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THE GOVERNANCE OF THE INTERNATIONAL MONETARY FUND

Ariel Buira

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Manor Road Building, Oxford OX1 3UQ

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Ariel Buira, Department of Economics and St. Antony's College, University of Oxford University

ABSTRACT

Since 1997, following the approval of the Guidance Note on Governance by the Executive Board, the IMF has given increased attention to governance issues in its member countries. In view of its influence, it is of interest to consider to what extent the Fund's own governance meets the standards of transparency and accountability required for the good use of public resources. The paper reviews the power structure of the Fund, i.e. the distribution of quotas and the role of the Executive Board and of the staff and Management in decision making. It finds that the concentration of power in a few countries impairs the transparency and political accountability of the Fund. It argues that as the changes in the world economy since the Bretton Woods Conference in 1944 have not been appropriately reflected in the quota structure some aspects of the system have become dysfunctional.

THE GOVERNANCE OF THE INTERNATIONAL MONETARY FUND

Since 1997, following the approval of the Guidance Note on Governance by the Executive Board, the IMF has given increased attention to governance issues in its member countries. The promotion of transparency and accountability are at the core of the Fund's efforts to ensure the good use of public resources as well as the domestic ownership of programmes. In recent years the Fund has developed and applied its instruments for promoting these objectives to an extent well beyond what was envisaged at the time the Guidance Note was approved.(See 1)

Indeed, the Fund helps countries identify any weaknesses that may exist in the countries' institutional and regulatory frameworks that could give rise to poor governance, and provides support in the design and implementation of remedial reforms. Given the strength of vested interests that benefit from the lack of transparency and accountability, overcoming these weaknesses often requires that the countries undertake significant structural reforms.

Although reluctant to attract media attention, the considerable influence of the IMF over the majority of its 183 member countries is well known. It exerts a significant, often decisive influence, on such economic and politically sensitive matters as wage policies, taxation and public expenditure levels, public sector prices and tariffs, subsidies and pensions, privatisation policies, the exchange regime and the exchange rate, interest rates and monetary policy, trade policy, financial sector regulations and others.

With resources of over $280 billion and an expanded mandate, the Fund is probably today the most powerful of all international institutions. In view of its influence, it is of interest to consider to what extent the Fund's own governance meets the standards of transparency and accountability required to ensure the ownership of programmes by member countries and the good use of public resources. To do so we must begin by understanding its power structure and the rules by which it is governed.

Decisionmaking

Although the IMF is an international organization, its members do not have equal voting power. The acceptance of weighted voting is a departure from the traditional practice of international organizations.The vote of an IMF member has two components. Each member has 250 basic votes simply by virtue of its membership; this is a symbolic recognition of the principle of the legal equality of states. Each member also has one additional vote for every 100,000 SDRs of its quota. Because the number of basic votes has not been changed with successive quota increases, the ratio of basic votes to total votes has declined from 12.4 percent of the voting power of the countries participating in the Bretton Woods conference (Articles of Agreement, Schedule A) to 2.1 per cent today, despite the entry of 135 new member countries. In fact, as a proportion of the total, the basic votes of the original members declined from over 12 percent to under 4 one thousandths i.e.(0.124 to 0.0038 percent) as a result of a 37 fold increase in total quotas.

This has changed the power structure of the Fund since the importance of the basic vote of a country is inversely related to the size of its economy, as basic votes represent a substantially higher proportion of the voting power of small countries. Let me illustrate the shift that occurs as quotas increase: A country with a quota of ten million would be entitled to 350 votes i.e. 100 votes on account of its quota size and 250 on basic votes for being a member. When the size of quotas is multiplied by ten, the country will have 1000 votes on account of its quota and 250 basic votes, for a total of 1250 votes. Thus the share of basic votes declines from over 70 percent to 20 percent of the total.
Recall that in 1945 there were fourteen countries, almost a third of the membership whose quota was $10 million or less, and twenty eight countries, over half of the total, whose quotas were $50 million or less. With the passage of time inflation and growth have combined to increase the size of the quotas, but as the number of basic votes has remained constant, their relative participation in the total has declined.

