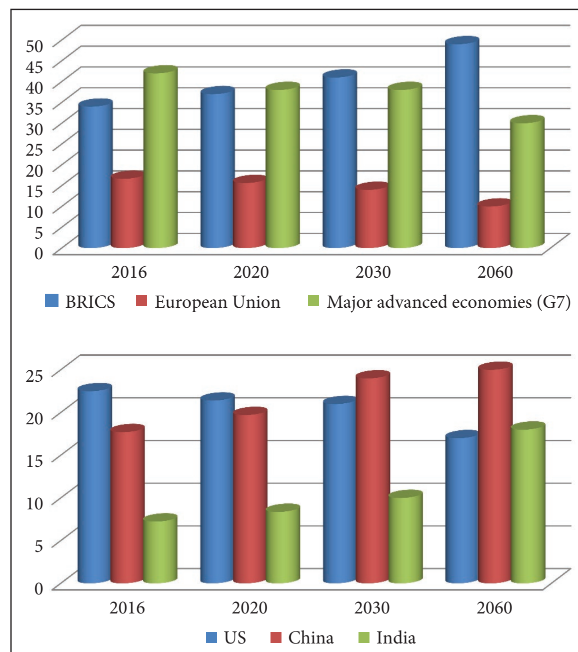
Figure 4. Forecasted Structure of the World Economy (2016-2060).



Source: Author's elaboration based on data extracted from OECD (2017).

approach till now followed in adjustment of quotas and delays in bringing them into effect and with some solemn faults in the prevailing quota formula, and this gap is likely to broaden in future.

Long-term forecasts from the OECD specify further prominence of these trends in favor of the EDEs[2] (Figure 4). As the economies of both G7 and BRICS have sustained rapid growth, even then the BRICS share in global GDP (34%) have 8% less than that of G7 (42%). In addition, OECD (2017) forecasts that by the end of 2022, the cumulative share in the global GDP of BRICS would surpass the same of G7. Further by 2060, the OECD estimates 49% increment in the share of BRICS, whereas the same of G7 would decrease to 30%. The OECD also estimates that, by the end of 2020, the individual share of China in world GDP would surpass the same of the US and it continues further and by the end of 2060, China's GDP (17%) would be 8% more than that of the US (25%). Most importantly, the OECD (2017) report also estimates that, by the end of 2060, India's individual share in global GDP (18%) would surpass the same of the US (17%) by 1% (Figure 4). Consequently, if these OECD (2017) forecasts come out to be precise, the world economic framework would definitely be palpably different from todays' position. Moreover, this change in the framework would be accepted by the world economic governance. Nonetheless, as all these estimates are imprecise, the question always haunts whether the high past growth sustained in future or not?[3]

3.1. Necessity of Revision in Present Quota Formula

Quota shares were considered instead of EDEs with an equally supportive equation and effective factors that are marked as remarkable alternative, where GDP was taken as the prime element. Prior to the quota

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[2] There may be difference between data from OECD (2017) and the same from (IMF, 2017b).

[3] "As Pritchett and Lawrence (2014) argue, abnormally rapid growth is rarely persistent; regression to the mean is empirically the most salient feature of economic growth. In developing countries, episodes of rapid growth are frequently punctuated by discontinuous drop-offs in growth and accordingly, these authors expect that growth in China and India will be much less rapid than is currently anticipated. We are, for example, witnessing a marked slowdown in EDE growth at the present time, including the BRICS countries"

share consideration, the PPP GDP statistics was questioned regarding the quality aspects, which were verified by the Fund staff and also were declared optimum to be implemented in the quota formula as per IMF statistics (IMF, 2014a, 2014b, 2015). Conceptually, 40% at PPP and 60% for GDP at MER were taken as weights for PPP GDP in the formula. The inclusion of PPP in GDP rather assisted the low income nations to have their say heard in the governance aspect (IMF, 2016a).

The GDP (PPP basis) formula was inclusive of a major drawback, in particular openness variable. In the present scenario, GDP and country size in the trade openness variable is inversely related. Though being openness variable has no link or reflection to the world`s economic and financial framework, this drawback had positive impact on the nation small in size as compared to a large economy. In addition, the drawback persists despite the policies relating to trade and external affairs are equivalent both to small and large economy. According to the World Bank report in 2014, the U.S. economy in the world (as measured by trade-to-GDP ratio) was well behind than that of Sweden, Finland, Norway, and even India! This biasness of openness variable has been experienced by euro countries as well. Hence, the change in the quota formula with respect to openness variable requires significant attention and responded adequately either by minimizing (the variable impact should favor the GDP blend) or by eliminating it fully, but the change according to the IMF report on quota data updates revealed that the openness variable continued to play significant role in the formula (IMF, 2016a).

The variability in current receipts and net capital flows is the third variable in the quota formula. The IMF fund staff itself acknowledged two major issues related to this context: first, there is a weak relationship among the variability and BOP needs; second, the increase in share for PPP GDP as compared to market GDP will benefit almost all countries placed in the bottommost part (measures in terms of income distribution), and their relative gains will also increase up to the maximum (Mohan and Kapur, 2015). Furthermore, the size does not play any significant role if the share of PPP GDP becomes high whereas gains from openness variable gets benefited as income is positively related to openness (IMF, 2014a, 2014b, 2015). Hence, the above findings conclude that the “variability” variable should be dropped in the next review and the increment weight in the PPP GDP share would largely be supportive to the low-income countries. This suggestion for dropping “variability” variable from the formula received considerable support but not yet removed with the major concern on how the portion of this variable is reallocated? (IMF, 2016a)

It can be noteworthy that a higher shift in the portion GDP variable will definitely help the US directly; else their CQS (under the current formula) might decline up to the level below the veto controlling threshold (currently 15%). Furthermore, the EDEs relative growth and the decrease in the U.S. quota shares from 19% in 2005 to 14.3% in 2014 (source: author’s elaboration based on data extracted from Table 1a, p. 9, IMF, 2016a), led EDEs to raise their voice in the governance of the IMF. Moreover, these issues become prominent at present, and this remains questionable that in coming years how this issue is addressed: Will there be any adjustment made in the articles to increase the voting shares of the super powers such as the US and the EU or will there be change in the existing quota formula such as shifting of weight toward GDP variable, or Will US let go its veto power?

Finally, the present quota formula is lagging since its inception, and the delays in implementation worsened the effect of these lags. For illustration, the fifteenth review meeting that is proposed to be completed by the 2017 Annual Meetings (IMF, 2016b) have to use the data available up to 2015. The noticeable point here is that the current formula applied three-year averages for the GDP variable. Therefore, in the fifteenth review, following the same averaging practice, the GDP variable thus should be calculated by averaging the values of 2013, 2014, and 2015. It can be noteworthy that the persistent growth of EDEs (almost 11% increase from 47.2 to 58.3%) with respect to AEs in the last decade portrays the backward look of the present quota formula. Further to address this issue, the following possibilities can be considered: first, instead of using three-year averages, the data for the latest year can be used for GDP variable; second, the proportionate weighted average for the last three years can also be used to compute the GDP with higher weight to the latest year data and less weights to the two foregoing years accordingly; and lastly, the two-years moving average can also be used, with more weight to the latest year. Meanwhile, the existing quota formula effectually relates to the dissemination of added quota resources, there is substantial change in the effect causing in the development of increasing voice in the IMF. As in the current scenario, for any IMF member, no arrangement has been set for decrease in the entire quotas. Thus, it can be said that such substantial change necessitates great value in delivering permanence in the governance of the IMF.

It can be noteworthy that since 1998 and prior to fourteenth general review (100% increase in quota resources) the IMF quota resources remain unaltered, although only nominal ad hoc increment was conducted in year 2006 and 2008. The period between 1998 and 2008 witnessed both the enormous growth in the world economy as well as the subsequent great recession. Furthermore, keeping in mind the fragile nature of the global economy and the repercussions of the NAFC, the size of IMF programs has also been on the governing part with respect to GDPs or quotas. Therefore, one could easily implicit that any increase in the IMF quota resources exposed the high importance of super powers in the world economic governance.

The aforementioned improvements have greater consequences for the legitimacy and integrity of the Fund. Hence, for the Fund to implement its activities, resourced should be sufficient, and it should have efficacy and reliability, and its governance framework should be afar criticism.

4. ROLE OF EDES IN GOVERNANCE IN DIVERSE GROUPS

The members of the executive board in the IMF have been changed due to rearrangements made in the quotas. During the first few years since the IMF inception, India and China were among the top five largest quotas countries. Consequently, both of them were authorized to "appoint" their individual Directors. It can be noteworthy that the number of representation of nonindustrial countries, as Executive Directors in the Board, has been nearly half although they have only 31% voting power (Boughton, 2001). India, due to its lethargic growth, lost its "appointed" prominence in the fifth general review (1970) before the quota amendment came into force in 1972. Moreover, due to its enormous growth performance, Japan took the appointed chair of India. Later on, India regained its position as "elected" seat in the Board (Table 2).

Despite the enormous growth of EDEs observed in the early 1990s in the world economy, it has been continuously argued that the two major global institutions namely the World Bank and the IMF governance have been ruled by the AEs, more specially by the European Union (hereafter EU). The dominance can be understood by the fact that every third chair in the Board is governed by the member of the "Advanced Europe" group (EU, Switzerland, and Norway), and hence their voting power rights were more than a third

Table 2. Quotas Distribution since Inception.