The developing countries have repeatedly, and fruitlessly, raised the question of the need to increase the number of basic votes in order to maintain a balance in decisionmaking.

Although most IMF decisions are taken without a formal vote, simply by interpreting the sense of the Board, the Fund's Secretary arrives at this sense by the informal tally of the voting power of those Executive Directors who are for or against a decision. In practice, this often means an additional loss of influence for those numerous developing countries that are represented at the Board by a developed country Director, since the position of the Director will normally reflect that of the majority of votes in his constituency, as the Articles require that all the votes which an Executive Director is entitled to cast shall be cast as a unit.(See IMF" Articles of Agreement" Art.XII Section 3 iv).

The Articles of Agreement stipulate that some decisions require a qualified majority of the votes cast, that is, a particular proportion of the votes. At the Bretton Woods conference, it was proposed that qualified majorities should be required in only two cases (one being quota adjustments), yet the subsequently accepted Articles of Agreement required qualified majorities for decisions in nine areas. With the First Amendment to the Articles of Agreement, the number of these decisions rose to eighteen; with the Second Amendment, the number rose to fifty-three. Forty of these are executive board decisions; thirteen are board of governors' decisions.

The obvious explanation for the increase is the desire to protect some particular interest that might be affected by such decisions, for decisions subject to a qualified majority can be taken only with the consent of the members having a high proportion of the total votes. Currently, the United States has 17.35 percent of the total vote, Japan has 6.22,Germany 6.08 and France and the United Kingdom have 5.02 percent each. The G-7 countries have a combined total vote of 47.7 percent, and together with the Swiss Director account for 50.34 percent. If the vote of the Dutch and Belgian Directors is also added, they exceed 60 percent.

The concentration of voting power in the hands of the major industrial countries ensures that they have a determining influence on IMF policies. Yet some of them have, in addition, sought actual veto power either for themselves or for a few countries with similar interests. The result is that decisions on eighteen subjects require 85 percent of the total vote, and so may be vetoed by one member country alone, and twenty-one other questions must be decided by a 70 percent majority, and so may be vetoed by the five countries with the most voting power.

Among the issues that the IMF Executive Board may resolve only by qualified majority are decisions on quota size, rates of charge, exchange-rate arrangements, SDRs, policies on access to IMF resources, payments to the IMF, use of the Fund's gold holdings and reserves, management of IMF
investment accounts, publication of reports, remuneration of creditor positions, and temporary suspension of IMF operations.
Thus, all decisions related to the size of the IMF and the use of its resources, SDRs, gold, and the international monetary system are subject to the will of one or a few countries.

Special majorities have been used to block decisions supported by an absolute majority of votes on increases in the size of the IMF (that is, quota increases) and on SDR allocations, sales of the IMF's vast gold holdings, and policies on access to IMF resources. The' special-majority requirement often has the effect of inhibiting even the discussion of important issues that would be difficult to resolve.

The developing countries have argued that because voting itself is weighted - a situation that favours the industrial countries in decisionmaking - there should be no need for special majorities. However, the countries that for various reasons have favoured such majorities have not been prepared to do away with them.

The Determination of Quotas

Because members' quotas are the main factor determining voting rights, the process for setting such quotas should be examined.
It has been said that the quotas of the United States, the United Kingdom, the Soviet Union, and China were politically determined at the Bretton Woods conference. Raymond Mikesell, asked by the U.S. Treasury to estimate the first quotas, writes:
In mid-April 1943, . . . White called me to his office and asked that I prepare a formula for the. . . 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. . .

. As was typical, White wanted something on his desk in a couple of days-it took me four, including a weekend. A modern computer would have saved several days of work on my state-of-the-art calculator and might have produced a more credible result.

Had there been reasonably good official national-income estimates for the major countries in 1943, it might not have been possible for me to approximate White's conditions. Only the United States and Britain had official figures, although several countries had unofficial estimates. There were published figures on gold and dollar holdings (except for the Soviet Union) and on foreign trade, but no formula could meet White's conditions without giving great weight to national income. My sources for the national incomes of the thirty-four countries I covered were estimates of average consumption found in country studies, estimates of wage rates and family expenditures and extrapolations from budget and tax data Countries at a similar stage of development were assumed to have the same per capita income. My national-income estimate for China was $12 billion, less than a fifth of U.S. national income in 1940, and my estimate for the Soviet Union was $32 billion. I confess to having exercised a certain amount of freedom in making these estimates in order to achieve the predetermined quotas. I went through dozens of trials, using different weights and combinations of trade data before reaching a formula that satisfied most of White's objectives. I then found that I could get even closer if I increased the quotas by the ratio of average exports . . to national income. . . . Not all the estimates were for a common date, but I tried to adjust the data to 1940. The final formula for determining quotas was 2 percent of national income, 5 percent of gold and dollar holdings, 10 percent of average imports, 10 percent of the maximum variation in exports, and these three percentages increased by the percentage ratio of average exports to national income. (Mikesell, 1994, pp. 22-23)

Subsequently, at the meeting of the Committee on Quotas, Mikesell was asked to explain the basis for his quota estimates I had anticipated this request and gave a rambling twenty-minute seminar on the factors taken into account in calculating the quotas, but I did not reveal the formula. I tried to make the process appear as scientific as possible, but the delegates were intelligent enough to know that the process was more political than scientific" (pp. 35-36). Mikesell goes on to say:

The use of a single Fund quota to serve three purposes was both illogical and unnecessary, and this was frequently pointed out during the conference. There could well have been one quota based on, say, foreign trade and export variability to govern drawing rights, a second quota based on reserves and balance-of-payments history to govern contributions to the Fund, and a third quota based on economic and political importance to determine voting rights. (R.Mikesell,The Bretton Woods Debates, 1994, pp. 37-38)

It is remarkable that, with some adjustments in the weighting and definition of the main variables, the IMF continues to use the original formula for determining members' quotas, and it is certainly understandable that the lack of equity and rationality in the quota criteria continue to cause controversy and mistrust among members today, just as it did fifty years ago. The original formula is now combined with four other formulas, which give different weights to the same variables, and an element of discretion is used in selecting the formula to be applied in each case. (At times, the average of the various calculations is used to set a country's quota.) It is therefore not surprising that current quotas are far from representative of the actual sizes of economies, of their ability to contribute to the Fund or of their importance in the world economy.

This can be easily illustrated by the fact that such large countries as China, Brazil, Mexico and Korea with real GNPs and populations much larger than those of Belgium, the Netherlands, and Switzerland, have quotas that are only a fraction of the latter's and fewer votes. Thus their share in decision making is not commensurate with the systemic importance of their economies. (See Table 1 below).

Table 1 QUOTAS AND GNP OF SELECTED COUNTRIES

	Quotas (bi.SDRs)	GNP (inPPP)	GNP(1998)
Russia	5,945	580.3	337.9
Netherlands	5,162	339.3	388.7
China	4,687	3983.6	928.9
Belgium	4,607	239.7	259.0
Switzerland	3,458	189.1	284.8
Brazil	3,036	1021.4	758.0
Mexico	2,586	785.8	380.9
Korea	1,634	569.3	369.9

Source: IMF for quotas, World Development Report 2000 of the World Bank for GNP figures

Today it would be difficult to argue that, for instance, the quota of China, the second largest economy in the world measured in terms of Purchasing Power Parity, should be smaller than that of The Netherlands and similar to that of Belgium! Or that Belgium's quota be 52 percent larger than that of Brazil and 74 percent larger than that of Mexico. Moreover, it appears that many of the major differences arise mainly between the quotas of developed and developing countries and are not simply the result of history. In the calculation of quotas for Switzerland, a recent member of the Fund, the quota was determined in line with that of other industrial countries with a similar economic structure and levels of development. As a result, the distribution of quotas is skewed.

Table 2 QUOTA DISTRIBUTION BY COUNTRY GROUPS

Total Quotas (millions of SDR	212,401	100 .0 %
Industrial countries (24)	130,567	61.4
Oil Exporting countries	20,307	9.6
Non-Oil Developing countries	61,527	29.0

Source: IFS March 2001

Quotas largely determine a country's access to financing. Except in exceptional cases, a member can borrow up to a total of 300 per cent of its quota under regular facilities.