"Country	1948	1959	1966	1970	1978	1980	1983	1992	1999	2011	2016
Quota share (percent to total)											
United States	32.5	28.4	24.3	23.1	21.2	21.2	20.2	18.8	17.7	17.7	17.4
Japan		3.4	3.4	4.1	4.2	4.2	4.8	5.8	6.3	6.6	6.5
China, P.R.: Mainland						3.0	2.7	2.4	2.2	4.0	6.4
Germany		5.4	5.7	5.5	5.4	5.4	6.1	5.8	6.2	6.1	5.6
United Kingdom	15.4	13.4	11.5	9.7	7.4	7.4	7.0	5.2	5.1	4.5	4.2
France	6.2	5.4	4.6	5.2	4.9	4.8	5.1	5.2	5.1	4.5	4.2
Italy	2.1	1.9	2.9	3.5	3.1	3.1	3.3	3.2	3.4	3.3	3.2
India	4.7	4.1	3.5	3.2	2.9	2.9	2.5	2.2	2.0	2.4	2.7
Russia								3.1	2.8	2.5	2.7
Brazil	1.8	1.0	1.7	1.5	1.7	1.7	1.7	1.5	1.4	1.8	2.3
Canada	3.5	3.8	3.5	3.8	3.4	3.4	3.3	3.1	3.0	2.7	2.3
Saudi Arabia		0.1	0.4	0.3	1.5	1.7	3.6	2.3	3.3	2.9	2.1

Continued

Table 2. *Continued*

"Country	1948	1959	1966	1970	1978	1980	1983	1992	1999	2011	2016
Spain		0.7	1.2	1.4	1.4	1.4	1.5	1.4	1.5	1.7	2.0
Mexico	1.1	1.2	1.3	1.3	1.4	1.3	1.3	1.2	1.2	1.5	1.9
Netherlands	3.3	2.8	2.5	2.4	2.4	2.4	2.6	2.4	2.5	2.2	1.8
Korea, Republic of		0.1	0.1	0.2	0.4	0.4	0.5	0.6	0.8	1.4	1.8
Australia	2.4	2.1	2.4	2.3	2.0	2.0	1.8	1.7	1.5	1.4	1.4
Belgium	2.7	2.3	2.0	2.2	2.2	2.2	2.4	2.2	2.2	1.9	1.3
Switzerland								1.7	1.6	1.5	1.2
Rank											
United States	1	1	1	1	1	1	1	1	1	1	1
Japan		7	7	5	5	5	5	2	2	2	2
China, P.R.: Mainland						8	9	10	11	6	3
Germany		3	3	3	3	3	3	2	3	3	4
United Kingdom	2	2	2	2	2	2	2	4	4	4	5
France	3	3	4	4	4	4	4	4	4	4	5
Italy	9	12	8	7	7	7	8	6	6	7	7
India	4	5	5	8	8	9	11	13	13	11	8
Russia								8	9	10	9
Brazil	10	15	12	12	12	14	14	16	17	14	10
Canada	5	6	6	6	6	6	7	7	8	9	11
Saudi Arabia		54	32	44	15	13	6	11	7	8	12
Spain		19	15	14	16	16	16	18	16	15	13
Mexico	12	13	14	15	17	17	17	19	19	16	14
Netherlands	6	8	9	9	9	10	10	9	10	12	15
Korea, Republic of		49	67	56	44	44	35	35	28	18	16
Australia	8	10	10	10	11	12	13	15	15	19	17
Belgium	7	9	11	11	10	11	12	12	12	13	18
Switzerland"								14	14	17	19

Note: The table encompasses top 20 countries with leading quota shares (as per 2010 reforms).
Source: Author's elaboration based on the data extracted from IMF (2016a).

on the Board (Mohan and Kapur, 2015). According to the IMF report, the share of these European countries in the world economy specifies a continuous and steady downfall; even then they have high shares in the quotas (IMF, 2016a).

The G-20 forum, which comprises a number of developing economies, served as a better platform to showcase the continuous increasing performance of EDEs since the 1990s in the world economy. With member countries holding more than 80% of global GDP, its only drawback lies in having insufficient

representation from Africa. Although the Bretton Woods institutions failed to adequately represent EDEs in their governance structure in the last six decades, things are slowly getting better. These changes are mandatory if it has to retain its credibility and to cope up with the legality of the issues it is dealing with.

There has been a general trend for almost seven decades now that the U.S. nationals ruled the World Bank, whereas the IMF is headed by the European nationals since their origin. In some aspect, it provides judgment that there should be an informal agreement for the same (Boughton, 2001). Despite the fact that GATT was headed by European nationals since their inception, its successor WTO is an exception to this nationality-based rule. This does not in many manners defy the proficiency of past heads of IMF but draws attention toward this reality that other members, including EDEs, could also provide to equally valuable leaders. It is high time now that the selection of the head of these global institutions should be made transparent so as to increase its legality and to counter the thought that only major developed economies can run the Fund (Kenen, 2007).

5. CONCLUSION

Currently, the IMF and the world economic power worldwide must go hand. With the growth in global GDP, the world economy has developed considerably, combined and mutually, in such a way that a little change in the economy of one country can be a cause of multiple changes in the global economy. The loans provided to Greece to save its economy in 2010, 2012, and 2015 vouch the statement effectively. Therefore, the most challenging task in the years to come is to maintain financial stability across the world by focusing on effective financial regulation. This becomes mandatory if the global economy should be saved from the fallouts of financial crisis that might occur in the future.

NAFC, which led to the Great Recession, has put a huge pressure on the IMF resources and accentuated the need to bring about reforms in the IMF. The reforms can take place in two ways: first, increase in quota resources in tandem with its share in global economy; second, equal distribution of voting powers in its governance structure. According to Truman (2015, p. 2), "The world needs the IMF to function for the benefit of strong and troubled counties alike. Its participation in the stabilization programs for countries in financial crisis in Europe from Ireland to Ukraine was only the most recent example of its indispensable role. But China and other countries have grown vary of the Fund's governance because they see it as failing to recognise their increasing importance in the world economy."

The formation of BRICS Bank (a $100 billion New Development Bank), BRICS' Contingent Reserve Arrangement (CRA) by the BRICS countries, and the AIIB majorly led by China are the sign of the dissatisfaction of EDEs with the present structure of global governance. So much is the deadlock in the quota increase that the IMF has to resort to borrowed resources to such unparalleled level that its own resources of SDR 475 billion (about US$ 675 billion) constitutes nearly 60% of the total possible fund accessible to the IMF. If at any point of time the situation arises to use a major chunk of borrowed resources, the IMF would come under much financial distress. With the increasingly growing size of IMF programs post NAFC and European sovereign debt crisis, its own financial trustworthiness is at greater risk. With ever-growing interdependency of economies, by the seventeenth review (2025), IMF should have increased its permanent resources (mostly quotas) to an amount of about US$ 1.25 trillion (Truman, 2015).

An important factor in determining the shares of economies in the global scenario, along with their per capita income, is the level of sophistication in their soft power, which unfortunately in case of EDEs is not rising in proportion to developed countries such as the US. However, this does not warrant delaying the process of realignment of quotas in any manner, knowing the fact that the US would not suffer in any case by the same. The US, being far superior to EDEs in terms of the efficient financial markets, will continue to provide headship even if the current quota system is modified in favor of EDEs. Knowing the fact that the leading reserve denomination across the globe is still the U.S. dollar at present and will continue as such in the subsequent years, the level of trust the US repose in the IMF determines to a large extent its efficacy and credit standing.

The upcoming fifteenth and the future reviews of IMF quotas should be vital with respect to the representation of EDEs in their governance. Although there is a disparity between EDEs, in particular BRICS, economic weight, and their relative shares, the major victim of this mismatch is the US itself. The share of

the US in the global GDP is analogous to that of the EU. But its CQS as per latest 2014 data is 13.1% less than that of the EU (IMF, 2017b). The same has been argued by Truman (2008, p. 6), "....until the Europeans agree to a substantial reduction of their combined voting share in the IMF from the current EU share of more than 30 per cent to something close to the US share, reducing the US voting share below 15 per cent is a non-starter."

It can be noteworthy that, in a broad sense, the combined BRICS shares as per market GDP are comparable to that of the US and the EU, while their quota portions are fairly changed. However, regarding GDP (PPP basis), the BRICS share is significantly high than that of the EU and the US. *Hence, in future, a need for revision in the present structure of quota formula is warranted, which offers a significant weight to GDP shares accompanied by any change in other variables that may be considered essential.*

As acknowledged in the paper, each quota review that took place earlier had very disruptive argument and to reduce the same in subsequent reviews the IMF must give greater thought to inoculating more automaticity with respect to quota resources. A revised formula could be designed in determining the complete IMF quota resources that pay more attention on the appropriate weight of global GDP, on gross trade produced by the concerned economy and on complete financial flows in the world economy.[4] If the IMF could design this formula, it would offer more permanence in terms of size of resources, comparative to the requirements of the world economy, accessible to them. This settlement on the comprehensive principles finally helps in reducing the time consumption in the Board's discussions.

There are serious drawbacks in the current quota formula such as poor PPP-GDP data and a mistaken openness indicator, which should be addressed appropriately to improve the representation issue. This would not be possible without the considerable guidance from the IMF management and the dominant countries in the IMF such as the US and G20.

The change of the century in terms of equitable and fair economic governance is the need of the hour in order to guarantee economic stability across the globe. The period of European and North American supremacy has now come to an end, and adequate measures should be taken to give the rising economies their due place in the global economy.

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[4] "Global output, trade and gross financial flows can be expected to continue with their upward trend and hence the IMF's quota resources need to increase commensurately. Although growth in both AEs and EDEs has slowed down since the NAFC, its [it] remains substantially positive, with growth in EDEs still outpacing that in the AEs. Therefore, the view that the level of global output might not increase in the coming decades (there might only be a shift of global output in favour of the EDEs) and hence there may not be case for an increase in the level of IMF quota resources does not appear to be realistic."

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Reforming the IMF to Increase FDI Led Economic Growth: The Case of Latin American and Caribbean Countries

Ashraf Mahate*
Hamdan bin Mohammed Smart University, Dubai Academic City, P.O. Box 71400, Dubai, UAE.