Thus the small quotas of developing countries limit both their share of voting power and their access to Fund resources.
The consequences of the imbalance of power have been further aggravated by the fact that since the late seventies no industrial country has resorted to Fund support. This, has changed the nature of the Fund, which has turned from a credit cooperative to which all members draw resources from time to time, and therefore have an interest in this being available on reasonable terms and conditions to an institution formed by two distinct groups of countries: industrial country creditors and developing country debtors. The fact that for over twenty years the Fund has only lent to developing countries has come to mean that the creditor countries try to lend as little as possible and therefore favour a hardening of conditionality, while the borrowers generally wishing to have ample access to financing on easy terms, tend to be defensive of their countries short term interests. Thus, the objectivity and impartiality of the Board, assumed by the Articles of Agreement has been eroded to a significant extent.

According to the Articles, quotas are to be reviewed by the Board of Governors at intervals of no more than five years and if appropriate adjusted. (Articles of Agreement, Art.III Sec.2a) The distribution of quotas tends to maintain the existing structure, one similar to that of half a century ago, largely because of the element of inertia resulting predominantly from so called equiproportional quota increases by which the quotas of all countries are increased by a similar proportion. On average, some 70 percent of all increases have been across the board, all quotas rose by the same percentage increase. While this procedure avoids the, at times, acrimonious discussions of countries' relative positions, it produces a substantial inertia in quota shares. As a result, quotas do not adequately reflect changes that have taken place in the world economy since 1944.
In the recently concluded Eleventh General Review of Quotas, 75 percent of the quota increase was distributed in proportion to members' shares in the total of pre-existing quotas, calculated according to the formulas. The other 25 percent was distributed in a somewhat discretionary manner, 15 percent based on the formulas that measure relative positions and 10 percent to correct the position of those countries whose calculated quotas most exceeded their shares in actual quotas. This was done in order to bring the quotas of those countries whose calculated quotas most exceeded their actual quotas, more in line with their relative economic positions.

However, in the past the changes in the quotas of the main industrial countries were not simply based on the formulas, questionable as they may be, but on political criteria. Thus, in the Ninth General Review Japan's and Germany's quotas were equalized (both in second place), although the Japanese economy was twice the size of the German economy. Similarly, the third largest quotas were given to France and the United Kingdom, although the Italian economy was somewhat larger than that of the United Kingdom at the time.
The limited representativeness of the Board has been implicitly recognized for several years by major industrial countries through the formation of the G-20, a forum established in the late nineties at the initiative of the US as a means for the G-7 of sustaining a dialogue with systemically significant countries whose representation in the Fund Board is limited. Unfortunately, by being outside the Fund, this excludes the majority of the Fund members from participating in the discussions.

Political Control and Accountability

In principle, the staff and Management of the Fund are subject to the political control of and accountable to the Board of Governors and its representatives, the Executive Directors. Thus, the line of control and supervision runs from the Board of Governors, formed by the Ministers of Finance and Bank Governors of member countries, to the Executive Directors that represent them, to Fund Management whom they appoint and to the staff that Management supervises.
Formally, the Executive Board, in which all member countries are represented, appoints the Managing Director. However, there is an unwritten understanding among major industrial countries by which the US appoints the President of the World Bank while the Managing Director of the Fund is appointed by Europe. As a result, a handful of European officials, essentially British, French and German, feel it is their prerogative to appoint the Managing Director with the consent of the US and little reference to the rest of the membership.
The widely publicized discussions and disagreements between the US and German governments leading to the appointment of the Managing Director of the Fund in 2000, with a touch of black comedy, as the US rejected the first German candidate, should have cleared all illusions as to the participation of most countries in the process.
As The New York Times expressed in its editorial comment "The Managing Director is too important to be chosen in secret by a few self-selected European countries. The IMF comes to the rescue of countries in distress, offering billions of dollars in loans if they adopt stringent economic reforms. It currently oversees about 50 such programmes in Latin America, Africa, the former Soviet Union and Asia. Critics say the programmes can cause needless economic pain."(See NYT 23/11/99) Further, "the Managing Director's judgement will often determine "whether the Korean currency should be defended, in the face of a looming depression by doubling interest rates. It decides whether to crack down on insolvent Indonesian banks, throwing the economy into a tail spin, or to prop up possibly corrupt or bankrupt institutions."
The selection process has to be opened up. Candidates to the position should state what their policies would be and how they would guide the Fund to attain its purposes. Since Fund operations are entirely with developing countries and transition economies, it is neo-colonial to assume that only a European is capable of becoming Managing Director. It is also entirely implausible to suppose there is no highly qualified national of a developing country that could take the position. The issue is doubly important as the Managing Director and senior staff can, in practice, only be held accountable by the governments of a handful of countries.

Recall that Executive Directors have a double role. On the one hand they collectively determine the policies under which the organization is run and appoint the Managing Director, who in turn appoints and supervises the staff. On the other hand they represent member countries. However, Directors representing developing countries, most of which will turn to the Fund for financial support from time to time, have a very limited ability to hold the staff, and much less the Management, accountable. The first reason for this is their limited voting power, which means they have little say on their promotion or removal. The second reason, no less important, is that being the representatives of petitioner governments limits the Directors' ability to question the staff, particularly that of their area departments, since they have to rely on that same staff to prepare the papers presenting their case for financial support to the Board. In addition, some Directors may be over-impressed by the power of the institution and may lack the combination of self-confidence and technical knowledge to challenge the assumptions or methodology of the generally very competent staff. This is of particular importance for developing country Directors, since the balance of power is loaded against them. Questioning the staff and Management may be particularly difficult for Directors who come from cultural traditions where respect for authority is greatest.

Not wishing to diminish their own effectiveness in securing financial support for the countries they represent often means Directors will not challenge or antagonize senior staff, much less Management, on whose judgment and goodwill their countries will have to rely. From the standpoint of transparency and accountability, a particularly sensitive issue arises when the staff and Management impose a requirement of prior action, such as the adoption of certain measures or the fulfillment of certain “pre-conditions”, on a country requesting a program without the knowledge of the Board.

In practice, the ability of developing country Directors to exercise effective control over staff and Management is seriously impaired. Indeed, Directors who try to exercise their supervisory role run the risk that the staff or Management complain about them to their authorities at the time financial support is negotiated, giving rise to a particularly delicate situation for Directors from third countries, since the confidence of the authorities in them may be undermined.

Given their limited voting power, developing countries are forced to join other countries to muster a sufficient number of votes to elect an Executive Director to represent them at the Board. Developing country constituencies or “chairs” representing several countries, usually rotate the positions of Executive Director and Alternate Executive Director every two years, among the several member countries they represent. While this policy, followed by most developing country constituencies permits a wide access of countries to the Board, it has two serious disadvantages. The first is that the rotation often means that Directors appointed are not familiar with the complexities and the policies of the institution, its programming techniques and past precedents on which they can draw. It will often take a year before the newcomers become familiar with the “modus operandi” of the institution. Consequently, they are at a disadvantage in policy discussions vis-a-vis the staff and developed country Directors of longer tenure and experience. Secondly the staff, whose appointments are permanent know that these Directors will depart at the end of the two year cycle; so if they request changes in the presentation of annual consultation reports, or on policy matters the staff do not favour, they can simply wait-them-out for, say a year, before the Director in question departs from the scene.

A further result of the quota distribution is that country representation at the Board is necessarily skewed. Thus, while 24 industrial countries, none of which has a Fund supported program, are at any one time represented by ten/eleven Executive Directors, who generally receive very considerable technical support from specialized offices in their capitals and are able to devote much of their time to policy issues, forty two African countries, excluding Arab countries, are represented by only two Executive Directors. Consequently, those Directors each representing twenty countries or more are barely able to attend to the copious amount of bilateral business with the Fund of the countries they represent, several of which may be engaged in programs or the negotiation of programs at the same time, and with no technical support from capitals, have little time to devote to the consideration of policy and systemic issues. Consequently, they have a limited ability to participate in informal consultations among Directors that often determine the outcome of discussions on policy matters. The situation of most other developing country Directors is similar, though generally not as extreme. Of course, since developed country Directors have a majority of the vote, they need not consult Directors outside their group.