***Correspondence:** ashrafmahate@gmail.com

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Abstract

There is a strong body of literature that finds a direct connection between inward foreign direct investment and economic growth in the host country. At the same time, economic growth in the host country attracts additional Foreign Direct Investment (FDI). This bidirectional relationship can be supported by the IMF through its lending program to countries to assist in dealing with short-term shocks as well as managing more long-term structural issues. In fact, the IMF programs in theory should provide an indicator to potential investors that the country is committed to making a change and opening its economy, which are typical requirements under IMF conditions. IMF intervention should lead to a positive impact on inward FDI. This study examines the impact of IMF-support programs on inward FDI for a sample of Latin American and Caribbean Countries. The results from this study reveal that being on an IMF borrowing program has a negative impact on inward FDI in the second and third year. We argue that being on an IMF borrowing program does not provide inward FDI with the seal of approval that it requires in making an investment.

Keywords: Foreign Direct Investment; International Monetary Fund; Latin America and Caribbean; Economic Growth.

1. INTRODUCTION

In the post-1970s period, countries worldwide have moved from a hostile stance towards inward foreign direct investment (FDI) to one that is very supportive and intentionally positive. Inward FDI is no longer viewed as parasitic and hindering the development of domestic industries. Instead, inward FDI is considered to have several positive effects to the host country, which includes enhancements in productivity as a result of the introduction of new processes and knowledge, technology transfer, development of local industry, and access to overseas markets (see Bende-Nabende and Ford, 1998; Borensztein *et al.*, 1998; Carkovic and Levine, 2002; De Gregorio, 2003). The prior literature on FDI has two main streams, namely, its impact on trade-related economic growth (Markussen and Vernables, 1998) and economic growth that takes place as a result of enhancing domestic capital through productivity improvements (Borensztein *et al.*, 1998; Driffield, 2001). Whether through trade or productivity or both, there is a strong body of prior studies supporting the linkage between inward investment and economic growth (De Mello, 1997; Borensztein *et al.*, 1998; Glass and Saggi, 1999). In fact, De Gregorio (2003) found that an increase of 1% of inward FDI increased economic growth in the host country by approximately 0.6%.

More recent studies have found that FDI is attracted to countries that have stable and growing economies. Therefore, the argument is that economic policy or growth stimulates inward FDI investment and with it the benefits that accrue from external finance. Economic policy can be assumed to be trade openness, regulatory environment, and labor market factors that attract inward investment (Fedderke and Romm, 2006). The outcomes of economic policy lead to increase in GDP, political and economic stability, and so forth (see Mateev, 2009). Other studies such as Porter (1994), and Dunning have argued that FDI is motivated by location-specific factors. These, in turn, are enhanced through economic policies that promote and encourage business-friendly conditions. For many countries, the implementation of sound economic policies is dependent on their ability to fund short-term shocks as well as longer period structural issues. Harms and Lutz (2006) report that the ability of the host country to finance outflows through an improvement of the balance of payments provided by organizations such as the IMF has a positive impact on FDI attraction. Similarly, programs that enhance the economic and social infrastructure of the host country funded by support

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agencies such as the IMF increase the marginal productivity of external capital (Harms and Lutz, 2006; Kimura and Todo, 2010). Perhaps, the most important aspect of IMF involvement in a country is the fact that it indicates to inward FDI that the host nation has made a public commitment to comply with the conditions.

This study examines the impact of IMF-support programs on inward FDI for Latin American and Caribbean countries (LAC). IMF-support programs have been helpful to countries that have experienced short-term liquidity issues as well as longer period structural problems. However, critics indicate that the repeated usage of IMF-support programs may be indicative of their ineffectiveness in assisting borrower countries. More importantly, critics also indicate that being on an IMF-support program may actually make matters worse for the borrowing country. It is to understand these very issues that we select the LAC countries where there has been a relatively high incidence of IMF-support programs. In addition, the LAC countries have a mix of some very large and developed countries in the world along with small and weak economies. As such, we believe that this diversity allows us to have a better and deeper understanding of the impact of IMF-support programs on host nations and their efficiency in attracting inward FDI.

2. THE FDI ECONOMIC GROWTH LITERATURE REVIEW

FDI has a very long history. However, its importance has gained prominence in the post Second World War period coinciding with the development of the new corporate firm. Post war production has meant that firms have sought to exploit economies of scale that necessitate large consumer markets with multiple distribution channels. In addition, the growth of modern complex global value chains implies that FDI takes place in a variety of different forms from production to research and development. From a corporate viewpoint, FDI has allowed firms to invest in foreign countries in order to secure resources, benefit from cost efficiencies, acquire strategic assets so that they do not fall under the control of a competitor, extend the market share of the parent company, acquire technology, have access to particular skills, and in some cases financing. Therefore, it is not a surprise to see that currently FDI inflows are over US$1.7 trillion or approximately 3% of world GDP (OECD, 2016).

Academic research on FDI studies has identified a number of direct and indirect benefits to the host country. Perhaps, the most important direct benefit of FDI takes the form of an increase in the level of capital formation in the host country that then provides greater employment opportunities and a positive multiplier takes place. Balasubramanyam *et al*. (1996) and Kohpaiboon (2003) find that economic growth in host country takes place when pro-export policies are adopted. Where the host nations implement import substitution policies these studies find a positive but weak impact to the economy. Similar results were found by Basu et al. (2003) as well as Trevino and Upadhyaya (2003) who indicate that trade openness as being an important factor that leads to FDI-induced economic growth. Borensztein *et al*. (1998) as well as Jyun-Yi, Wu, and Hsu Chin-Chiang (2008) find that FDI has a positive impact however its size depends on the quality of the human capital in the host country. Olofsodotter (1998) finds that FDI has a large impact on economic growth through technology transfer which is substantially stronger when the host nation has laws and regulations that protect intellectual property rights. Wu and Hsu (2008) find that FDI has a considerably stronger impact on economic growth when the host nation has a higher level of initial GDP and human capital. At a sectoral level, Wang (2009) found that the impact of FDI on host country economic growth was higher when the inward investment was in the manufacturing areas.

3. THE ROLE OF THE IMF IN FACILITATING ECONOMIC GROWTH

In order to understand the linkage between the IMF programs with economic growth and FDI, it is important to appreciate its role. The functions of the IMF were agreed during the meetings that took place in Bretton Woods in 1944 as follows:

(i) Surveillance function, which (Bordo and James, 2000) claims at "promoting world trade, and securing the general well-being of the world economy, through analysis and advice." The surveillance function can be divided into national country performance reporting and policy dialogue.

In the case of the former, the performance reporting consists of producing economic forecasts. Meanwhile, the latter focuses on having periodic dialogues with member countries in order to enhance their policy decisions.

(ii) Providing credits or the ability to make drawing by member countries. Typically, the credits are made in tranches of 25% of a member's quota.

(iii) Provision of subsidized credit, which was initiated in the 1970s to assist low-income countries that were adversely affected by the increase in oil prices. The costs of the credit subsidy are funded by a trust fund established in the 1970s along with donations and loans from rich member countries.

(iv) The creation of Special Drawing Right (SDRs), which are not technically a currency but represent a reserve asset and held by IMF member countries (IMF, 2014a).

(v) Data, which are the collection and dissemination of country level information in a standardized manner.

(vi) Training and technical assistance, which is aimed at increasing the capacity of some of the weaker members.

Among all the above functions, two functions are of relevance for this study, namely the provision of credits and subsidized loans. There are a number of different ways in which loans are provided to member countries and are as follows:

(i) Stand-by Arrangement (SBA), which was initiated in order to assist countries with their balance of payments issues. Although, the borrowing rates for this credit facility are lower than commercial rates, nevertheless it is considered as a non-concessionary loan. Typically, SBAs are for a year to two years with a limit set at three years. Repayment typically takes place in three to five years after the drawdown of the loan (IMF, 2014b).

(ii) Extended Fund Facility (EFF) like the SBF is also developed to assist countries with their balance of payments problems. However, different from a SBA, an EFF is intended for a longer maturity of between four and ten years and seeks to deal with more complex structural problems that usually may take more time to redress than macroeconomic imbalances. As a part of this program, the IMF seeks to address the country level rigidities in markets and institutions and promote the privatization of state-owned enterprises as well as reforming the financial sector. The SBA and EFF are the main sources of IMF programs for balance of payments issues.

(iii) Flexible Credit Line (FCL) was developed for member countries that have a good record of policy enactment. As such, the IMF does not impose any limits on the loan size or conditions for drawdown. Typically, a FCL extends for one to two years and repayments are made over a three- to five-year period (IMF, 2014b).

(iv) Precautionary and Liquidity Line (PLL) was developed to meet the short-term liquidity requirements of countries that cannot utilize the FCL. The PLL is for a period of six months to two years with a two-year cooling-off period (IMF, 2014b).

(v) Rapid Financing Instrument (RFI) provides a quick solution to countries that need to resolve more pressing balance of payments issues. Typically, RFI is paid over three to five years.

(vi) Trade Integration Mechanism (TIM) was developed to assist member countries dealing with balance of payments issues related to recently implemented trade liberalization measures.

(vii) Extended Credit Facility (ECF), which replaced the Poverty Reduction and Growth Facility (PRGF), is intended for member countries that have more extensive balance of payments problems issues. The ECF offers more concessional and flexible financing terms typically at zero interest rate and payment to start five years after the drawdown.

(viii) Rapid Credit Facility (RCF) is a facility intended for low-income member countries with little in the way of conditionality and intended for urgent balance of payments problems. Similar to the ECF, the RCF has a zero interest rate, and payments start five years after the drawdown.

(ix) Standby Credit Facility (SCF) is intended for low-income countries that experience short-term shocks. As such, it is intended for one- to two-year maturity with an interest rate that is typically at 0.25%. The repayments do not need to start until four years from maturity and can extend to 8 years.

The common thread among all the credit arrangements is to assist member countries to deal with balance of payments issues and help foster economic growth. The IMF has a number of channels to influence economic growth within a member country. In the simplest form, the IMF credit is expected to resolve short- and long-term issues in the economy. However, this viewpoint has been challenged by prior studies such as Boockmann and Dreher (2003) who argue that the receipt of an IMF loan leads the distressed country to assume that the problem has been resolved while this may not be the case. In fact, they argue that it reduces the incentive to carry out changes that may reduce their incentive to reform. Bandow (1994) argues that such a misconception allows the distressed country to continue with existing or misguided policies longer than necessary. Evrensel (2002) finds that budget deficits, inflation rates, and domestic credit tend to be worse in second lending programs compared with the first one. Conway (1994) finds evidence of repeated participation in an IMF lending program rather than one-off assistance. Dreher and Vaubel (2004) showed that economic policy is undeniably more expansive in countries with higher IMF loans available, when compared with the country's undrawn quota with the fund. If the hypothesis that IMF induces moral hazard and bad economic policy is true, then the effect of all this would be the reduced growth (Dreher, 2006).

Perhaps, the most damning criticism of the IMF relates to the conditions that it places on its loans. The IMF conditions seek to bring about changes in the borrower country's economic policies in return for the provision of financial assistance. In theory, the IMF conditions are designed to be a balance between bringing about change yet seeking to ensure the borrower country is able to repay the loan. However, prior studies (see Bird, 2001; Meltzer, 2005) argue that the IMF imposes the same conditions on all borrowers and this "one size fits all" methodology is inappropriate and ineffective. Dreher (2006) argues that owing to the inappropriateness of the IMF conditions, there is a high level of noncompliance and, with it, little positive impact on the economy of the borrower country. One manner in which to enhance economic growth may take place through IMF support is through its technical assistance program (Boockmann and Dreher, 2003). Fischer (2001) claims that the real benefit of the IMF's technical assistance is the long-term benefit from getting countries to think and implement economic policy in a certain manner. As a result, studies such as Dreher (2006) claim that the IMF has a positive impact on economic growth regardless of its conditionality regime.

Prior studies examining the impact of IMF programs on economic growth have employed three different methodologies. The first method is the before–after analysis that considers the levels of economic growth before and after an IMF program has been agreed. The obvious problem with this methodology is that a country entering into an IMF program is experiencing difficulties. Moreover, the benefits may not be immediate as policy actions may take time to materialize (Dreher, 2006). The second method is to compare the countries in the IMF program to a pool of benchmark nations. The idea is that any shock will affect both the borrowing nations as well as the benchmarks. However, the obvious problem is that of identifying an appropriate pool of countries that can serve as a benchmark. The third method is to use statistical techniques such as regression analysis. Przeworski and Vreeland (2000) report that a country's participation in an IMF borrowing program has a negative impact on its economic growth. The study finds that countries on the IMF program experience an economic growth that is on average 2.5% lower than countries not on the IMF program.

From an inward FDI perspective, being on an IMF program should have a positive impact for the borrowing nation as it provides potential investors with a clear message that the country be committed to conducting economic and financial reforms as directed by the IMF. Corsetti *et al*. (2003) argue that the provision of liquidity by the IMF allows private investors to roll over their debt. Bauer *et al*. (2012) find that being on an IMF program has a positive impact on inward FDI only for democratic countries while it has a negative impact in the case of autocratic nations. van der Veer and de Jong (2013) find that inward FDI has a positive bias toward nations that do not default on their IMF obligations. On the other hand, Jensen (2004) finds that being on an IMF program results in a negative impact on inward FDI equivalent to 25% less nations not on the IMF program. Other studies such as Edwards (2006) find that being on an IMF program leads to capital flight. Bird and Rowlands (2007) find that the impact is dependent on the level of debt and negative impact for those with medium to and high levels of indebtedness. On the other hand, for countries with low levels of debt, there was a positive impact on inward FDI.

Table 1 lists the LAC countries along with their membership of the IMF and the number of programs that they have undergone. It appears that the average LAC country became a member of the IMF in 1945 and has over this period received loans under 12.5 different programs. If a typical program is of a three-year

Table 1. List of LAC Countries and Number of IMF Programs since Joining.

Country	GDP in billions US$	GDP per capita in US$	IADB member	Year of joining the IMF	Number of arrangements since membership
Argentina	628.9	14,267.3	Y	1956	20
Bahamas	10.5	27,802.6	Y	1973	0
Barbados	4.8	16,937.6	Y	1970	2
Belize	2.3	5,954.4	Y	1982	1
Bolivia	39.3	3,546.9	Y	1945	19
Brazil	2,140.9	10,308.8	Y	1946	16
Chile	251.2	13,662.9	Y	1945	15
Colombia	306.4	6,216.6	Y	1945	24
Costa Rica	78.8	13,190.1	Y	1946	16
Dominica	0.5	7,621.5	N	1978	5
Dominican Republic	76.9	7,543.0	Y	1945	9
Ecuador	97.4	5,803.3	Y	1945	18
El Salvador	27.5	4,465.9	Y	1946	21
Grenada	1.1	10,126.9	N	1975	8
Guatemala	70.9	4,151.2	Y	1945	15
Guyana	3.6	4,662.3	Y	1966	18
Haiti	9.9	902.8	Y	1953	27
Honduras	21.8	2,623.2	Y	1945	23
Jamaica	14.3	5,017.5	Y	1963	16
Mexico	987.3	7,993.2	Y	1945	15
Nicaragua	13.7	2,115.0	Y	1946	16
Panama	59.5	14,515.4	Y	1946	20
Paraguay	28.7	4,133.6	Y	1945	11
Peru	207.1	6,506.0	Y	1945	25
Saint Kitts and Nevis	1.3	21,971.0	N	1984	1
Saint Lucia	1.6	9,146.5	N	1979	0
Saint Vincent and the Grenadines	0.8	7,342.4	N	1979	0
Suriname	3.6	6,373.5	Y	1978	1
Trinidad and Tobago	27.5	20,444.1	Y	1963	2
Uruguay	58.1	16,638.8	Y	1946	22
Venezuela	251.6	8,004.5	Y	1946	3

Continued

Table 1. *Continued*

Country	GDP in billions US$	GDP per capita in US$	IADB member	Year of joining the IMF	Number of arrangements since membership
Mean	175.1	9,354.5			12.5
Mode	27.5			1945	16
Median	27.5	7,543.0		1946	15
Minimum	0.5	902.8		1945	0.0
Maximum	2,140.9	27,802.6		1984	27.0

Source: https://www.imf.org/external/pubs/ft/weo/2017/01/weodata/weorept.aspx for nominal GDP data and http://www.imf.org/en/Countries/ARG for date of joining the IMF and programs.
Note: Cuba is excluded as it voluntarily left the IMF in 1964 and Antigua and Barbuda, because it is not a member of the IMF.

maturity, it implies that for half the membership period an average LAC country has been under an IMF program. For some LAC countries, the experience has been far worse with the highest number of programs at 27 for Haiti. The most common number of programs has been 16 while the median is 15. On the other extreme, only three of the 31 LAC countries in the sample have not participated in any type of IMF borrowing arrangement. Interestingly, these three countries are very tiny islands of Bahamas, Saint Vincent, and Saint Lucia. Table 1 shows no relationship between the length of IMF membership and the number of financing programs that a country conducts. Similarly, there is very little relationship between the GDP or the GDP per capita and the number of IMF arrangements that have been initiated. It is interesting that Haiti with a per capita GDP of US$902 has initiated 27 IMF programs, whereas Uruguay with a per capita GDP of US$16,638 has 22 arrangements. The two countries are with very different per capital GDPs but rather similar number of IMF borrowing programs.

3.1. Development of Testable Hypotheses

Based on our discussion of the literature and the rationale of the IMF lending programs, we argue that IMF participation should have a beneficial impact on the host country and thus should lead to a greater level of FDSI inflows. As a result, we develop into testable hypotheses for the LAC countries in the following manner:

H^0_1: Participation in an IMF financing program has a positive impact on the level of host country FDI inflows.
H^1_1: Participation in an IMF financing program do not have a positive impact on the level host country FDI inflows.

In order to understand the lagged importance of participation in an IMF financing programme the following hypotheses are developed:

H^0_2: Participation in an IMF financing programme have a positive impact on the level of host country FDI inflows one year after the start of the arrangement.
H^1_2: Participation in an IMF financing programme do not have a positive impact on the level host country FDI inflowsone year after the start of the arrangement.

H^0_3: Participation in an IMF financing program has a positive impact on the level of host country FDI inflows two years after the start of the arrangement.
H^1_3: Participation in an IMF financing program do not have a positive impact on the level host country FDI inflows two years after the start of the arrangement.

4. TRENDS IN FDI IN THE LAC COUNTRIES

Statistics produced by UNCTAD (2017) show that global FDI has experienced a mixed picture over the last decade. There was a period of growth until the International Financial Crisis in 2007 recovering slightly from 2010 onwards. However, the weak global economic performance and very low levels of growth in international trade have dampened FDI flows. Developing countries have experienced the sharpest decline in FDI inflows as from 2015. The regional FDI inflows in 2016 compared to 2015 shows Europe to have experienced the greatest decline at 29% followed by developing countries in Asia and Oceania at 22% and Latin America and the Caribbean (LAC) with 19%. Interestingly, transition economies experienced an increase in FDI inflows of 38%, as did North America and other developed nations at 6 and 139%, respectively. Over the last 25 years, the LAC region has experienced two periods of an increase and one decline in FDI. The periods of increase were from 1990 to 1999 and then 2003 to 2011 while the decline took place between 1999 and 2003. Overall, FDI inflows into LAC have tended to be approximately 3.5% of GDP; however, the distribution is not equal and with 2.5% of GDP for Mexico and 10% for both Chile and Panama. In addition, the volume of FDI is not equal and heavyweight economies such as Brazil account for 42% of all FDI inflows into the LAC region. The main source of FDI inflows into the LAC region is the United States accounting for 26%. However, in the case of some LAC countries such as Mexico, the United States is an important investing nation accounting for 52% of the investment inflows. Other important investing nations into the LAC region are the Netherlands at 16% and Spain with 12%.

At a country level, Brazil is not only the largest economy in the LAC region but the greatest recipient of FDI inflows with US$96,895 billion in 2015 compared to US$ 75,075 billion in 2014. Way behind Brazil come Chile, Colombia, and Argentina. The Central American region experienced an increase of 6% in FDI inflows with Panama being the most important accounting for 43% of the subregional figure. Other significant subregional recipients are Costa Rica at 26%, Honduras at 10%, and Guatemala with 10%. Interestingly, four countries account for approximately 90% of the subregional FDI inflows. The Dominican Republic is the largest recipient of FDI inflows within the Caribbean subregion at 39% of the total followed by Trinidad and Tobago at 20% and Jamaica at 13%. These three countries account for three quarters of all the FDI inflows into the subregion.