While the Fund staff includes nationals from most (127 out of 183) member countries there is a longstanding predominance of nationals of industrial countries among Management and Senior Officers. As listed in IFS these accounted for 26 out of 31 officials listed as such five years ago (1996).The number had declined to 22 out of 29 listed officials in March 2001; this still represented some three quarters of the total. Moreover, numerous developing country nationals in senior positions went directly from a US university to a position in the Fund and their professional experience was gained rising through the ranks. Therefore, they cannot be said to bring the experience and sensibility that comes from work in their own countries. A training in economics in the better graduate schools in the US, UK or Canadian universities,which is common to high proportion of the staff, provides remarkable homogeneity in economic thought, greatly facilitating communication and cohesion of staff members around what has been characterized as the "Washington consensus". This common approach facilitates Fund operations, but at times may lead to a lack of pragmatism that creates difficulties in different environments.
In the light of the power structure of the Fund, and keeping in mind that economic policy is not an exact science, it is inconceivable that the staff not be influenced by their knowledge of what country or groups of countries exert control over the institution and its policies and what are the interests of those countries.

Furthermore, the current power structure, which places a small number of countries in a dominant position, impairs the objectivity of IMF decisions and recommendations. While the dramatic experience of the volatility of capital flows and the high costs of the Mexican crisis of 1994-95 should have been sufficient to lead the Fund to take a careful second look at the risks implied by full capital account liberalization and the integration of developing countries with international capital markets, particularly of countries without strong banking systems, the Fund continued to vigorously pursue the amendment to the Articles of Agreement to demand the opening of the capital account of developing countries. Only well after the Asian crisis of 1997-98 did the Fund and Bank concede that the volatility of capital associated with these crises does raise questions about the desirability of completely free capital movements and full capital account convertibility. The staff report published in January 2000 "Country Experiences with the Use and Liberalization of Capital Controls" finally concedes that controls have helped some countries insulate themselves - if temporarily - from financial crises and acknowledges that rapid liberalization can increase vulnerability to external and domestic shocks. This policy shift followed what were widely accepted as serious mistakes in the Fund's performance during the Asian crisis.

Arguing for greater accountability and transparency and for public scrutiny of Fund deliberations The New York Times argues editorially "The IMF predicted that its intervention in Asia in 1998 would lead to a quick turnaround. Instead, it lead to economic collapse, although Asia appears to be on the mend. Many of the countries in sub-Saharan Africa remain buried in debt and poverty despite two decades of IMF supervised economic reform. In Russia and Brazil the IMF wasted billions of dollars and delayed reforms, by propping up currencies. In both cases the currencies collapsed anyway."(op.cit.1999)

Technically questionable programs have sometimes been approved in order to support governments allied with the interests of the dominant country or countries, thereby placing the resources of the international community at risk. These cases have a demoralizing effect on the IMF staff, who are made to recognize that there are "special cases" based on non-economic considerations and who may, as a result, impose a degree of self-censorship.(3) Thus, it is difficult, if not impossible, to examine and analyse objectively initiatives or proposals that go against the interests of the major industrial countries.

Turning to another matter, it would seem that the countries with the largest quotas, the creditor countries of the IMF, have opted to reduce their relative contributions and their exposure to Fund borrowing, thereby reducing the size of the IMF relative to world trade. (See Table 3). The years shown below correspond to those in which a review of quotas led to a quota increase.

Table 3 THE RATIO OF TOTAL IMF QUOTAS TO IMPORTS

1944	1950	1965	1970	1978	1990	1998
0.58	0.17	0.15	0.14	0.09	0.06	0.06

SOURCE: IMF-Report to the IMF Executive Board of the Quota Formula Review Group

In recent years, with the increase in capital mobility, developing countries have become much more vulnerable than in the past. They have frequently faced massive capital outflows leading to financial crises. The financial support required in such cases is much larger than that necessitated by traditional balance of payments crises and greatly in excess, both in absolute terms and as a proportion of quotas, of that contemplated by Fund policies.