5. DATA AND METHODOLOGY

This study employs annual data for the 31 LAC countries over the period 1993 to 2015. We have excluded Cuba as it left the IMF in 1964 and Antigua and Barbuda because it is not a member. Country-level data are obtained from the World Bank's World Development Indicators database.[1] To examine the link between FDI flows and IMF lending programs, we estimate the following model:

$$\text{FDI flowsi,t} = \alpha \text{ IMF programsi,t} + \text{IMF programsi,t} + 1 + \text{IMF programsi,t} + 2 + \beta \text{ Control Variablesi,t} + \varepsilon\text{i,t}$$

where FDI flowsi,t is the measure of FDI flows; IMF programsi,t is a dummy variable used as proxy for the existence of an IMF lending program; to incorporate the lag impact we also use t = 1 and t + 2, Control Variablesi,t is a vector of controls, εi,t is an error term; i = 1, ..., N represents the country; and t = 1, ..., T represents time. Finally, α is the coefficient of interest to us, and it measures the effect of IMF programs on FDI flows.

Consistent with prior literature, our main dependent variable is FDI flows which is measured in US$. The World Bank's definition of FDI is "the net inflows of investment to acquire a lasting management interest (10 percent or more of voting stock) in an enterprise operating in an economy other than that of the investor" (World Bank, 2015). Table 2 provides an overview of variables employed in this study whereby the presence of an IMF facility is represented by a dummy variable equal to one if a country (i) has had an arrangement in effect for at least 5 months in a particular year (t). We argue that the impact of an IMF arrangement on FDI may not be immediate and can take up to three years; therefore, we also use a dummy variable for the

[1] We are grateful to Axel Dreher for making the data available on his webpage.

Table 2. Variable Definition and Sources.

Variable (abbreviation)	Definition (according to data provider)	Source
FDI flows in US$	Foreign direct investment, net inflows (BoP, current US$)	World Development Indicators, World Bank Data code: BX.KLT.DINV.CD.WD
IMF Program Year 1 (IMF1)	Dummy variable set equal to 1 if a country is under an IMF program in that year	Dreher (2006)
IMF Program Year 2 (IMF2)	Dummy variable set equal to 1 if a country is under an IMF program in the previous year	Dreher (2006)
IMF Program Year 3 (IMF3)	Dummy variable set equal to 1 if a country is under an IMF program two years ago	Dreher (2006)
Inflation (INF)	Inflation (annual %) as measured by the consumer price index reflects the annual percentage change in the cost to the average consumer	World Development Indicators, World Bank Data code: FP.CPI.TOTL.ZG
Exchange rate (EXCH)	Purchasing power parity conversion factor is the number of units of a country's currency required to buy the same amount of goods and services in the domestic market as a U.S. dollar would buy in the United States	World Development Indicators, World Bank Data code: PA.NUS.PPPC.RF
Tariffs (TARIFFS)	Simple mean bound rate is the unweighted average of all the lines in the tariff schedule in which bound rates have been set.	World Development Indicators, World Bank Data code: TM.TAX.MRCH.BR.ZS
Taxes (TAXES)	Taxes on income, profits, and capital gains are levied on the actual or presumptive net income of individuals, on the profits of corporations and enterprises, and on capital gains	World Development Indicators, World Bank Data code: GC.TAX.YPKG.ZS

lag years 2 and 3, which has the same value as year 1. We focus our attention on the key programs namely the Stand-by Arrangement (SBA), the Extended Fund Facility (EFF), the Extended Credit Facility (ECF), the Precautionary and Liquidity Line (PLL), and the Flexible Credit Line (FCL).

We appreciate that, being on an IMF program is an important indicator for inward investment however to incorporate the complicated nature of FDI decision-making within a modern firm, we also incorporate certain control variables. Our literature review highlights the importance of trade openness, and therefore we use a measure of trade restrictions in the form tariffs. This is a charge on the quantity of the product imported into the host nation. Tariffs are imposed to generate revenue but more commonly to protect the domestic industry (Gamberoni and Newfarmer, 2009). With the presence of tariffs, exporting to the country may become expensive and uncompetitive. Hence, FDI may be motivated to bypass these restrictions and establish a presence in the host country. This form of FDI is often referred to as tariff jumping FDI. Blogigen and Figlio (1998) and Blonigen (2002) among others find evidence to support tariff jumping FDI to take place.

A key consideration for inward investment is the rate of return on an investment after taxation. An early study that examined the impact of taxation on FDI was by Hartman (1984). Moreover, this study looked at after-tax rate of return on US investment for foreign investors, the gross rate of return on investment after United States, and the relative tax rates between host countries. The study found a strong and positive impact of the tax rate on FDI. Similar results were found by Boskin and Gale (1987), Young (1988), Murthy (1989), Grubert and Mutti (1991), Hines and Rice (1994), Gorter and Parikh (2000), and Benassy-Quere *et al.* (2001); all find evidence to show a statistically significant impact of tax on FDI.

Table 3. Summary Statistics.

	FDI	IMF1	IMF2	IMF3	INF	EXC	TARIFF	TAXES
Mean	1,925,689,591	0.31	0.31	0.31	73.66	0.53	41.01	27.47
Mode	2,800,000	0.00	0.00	0.00			39.98	22.70
Median	100,775,000	0.00	0.00	0.00	7.71	0.51	36.63	25.88
Minimum	(1,891,033,844)	0.00	0.00	0.00	−11.45	0.13	17.61	3.17
Maximum	101,157,817,518	1.00	1.00	1.00	11,749.64	1.11	78.25	72.31
Std dev	7,635,653,684	0.46	0.46	0.46	597.72	0.18	14.85	11.30

Any form of FDI involves the process of converting currency from the home country to that of the host nation. As such, an important consideration for FDI is the current conversion rate as well as the volatility of the future repatriation of profits. Froot and Stein (1991), Stevens (1993), and Blonigen (1997) find that a depreciation in the host country exchange rate increases the level of FDI. However, this also impacts the future profits. Moreover, Campa (1993), Tomlin (2000), and Chakrabarti and Scholnick (2002) find that a depreciation in the host country currency reduces the level of FDI. Chen *et al.* (2006) examines not only the level of FDI but also the motivation namely market-oriented that is to capitalize on the market size of the host nation and cost-oriented FDI that seeks to benefit from lower costs in the country. Chen (2006) finds that expected weakening in the host country currency exhibits a negative impact for market-seeking FDI, whereas it was positive for cost-oriented investment.

The data for this study cover the period 1970 to 2013, and the summary statistics are presented in Table 3. The LAC countries show a wide contrast in FDI experience with inflows of over US$100 billion with capital flight approaching US$2 billion. The mixed performance is representative of the huge diversity between the 31 countries as well as the experiences over the 43 years from 1970 to 2013. The diversity of economic experience is illustrated in the inflation data whereby some countries have undergone periods of hyperinflation. As a result, the mean value for the LAC countries is relatively high; however, the mode figure at 7.7% is more respectable. Evident within the LAC countries is the relatively high levels of tariffs at 41%, with the maximum value at 78% and the minimum value at 17.61%. It appears that the LAC region is very trade protective. In the case of taxation, the LAC region is very diverse with maximum rates of 72% and a minimum value of 3.17%. The average taxation rate for the LAC countries is 27%.

6. RESULTS AND DISCUSSION

Table 4 presents our results from the multiple OLS regression for the 31 LAC countries over the period 1970 to 2013. Our results reveal that participation in an IMF to have a positive but not statistically significant impact on inward FDI. Therefore, we find evidence to support our hypothesis. However, it is not statistically significant. Interestingly, the lag terms for IMF participation in year two and three are negative. This implies that FDI inflows have a negative impact once a host country embarks on a borrowing program. As such, we do not find evidence to support our second and third hypothesis. Although, the results are not statistically significant, they indicate that potential investors negatively view a country that is on an IMF program. As such potential investors feel that being on an IMF program is likely to lead to greater uncertainty and possibly a repeated borrowing by the host nation. We believe that the negative impact of being on an IMF program on FDI occurs regardless of whether the host country agrees to comply with the IMF conditions and reform their economies. We believe that potential investors are risk averse and hence may actually take capital out of a country if it participates in an IMF program on the belief that the economy will become worse before it improves. During the difficult period before the economy improves, investors may wish to relocate their capital.

We believe that a fundamental weakness within the IMF borrowing program is that it provides a negative signal to private investors. To a large extent, private investors are justified as in Table 1, which illustrates

Table 4. Impact of IMF Lending Programs on FDI Flows.

	Unstandardized coefficients		Standardized coefficients		
	B	Std. error	Beta	t	Sig.
(Constant)	−3,686,258,719.284	4,332,214,584.804		−0.851	0.396
IMF1	669,983,412.906	2,054,710,096.848	0.024	0.326	0.745
IMF2	−353,383,796.483	2,409,027,644.982	−0.013	−0.147	0.883
IMF3	−224,191,278.799	1,999,530,793.461	−0.008	−0.112	0.911
INF	−77,735,860.635	116,972,494.425	−0.034	−0.665	0.507
EXC	29,467,355,281.796	5,228,844,685.358	0.334	5.636	0.000
TARIFF	−397,510,117.229	55,267,548.061	−0.411	−7.192	0.000
TAXES	334,996,229.079	69,540,781.102	0.259	4.817	0.000

that some LAC countries have been on 27 IMF borrowing program over a 60-year period. Therefore, there is a very high probability that being on an IMF borrowing program will lead to a repeated admission. In fact, every single country that participated in an IMF borrowing program in Table 1 has repeated this at least once. Therefore, it is felt that the IMF program does not deal with the core problems within the country that allow them to be self-reliant. More importantly, the reforms that are required by the IMF should not be conducted in vacuum but in consultation with inward investors. As stated above, FDI accounts for 3% of global GDP. Therefore, it has the potential to make a significant and positive contribution to the host nation. In addition, the literature review that has been presented shows the positive impact of FDI on host country GDP. Therefore, the IMF conditions should ensure that inward FDI is encouraged as a part of the lending criteria.

We believe that the performance metrics used by the IMF in order to make the next tranche of payments should be adapted so that it considers the actual performance as experienced by the private sector. We believe that policy actions undertaken by the host nation are reflected in the business conditions that are experienced by private sector investors both domestic and international. Therefore, the performance metrics should include trade openness, which according to our literature review positively impacts the host country. In addition, our results in Table 4 reveal that high tariffs have a negative and statistically significant impact on FDI. This implies that inward FDI does not positively value host nations that are protective over their domestic industry. Instead, inward FDI looks for economies that encourage competition and have low tariffs.

We find high inflation to have a negative impact on FDI and that reflects the fact that investors prefer a higher level of predictability. We also find that a stable and strong exchange rate exhibits a positive and statically significant impact on inward FDI. We believe that inward investors take a long-term view and are concerned not only regarding the rate that the initial investment is made into the host nation but also when profits will be repatriated to the home country. Therefore, the greater the exchange rate certainty the higher the likelihood of inward IMF. In theory, inward investors can use financial markets to hedge their exchange rate exposure. However, two issues arise, namely the time period of the financial hedge as well as its cost. Second, for hedging to be conducted through financial markets, the company should be able to state the value of local currency that needs to be converted. However, for most part, this value is not known and depends on market conditions. Therefore, currency hedging through financial markets is not always an option for investors.

Finally, we find that high taxes do not deter inward investors, and actually there is a positive relationship that is statistically significant. We believe that this relationship may reflect the fact that the mean value at 27% is lower than many other non-LAC countries. Second, the existence of double taxation agreements allows investors to offset tax paid in one jurisdiction with that of another. Typically, double taxation

agreements have the credit or the exemption concept. In the case of the former, tax paid in one jurisdiction can be offset when repatriated to the home country. In the case of the exempt criteria, the income for which tax has been paid in one jurisdiction is exempt from any further levies in the home country. Both types of double taxation agreements provide investors an advantage; whereas, in many cases, the exempt criteria may be better.

7. CONCLUSIONS

The LAC countries have experienced two periods of relatively high inward FDI namely during the 1990s and then prior to the international financial crisis. However, among the 31 LAC countries, we find that heavy-weight nations such as Brazil account for 42% of all inward investment. In addition, as far as the investor nations is concerned, the inflows into the LAC countries is highly concentrated with three countries namely the United States, the Netherlands, and Spain accounting for 80% of the total value. In part, this is reflected by the geographical proximity, historical ties, and language.

The objective of this study was to examine the impact of a country being on an IMF borrowing program on its FDI inflows. The traditional arguments are that being on an IMF program should provide investors with a positive message that the country is reforming as well as making data and policy more transparent. However, this study has found that in the year of being on the program, the FDI inflows remain positive but there is a negative impact in the second and third year. Therefore, we find that investors are acutely aware that being on an IMF borrowing program will lead to a repetition of this and hence view it negatively. As such, we argue that the IMF does not deal with the core problems that do not make the host nation self-reliant. Therefore, we argue that the IMF borrowing program should be reformed so that policy objectives are not developed in a vacuum but in consultation with inward investors. We believe that inward FDI is a very important stakeholder in any policy reforms that the IMF recommends. Second, we argue that the IMF performance metrics that are used to decide on whether the next trance of funds are made available should include issues that are important to the business community both domestic and international. Finally, we believe that the power of inward FDI is understated to bring about a positive impact to the host country and its economic growth. Therefore, we argue that IMF policy reforms should be centered on those aspects that attract inward FDI. Our findings show that being on an IMF borrowing program does not provide inward FDI with the seal of approval that they require for an investment.

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India’s Growth Trajectory and Its Dynamics with International Monetary Fund Reforms

Abdul M. Turay[1]*, Mohd Nayyer Rahman[2]
[1]School of Business, Kentucky State University, Frankfort, Kentucky, USA
[2]Postdoctoral Fellow-ICSSR, Department of Commerce, Aligarh Muslim University, India

***Correspondence:** abdul.turay@kysu.edu

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Abstract

Since the Breton Woods and the emergence of the International Monetary Fund (IMF) in 1947, developed countries had an upper hand in the dynamics of international financial management. The IMF has claimed to add insights about the developing and under-developed countries development. All over the world, the growth trajectory of the developing nations has been affected by the policies and procedures of the IMF. India got independence in the year 1947 and became an IMF signatory in the year 1945. Since then, India has been involved in the economic management on the parameters of the IMF. The growth story of India is a mixed response yet a success story until now. The recent phase of opening up the economy that started in 1991 has had a great impact on the growth trajectory of Indian economy. The present study aims to study the growth pattern of India and the economic reforms pushed by the IMF. Gross Domestic Product (GDP) and Current Account are considered as two variables for the study. Moreover, identification of structural breaks for Indian economy is performed with the use of econometric techniques.

Keywords: Growth; IMF reforms; Structural breaks; Current account.

1. INTRODUCTION

International Monetary Fund (IMF) came into existence with the Breton Woods Agreement in 1945. The disappointment of the world with the existing system created considerable problems in the world economic environment. However, with the inception of the IMF and the growth bust of the developed world, it became the dominant view that the IMF will be leading the world in the next phase of growth and development. In addition, for the newly independent states, it became not a choice but a natural alignment. India’s story of growth is a mixture of vicissitudes yet it holds promising future. India got independence in 1947 and started its growth gradually; the vacuum created owing to it being a newly independent country affected it severely. The growth and liberalization in India were gradual, but the economy remained a closed one. The nature of the Indian economy was promoted on the lines of socialist economy. However, it was never named so owing to the liberal ideology of the first Prime Minister Pt. Jawaharlal Nehru. India, therefore, became a mixed economy with the components of both capitalism and socialism. However, as the time passed, the word mixed economy was a mere term, and it became increasingly difficult to demarcate between mixed economy and controlled capitalism. The major liberalization emerged in the year 1991 with the standing arrangement made by the IMF for India. From the beginning, India took the assistance of the IMF as well as responded positively to the concerns of the IMF. The IMF concerns were particularly related to further liberalizing the economy while also ending the license raj regime. The present study attempts to capture growth evolution of India and its dynamics with the IMF. The study is divided into eight sections. Section 2 deals with the review of the literature and expounds the theoretical considerations in the existing body of knowledge. Section 3 captures the trends in India’s growth along with a discussion on structural breaks; whereas, Section 4 evaluates the linkages between India’s Growth and IMF Reforms in the past. Sections 5-7 deal with the empirical investigation for structural breaks in the macroeconomic series. The study concludes in Section 8.

2. REVIEW OF LITERATURE

Several studies have been conducted on the growth pattern of India and the economic reforms undertaken. However, major studies by academia focus on the economic reforms that emerged after 1991 liberalization (Krueger and Chinoy, 2002; Panchamukhi, 2000; Joshi and Little, 1996; Ahluwalia, 2002). From independence until the decade of 1980s, India remained a closed economy characterized by strict government licensing. However, it is to be noted that India was the original signatory to IMF ratifications in the year 1945. In the late 1980s, India faced a severe balance of payments crisis and macroeconomic imbalances. Its forex reserves were considerably less to import oil from the international market. India had to continue with the stand by arrangement of the IMF as a responsible signatory of the IMF. India on the verge of the downfall under the guidance and pressure of the IMF opened up its economy and agreed to further macroeconomic structural changes (Cerra and Saxena, 2002). From 1991, a chapter of economic growth and liberalization started for India under the watch of the IMF. Repeatedly, there arose a need for evaluation and re-evaluation of the performance of economic reforms. In the present times, economic restructuring has been synonymous to economic reforms in the sense that both target new objectives of aligning with international standards, monetary arrangements, balance of payments manual, etc. The restructuring experiment in India has witnessed a mixed response (Agrawal *et al.*, 2016). It is generally accepted that the reduction in tariffs started owing to India's agreement with the IMF in 1991 (Pursell, Kishor, and Gupta, 2007). The 1991 liberalization was not just accepted as it is, rather it was felt by some to be an imposition and a foreign rule. One of the prominent researchers considered it a breach of democracy and an indirect rule by the IMF-World Bank system (Chossudovsky, 1993). Economic Growth has remained as one of the most important concerns of the economy in order to open to the external economy. The most acceptable indicators of economic growth are Gross Domestic Product (GDP) and other measures of national income. Most of the studies focusing on economic growth have considered GDP as indicator (Grossman and Krueger, 1995; Castelló and Doménech, 2002). Work on structural breaks for India is relatively less confined to two or three studies. Study has been conducted on endogenous structural breaks in Foreign Direct Investment Inflows and Current Account Balance identifying a unique long run relationship between the series (Mukherjee, Chakraborty, and Sinha, 2014). It is to be noted that considerably less research work has been conducted on the structural breaks pertaining to Capital Account than Current Account of Balance of Payments. The decision to resort to IMF loan in order to tackle BOP crisis of 1970s was based on the principal argument that it would be a positive structural change in the economy as three years respite period would be provided by the IMF. This boosted exports and curtailed imports to an extent required to substantially reduce Balance of Trade deficit in the year 1970-1980 (Chandrasekhar, 1985). Structural breaks also help to define short run period for a country. It is determined as the period between two structural breaks based on trimming percentage (Rahman, 2016).