Although in a number of well known cases such exceptional support has been forthcoming, i.e. Mexico received $48 billion of which SDR12.3 came from the Fund, Korea $57 billion of which SDR 15.5 from the Fund, Indonesia $43 billion, Thailand $$17 billion, etc. this support has been decided on an "ad hoc", discretionary basis, by major industrial countries outside the framework of Fund policies. Of course, such arrangements are unlikely to comply with the principle of equality of treatment for all members.

Moreover, as Fund resources have not kept pace with financing needs, countries do not know what, if any, financial support may be forthcoming. Does this lack of transparency as to what support may be available matter? Some developed country high officials defend this discretional approach, which they have characterized as one of "constructive ambiguity", on the entirely implausible grounds for anyone familiar with the economic and social devastation caused by these crises, that a predictable framework for financial support would encourage moral hazard on the part of prospective debtors of the Fund. Placing the discretion of the strong over

predictable rules does not rate high marks in terms of transparency and accountability and may be seen as a step back in international relations.
Can countries obtain financing from the markets? In fact, at times of great uncertainty or crisis it is very difficult for any country to obtain significant financing from the markets and normally countries cannot. In such circumstances, in the absence of sufficient financial support from the Fund, bilateral assistance may come with conditions and strings attached that have no bearing on the resolution of the crisis. For instance, support for Korea was made conditional on that country implementing eight structural measures, which include allowing foreign investors to purchase Korean businesses, opening the domestic financial sector to foreign banks and insurance companies, liberalizing imports of some industrial products, especially Japanese cars, etc. “The fundamental issue is the appropriate role for an international agency and its technical staff in dealing with sovereign countries that come to it for assistance. It is important to remember that the IMF cannot initiate programs but develop a programme for a member country only when that country seeks help. The country is then the IMF’s client or patient, but not its ward. The legitimate political institutions of the country should determine the nation’s economic structure and the nature of its institutions. A nation’s desperate need for short-term financial help does not give the IMF the moral right to substitute its technical judgements for the outcomes of the nation’s political process.” (See Martin Feldstein in “Refocusing the Fund”, Foreign Affairs, Vol.77, number 3, 1998)

As the size of the IMF and access to its resources have been reduced, a new doctrine has emerged whereby the IMF is deemed to act mainly as a catalyst for other resources by putting its seal of approval on country programs.
The Articles of Agreement make no mention of a “catalytic role” for the IMF nor do they describe it as a credit-rating agency enabling certain countries-but not others- to access international credit markets. This was not the role its founders had in mind when they spoke of promoting international monetary cooperation.

Evidently, the Fund has moved away from Keynes’ idea that what we need is a means of reassurance to a troubled world by which any country whose affairs are conducted with due prudence is relieved of anxiety for causes that are not of its own making, concerning its ability to meet its international liabilities and which therefore make necessary resort to restriction, not on its merits but as a measure of self protection from disruptive outside forces.

The inequities in the quota structure and decision-making process of the IMF notwithstanding, the financial authorities of most member countries maintain reasonably cordial relations with the Fund’s staff. They try to do so not only because the IMF is often an important source of financial assistance, but also because they often seek the support of the Fund staff in domestic policy discussions in which they seek to limit expansionary expenditure and monetary policies. Thus, finance ministers and central bankers generally agree with the IMF on the importance of balancing government finances, on low inflation, and, more recently, on opening up economies and downsizing the parastatal sector to increase efficiency and boost growth rates. These shared views usually make it possible to establish good working relations, even political alliances, between the governments' economic teams and the IMF with a view to achieving certain common objectives.

The success of the post-war economic system, under which international trade grew by more than production, is widely acknowledged. It is also clear that, with the passage of time and ensuing changes in the relative size of member's economies, some aspects of the system have become dysfunctional. The efficient functioning of the international economy would be facilitated by certain reforms in the current international monetary order. Yet these reforms encounter serious political resistance from vested interests reflected in the existing power structure.