3. INDIA'S GROWTH TRAJECTORY: TRENDS AND STRUCTURAL BREAKS

The growth story of India with respect to two macroeconomic variables should be evaluated, that is, Gross Domestic Product (GDP) and Current Account Balance (CAB). Although GDP is the standard indicator of economic growth, (CAB) is subject to sustainability and is important to indicate balance of payments problems. The IMF has always focused on the sustainability of Current Account Deficit (negative CAB). Trends in GDP and CAB will suffice for the overview of the growth story of India. However, the visible trends are the dynamic processes, and there can be certain change-point problem in the series. Such an issue of change-point problem in time series data has been captured by several studies (Banerjee, Lumsdaine, and Stock, 1992; Chu and White, 1992; Perron and Vogelsang, 1992; Andrews, 2003; Andrews and Ploberger, 1994; Vogelsang and Perron, 1998). This change-point problem in the series has been termed in subtle manner as structural change or break. The philosophy of structural change suggests that a series over a period of time may change dramatically for which there cannot be a uniform trend. It is difficult to capture visibly as it is required to check the trends of the stochastic processes. The macroeconomic policy changes in the economy may bring about structural changes but that is the limited understanding unless there is clear empirical evidence for the same. This clear evidence needs the usage of recent techniques of identifying structural

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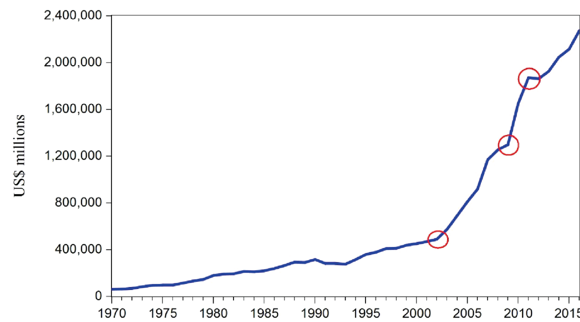
Figure 1. Trends in India's GDP.

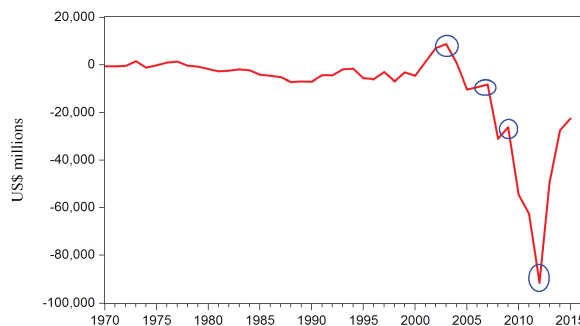


Source: Prepared by researchers from dataset 1.

changes (Dufour and Ghysels, 1996; Banerjee and Urga, 2005; Bai and Perron, 2003a, 2003b).The existing literature on structural changes focuses on macroeconomic variables such as aggregate output, measures of national income, international trade, employment, money, and interest rates. With respect to India, most will agree to 1991 as the year of structural change (structural break) yet there is dearth of evidence for the same. Specifically, there is no such study conducted to identify empirically the years of structural breaks for India with respect to different macroeconomic series. Thus, there is a need for evidence in favor or against 1991 as the year of structural break. Moreover, this will be focused in Sections 6 and 7. Returning to the trends in India's growth story, Figure 1 shows the GDP trends for the common sample period of 1970-2016 (2016 value for CAB not available). The two figures are taken separately owing to the huge variation in the scales of the two series.

From Figure 1, the trends in GDP of India are clear, and it suggests an overall increasing trend. However, it appears that the increase was sluggish until 2002, and after 2002 the rate of increase in GDP was much accelerated. From this trend, there can be certain structural breaks points assumed by the researchers. From the figure, it appears that 2002 (first red circle), 2009 (second red circle), and 2011 (third red circle) can be assumed to be the years witnessing structural breaks. The argument is that the series is abruptly changing the course. However, the limitation and the flaw in this approach is that visible identification is not subject to the undergoing white noise and stochastic processes. India has witnessed fluctuating growth rates in the course of growth trajectory. The highest growth rates (more than 10% on year-on-year basis) achieved by India were in the years 1973 (19.25%), 1974 (12.87%), 1977 (16.03%), 1978 (15.68%), 1980 (22.91%), 1994 (14.56%), 1993 (13.49%), 2003 (17.11%), 2004 (20.99%), 2005 (17.06%), 2006 (13.18%), 2007 (27.24%), 2010 (27.21%), and 2011 (13.40%). The mean value of GDP for the series is US$ 608583 million; whereas, the maximum and minimum values are US$ 2274998 million (2016) and US$ 59602 million (1970). However, the growth rate in 1991 appears as a negative of 11.36% indicating conformity of the pathetic economic

Figure 2. Trends in India's Current Account Balance.



Source: Prepared by researchers from dataset 1.

instability in the country. Other trends in Current Account Balance over the sample period should be studied as given in Figure 2.

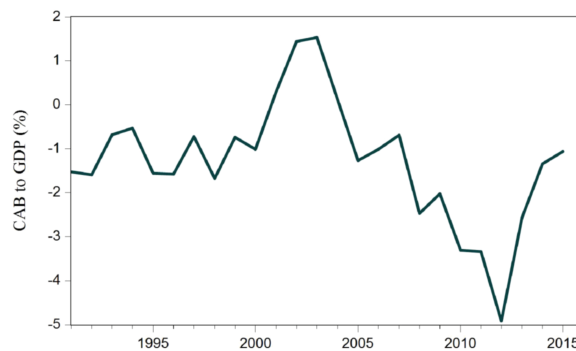
From Figure 2, it is clear that India has witnessed Current Account Deficit (CAD) and after 2004 it has widened. In recent years, it has even expanded. The mean value of CAD is US$ 10,051 million; whereas, the maximum and minimum values are US$ 8772 million (the positive denotes Current Account Surplus) and US$ 91471 million (Current Account Deficit), respectively. From the graphic visibility, few of the years may be assumed structural breaks though there may not be evidence for the same. The years that appear to be structural breaks may be 2003 (first blue circle), 2007 (second blue circle), 2009 (third blue circle), and 2012 (fourth blue circle). However, econometric testing is required to examine whether there is actually any structural break or not.

4. LINKAGES BETWEEN INDIA'S GROWTH AND IMF REFORMS

The trends presented in Section 3 and shown in Figures 1 and 2 are influenced by reforms pushed by the IMF. As has been reiterated, India is the original signatory to the IMF and has continuously sought assistance from the multilateral organization. Even before 1991, the IMF closely monitored India's economic trajectory and at times highlighted the lacunas. The nationalization of the major banks in India in 1969, when 14 commercial banks in India were nationalized that accounted for 85% of the total deposits of the country, was under the close monitoring of the IMF. Soon after the nationalization, the IMF suggested several measures of further bolstering the economy. In the era of post liberalization (post 1991), the intervention by the IMF increased. In the period between 1992 and 1997 IMF monitoring was used to measure the changes in the economy in post liberalisation period. These reforms included further de-licensing of banking sector, adoption of rupee devaluation strategy, Capital Adequacy norms, and Prudential norms. In the period 1997-2003, the IMF reiterated its concerns of Central Banks (Reserve Bank of India) transparency and clear monetary policy. India responded to the suggestions and concerns of the IMF by implementing the recommendations of several committees setup for the matter such as Narsimha Committee. From time to time, the IMF tracked the trend in the macroeconomic variables of India and at times concerns or suggestions were raised to which India always responded positively. In this regard, the IMF country reports for India highlighted the same. The IMF remained committed to Current account sustainability, and the number of countries facing such crises went on increasing owing to Global Financial Crisis, Brexit, and European crisis. India also faced the same fate of widening Current Account Deficit. Figure 3 shows the Current Account sustainability position monitored by the IMF from 1991 to 2016.

The positive values denote the Current Account surplus as percentage of GDP, and the IMF considers the positive values as sustainable. However, in most of the years after 1991, India has witnessed a Current Account Deficit. The maximum ratio of CAB to GDP has been 1.5% in the year 2003 while the highest deficit in the year 2012 with a ratio of 4.9%. The liberal view with respect to CAB ratio as per IMF is 5% of GDP. Any

Figure 3. Current Account Sustainability.



Source: Prepared by researchers from dataset 1.

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ratio beyond this is bound to be considered as unsustainable. In case of India, still India has not crossed the upper limit, but it has reached very close to 5% (4.9% in 2012). Still, considering the long-term trend, there is no major concern from India with respect to Current Account constraint. The reforms pushed and influenced by the IMF continued in India. In the period 2008-2013, India implemented the long awaited Basel III norms for the banking sector and further liberalized the sectors for 100% automatic route Foreign Direct Investment (FDI). Even in the sectors such as Defense and Railways, talks were held for liberalization in the form of government route clearance for FDI. In totality, FDI and Foreign Institutional Investment (FII) limits were extended after a long demand of the IMF. The term of Raghuram Rajan as the Governor of Central Bank in India opened up a new phase of cooperation with the IMF owing to his past professional experience with the IMF as chief economist. As a Governor of Central Bank of developing country, he highlighted the need for more inclusive and non-discriminatory policies of the IMF particularly in case of appointing executives in the IMF. The period between 2013 and 2016 witnessed accelerated compliance with the IMF. However, there remain lacunae on part of India as per the IMF. For example, in case of Balance of Payments Manual preparation, the latest manual to be complied is the sixth edition. India has still not adhered to that requirement. Even the concern is that the last Balance of Payments manual published by RBI was in the year 2010, and until now it has not been fully implemented.

For example, under Balance of Payments Manual6 (BPM) of the IMF, the reporting of goods includes Net Exports of goods under Merchanting. However, in the present Balance of Payments (BOP) reporting by India, this is not included in goods. On the contrary, it is shown as business services. Same is the case with non-monetary gold, which is to be shown separately as per the IMF guidelines. However, India has not shown it separately.

5. ECONOMETRIC MODELS AND ESTIMATION METHODS

The empirical objective of the study is to identify structural breaks in the macroeconomic constraints of India. The underlying logic holds that structural breaks identified, if any, are in part due to the involvement of the IMF and the reforms promoted by it. For the present study, two macroeconomic variables (about which IMF is most concerned), that is, GDP and CAB, are selected. Identification of structural breaks may indicate either single structural break or multiple structural breaks. However, the study has assumed in Section 3 based on graphical representation that there are multiple breaks in the macroeconomic series. The natural selection tends to multiple breaks tests. For identifying multiple breaks, Bai and Perron (1998, 2003a)'s breakpoint test is used, as it provides computational and robust results that extend upon the Quandt-Andrews framework. The test allows for multiple unknown breaks. For the sake of analysis, a standard multiple linear model with T periods and m breaks (which generates m + 1 regimes) is considered. The breaks category selected is Global l breaks versus none, which is the most comprehensive test developed by Bai-Perron (2003a). The test assumes null of "no breaks" against an alternative of l breaks. The maintained null hypothesis is as follows:

$$\vartheta_0 = \vartheta_1 = \dots = \vartheta_{l+1} \quad \text{.....(5.1)}$$

The model specification of Bai-Perron test (2003a) for multiple breaks is as follows:

$$F(\hat{\vartheta}) = \frac{1}{T}\left(\frac{T-(l+1)q-p}{kq}\right)(R\hat{\vartheta})'\,(R\hat{V}(\hat{\vartheta})R')^{-1}R\hat{\vartheta} \quad \text{.....(5.2)}$$

where ϑ is the optimal l break of $\hat{\vartheta}$,

$$(R\vartheta)' = \left(\vartheta_0' - \vartheta_1', \dots, \vartheta_l' - \vartheta_{l+1}'\right) \quad \text{.....(5.3)}$$

Moreover, $\hat{V}(\hat{\vartheta})$ is an estimate of the variance covariance matrix of $\hat{\vartheta}$.

The test requires pre-specification of the number of breaks expected. The critical values of Bai-Perron (2003b) are used as response surface computations for various trimming parameters. It is up to the researchers to identify the number of pre-specification structural breaks. In the present study, three breaks are assumed as Global l breaks against the alternative of "no breaks at all."

6. THE DATA

Two macroeconomic variables are selected for the study namely GDP and CAB for the sample period 1970-2016. Observations for CAB from 1970 to 1979 are taken from Reserve Bank of India Statistics; whereas, the remaining data (GDP and CAB) are taken from United Nations Conferences on Trade and Development (UNCTAD) database. The dataset 1 presents all the data and is given under the head annexures.

7. RESULTS

First GDP series is checked for structural breaks with the use of Bai-Perron breakpoint test (2003a) with the Global L Breaks versus None condition. To estimate GDP is regressed with a constant intercept while ignoring the presence of any endogenous parameter. The trimming is set at 15%, which indicates that the regimes are restricted to have at least 15% of the observations at a time. It indicates that in one regime at least seven observations will fall. The trimming outcome of 7 years difference is logical, as it is not considered a very long period in the macroeconomic cycle. Table 1 shows the output of structural breaks testing for GDP.

Table 1. Bai-Perron Multiple Breakpoint Test for GDP.

Sequential F-statistic determined breaks				3	
Significant F-statistic largest breaks				3	
UDmax determined breaks				2	
WDmax determined breaks				3	
		Scaled	Weighted	Critical	
Breaks	F-statistic	F-statistic	F-statistic	value	
1*	258.9857	258.9857	258.9857	8.58	
2*	312.0280	312.0280	370.8034	7.22	
3*	298.4629	298.4629	429.6664	5.96	
UDMax statistic*		312.0280	UDMax critical value**		8.88
WDMax statistic*		429.6664	WDMax critical value**		9.91
*Significant at the 0.05 level.					
**Bai-Perron (Econometric Journal, 2003) critical values.					
Estimated break dates					
1: 2007					
2: 2003, 2010					
3: 1987, 2003, 2010					

Source: Prepared by researchers based on econometric analysis in eviews9.5.

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From Table 1, it is clear that all the breaks are significant at 5% level of significance. The UDmax statistics shows the results as per unweighted maximized statistics. According to UDmax, maximum two structural breaks have been identified. It indicates that estimated structural break dates according to unweighted statistics are 1(2007) and 2(2003, 2010). On the other hand, WDmax suggests the determination of breaks on the basis of weighted statistics. According to WDmax, there are three breaks in the GDP of India. These dates are the options 1(2007), 2(2003, 2010), and 3(1987, 2003, 2010). All the three breaks are significant as the F-statistic is far more than the critical values, suggesting the rejection of the null hypothesis (Null being the presence of no structural breaks in GDP for India). Similarly, the identification of structural breaks is performed for CAB series of India for the sample period 1970-2016 (shown in Table 2).

Table 2. Bai-Perron Multiple Breakpoint Test for CAB.

Sequential F-statistic determined breaks				3	
Significant F-statistic largest breaks				3	
UDmax determined breaks				1	
WDmax determined breaks				1	
		Scaled	Weighted	Critical	
Breaks	F-statistic	F-statistic	F-statistic	value	
1*	119.1287	119.1287	119.1287	8.58	
2*	62.14174	62.14174	73.84711	7.22	
3*	41.22864	41.22864	59.35264	5.96	
UDMax statistic*		119.1287	UDMax critical value**		8.88
WDMax statistic*		119.1287	WDMax critical value**		9.91
*Significant at the 0.05 level.					
**Bai-Perron (Econometric Journal, 2003) critical values.					
Estimated break dates:					
1: 2008					
2: 2004, 2010					
3: 1980, 2004, 2010					

Source: Prepared by researchers based on econometric analysis in eviews9.5.

Table 3. Summarized Result for Structural Breaks in India's Growth Trajectory.

Null hypothesis	Result	Break dates with necessary condition	UDmax structural breaks	WDmax structural breaks
H_{01}: There is no structural break in GDP of India.	Rejected owing to significance at 0.05	1987, 2003, 2007, 2010	2 (2003, 2010)	3 (1987, 2003, 2010)
H_{02}: There is no structural break in CAB of India.	Rejected owing to significance at 0.05	1980, 2004, 2010	1 (2008)	3 (2008)

Source: Prepared by researchers from Tables 1 and 2.

Table 2 testifies that all the breaks are significant at 5% level of significance. The UDmax statistics identifies one break that is 2008, and WDmax also identifies one break that is 2008. Overall, the three structural breaks are significant at 0.05 but not supported by UDmax and WDmax. The UDmax and WDmax conditions are not necessary and satisfactory but only satisfactory. Therefore, the three structural breaks are accepted, that is, 1 (2008), 2 (2004, 2010), and 3 (1980, 2004, 2010). All the three breaks for CAB of India are significant as the F-statistic is far more than the critical values, suggesting the rejection of the null hypothesis (null being the presence of no structural breaks in CAB for India). The summarized result is shown in Table 3.

8. CONCLUSION

The study has identified the linkages between economic growth of India and the reforms pushed by the IMF. There is substantial evidence for the key role played by the IMF in the liberalization of India in 1991. The GDP growth trend in India has remained positive. However, India has witnessed a widening current account deficit, which is now closely monitored by the IMF. Several reforms in India on IMF benchmarks, such as Basel norms III, Capital Adequacy norms, and Prudential norms, have been successfully implemented in India. With respect to the evidence for structural breaks, the assumption that India has no structural break is rejected. The structural break dates for GDP are 1987, 2003, 2007, and 2010, which show a fluctuating growth trajectory as well as indication for a transition economy. With respect to Current Account, the structural breaks were identified for the years 1980, 2004, and 2010. The common structural break for GDP and CAB is in the year 2010. The plausible explanation for common break may be the convergence of economic policies toward both the variables. However, the populist view that 1991 is a year of structural change is not accepted owing to lack of empirical evidence. This also indicates that the graphical appearance of structural break may be misleading. The future research can be conducted to include more macroeconomic variables for identifying structural breaks.

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Annexures

Dataset 1. GDP and CAB of India (US$ Millions).

Year	Gross domestic product	Current account balance	CAB to GDP (%)
1970	59602.91	−594.000	−0.996596
1971	63944.12	−669.000	−1.046226
1972	69555.67	−403.000	−0.579392
1973	82947.35	1444.000	1.740863
1974	93619.18	−1198.000	−1.279652
1975	97386.17	−206.000	−0.211529
1976	98121.94	1001.000	1.020159
1977	113854.6	1313.000	1.153225
1978	131706.9	−290.000	−0.220186
1979	145750.6	−685.000	−0.469981
1980	179148.2	−1785.130	−0.996455
1981	191091.5	−2698.330	−1.412062
1982	195115.4	−2523.540	−1.293358
1983	212886.2	−1936.940	−0.909848
1984	210861.1	−2311.070	−1.096015
1985	219581.2	−4140.580	−1.885671
1986	240583.2	−4567.700	−1.898594

(Continued)

Year	Gross domestic product	Current account balance	CAB to GDP (%)
1987	266236.9	−5171.170	−1.942319
1988	294526.9	−7143.230	−2.425324
1989	291585.0	−6812.770	−2.336461
1990	316868.7	−7035.650	−2.220368
1991	280882.0	−4291.730	−1.527948
1992	282077.5	−4485.220	−1.590066
1993	275359.0	−1875.800	−0.68122
1994	315459.6	−1676.280	−0.531377
1995	358024.1	−5563.230	−1.55387
1996	377347.3	−5956.140	−1.578424
1997	409736.2	−2965.200	−0.723685
1998	412355.4	−6903.110	−1.674068
1999	439605.4	−3228.020	−0.734299
2000	453578.2	−4601.250	−1.014434
2001	468297.1	1410.180	0.301129
2002	489608.0	7059.500	1.441868
2003	573369.8	8772.510	1.529992
2004	693726.3	780.196	0.112465
2005	812058.9	−10283.500	−1.266349
2006	919117.9	−9299.060	−1.011737
2007	1169473	−8075.690	−0.690541
2008	1254803	−30972.000	−2.468276
2009	1297597	−26186.400	−2.018068
2010	1650635	−54515.900	−3.302723
2011	1871856	−62517.600	−3.339872
2012	1862249	−91471.200	−4.911867
2013	1923751	−49226.000	−2.558855
2014	2046257	−27451.600	−1.341552
2015	2116239	−22456.000	−1.061128
2016	2274998	NA	NA

Source: UNCTAD Statistics; 1970-1979 CAB data from Reserve Bank of India Statistics.

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