Good governance requires transparency and accountability. International institutions must reconcile countries' political objectives with the interests of the international community. Transparency requires that decisions be the result of an open discussion with broad participation. Accountability requires that those taking decisions face up to their consequences.

These objectives will not be attained as long as political decisions are taken by a very small group of industrial countries, the G-7, meeting outside the IMF. Legitimacy requires that the views and interests of the other IMF members- some 175, mostly developing countries and economies in transition- be given appropriate consideration.

The concentration of power in the hands of a very few countries also impairs the adjustment process between deficit and surplus countries. Although the IMF can bring considerable pressure to bear on the economic policies of the developing countries seeking financial assistance, it cannot induce the largest deficit country nor surplus countries to reduce their external imbalances.

Furthermore, the current power structure, which places a single country in a dominant position, impairs the accountability of the Fund for its decisions and recommendations.

Final Considerations

The world has changed considerably since the Bretton Woods Conference of 1944: the developing countries now account for a much larger share of the world economy, with China, India, Brazil and Mexico among the world's ten largest economies measured in real terms. The Soviet Union has disappeared. Trade has grown beyond expectations and vastly expanded international capital markets have taken a major unforeseen role.

During the past more than twenty years, the Fund's operations have been conducted exclusively with the developing countries and, recently, also with countries in transition. Moreover, in recent years, the Fund has extended its conditionality to issues of governance. This situation has widened the divide among IMF members. On the one hand is a small group of creditor industrial countries with a majority vote; on the other is the large number of largely debtor developing countries with a minority vote and limited influence on policies. Consequently, decisions on major Fund support programs are taken outside the Fund, on a discretionary basis, without rules. This power distribution raises questions on the legitimacy, transparency and accountability of Fund governance.

It is hardly coincidental that while the need for support of a significant group of developing countries has risen the size of the IMF has shrunk relative to world trade, and even more in relation to international capital movements. Over the last twenty years countries' access to IMF resources has become less predictable, conditionality has become gradually more restrictive, even for the compensatory financing facility, and SDR allocations have been suspended since 1981. These are manifestations of the growing gap between debtor and creditor countries and of the corresponding change in the industrial countries' view of the IMF. The industrial countries no longer regard the IMF as being the centre of the international monetary system but treat it instead as a specialized agency that assists the developing countries. Therefore, availability of sufficient support cannot be relied on. With this approach Keynes would disagree: "This (the Fund) is not a Red Cross philanthropic relief scheme, by which rich countries come to the rescue of the poor," he declared, "it is a piece of highly necessary business mechanism which is at least as useful to the creditor as to the debtor."4

The pressures of short-term self- interest and political expediency appear to have blurred the Bretton Woods vision of international cooperation as a means to improve the workings of the world economy. The notion that national goals are often best attained through international cooperation tends to be forgotten. This situation is unsatisfactory. To improve the governance of the Fund in terms of participation, transparency and accountability, and to enable it meet the new challenges of the world economy will require the reform of the quota and decision making structures.

Footnotes:

1-See" Review of the Fund's Experience in Governance Issues",SM/01/30 March 29, 2001 IMF Washington D.C.

2-Articles of Agreement, International Monetary Fund, Washington D.C. April 1993

3- David Finch, former director of the Exchange and Trade Relations Department responsible for ensuring the coherence of adjustment programs and equal treatment of member countries, resigned under political pressure to relax IMF conditionality for Egypt and Zaire ("IMF Silent on Resignation," Financial Times, March 21, 1987). Other well known cases of geo-political considerations determining support for poor programmes were support for Argentina in the second part of the eighties and for Russia in the 1990s. See also Bordo M.D. and James H. in "the International Monetary Fund: Its Present Role in Historical Perspective", NBER, W.P.7724 June, 2000 and Krueger, Anne O. in "Whither the World Bank and the IMF?", NBER W.P.6327, Dec.1997

4- Quoted by Anand G. Chandavarkar (IMF, 1984, p. 1).

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