Delivering On IMF Quota and Governance Reform: Principles of IMF Quota Reform

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(Views are Personal)

Introduction

- Major changes in World Economy
  - Trends since 1980, accelerated since 2003, Crisis
- IMF Mandate(potential): Global Macro/ monetary oversight(rules); Crises management
- Traditional approach: Multiple objectives
  - Country Representation: Basic Vote
  - Access: Reality (100xQuota, Gdp link->role)
  - Resources: Ad hoc contribution vs. Quota based; Issue Debt, Macro prudential; Subsidy funds.
  - Governance heavily influenced by Vote share
    - Focus: Principles based approach

Introduction

- Governance and Quota share
  - Appropriate Principles?
- Global Governance Principles
  - Democratic Principle, Sovereignty/Power => Size
  - Consistency (IC): Policy Advise-Formula
- Openness: Trade, Financial flows
  - Natural comparative advantage as benchmark
  - Negative effect of excess, policy distortion
- Demand/Borrowers Voice:
  - Variability vs. Poverty/Popullation

IMF Mandate: Macro-Financial Balance, Stability

- "The Fund shall oversee the international monetary system in order to ensure its effective operation and shall over see the compliance of…" [Art IV, sec 3(a)]
- Lessons of US/Global crisis
  - Real and Monetary/Financial are not separable (as imagined by Rational expectations orthodoxy/theory)
  - Macro Imbalances, Monetary-Financial spill-overs
- *Imbalance:* Excess relative to benchmark
  - Potential negative impact on global economy
  - Too much of a good thing is also bad for global stability
- Quota Formula and Shares should reflect these

Traditional Principle Set A

- One Country One Vote :
  - UN General Assembly: Gridlock and irrelevance
  - => Modified principle: Basic Votes
- One Person One Vote:
  - Protection of individual/minority rights through rule of law essential for true democracy.
  - =>Modified principle: Share of World Population
- Economic Weight in World Economy:
  - =>Modified principle: Share of World GDP

Traditional Principle Set B

- Demand/Debtors:
  - Vulnerability/Variability of BOP => Access(quota tranches)
    - Reality: Linked to (a) Size/GDP and (b) Contagion (negative effect on others).
  - =>Modified principle:
    - Formula based on GDP will automatically address the dissonance between theory and reality.
    - Asymmetric treatment of positive and negative contributions to Rest of the World.
    - Formula should logically result in higher quota in the former case and lower quota in the latter case!

Traditional Principle Set B

- Supply/Creditors:
  - Resources: One time contribution-> Higher share ever after?
  - Equity Based Institution: Not company with free market in shares and individuals free to buy from or sell to company.
  - All countries have to accept IMF rules (e.g. surveillance)
  - =>Modified principle: Quota formula - maximum equity/voting right.
    - Large majority of countries is willing to contribute more if it translates into higher quota/voting share.
    - Minority of countries with fund constraints, are free to to contribute less and have a lower share of votes.
  - Temporary needs can be met through counter cyclical Debt/borrowing limits.

Principle Set C (new)

- Domestic Government
  - Democratic principle: 1 person 1 vote
- Global Economic Governance:
  - Partial surrender of Ec. sovereignty
  - More autonomy => greater sacrifice
  - Economic size => Autonomy/Power
- Global Role ⇔ Economic size (GdpPpp)
  - Economy share in Aggregate (World)GDP => Quota Share

QUOTA FORMULA

- $$\mathbf{CQS = (0.5*Y + 0.3*O + 0.15*V + 0.05*R\,)^{k}}$$
  - CQS = calculated quota share;
  - Y = a blend of GDP converted at market rates and PPP exchange rates averaged over the immediate three year period for which data are available, with weights of 0.60 and 0.40, respectively;
  - O = Openness - the annual average of the sum of current payments and current receipts (goods, services, income, and transfers) for the latest five year period;
  - V = Variability of current receipts and net capital flows (measured as a standard deviation from the centered three-year trend over the recent thirteen year period);
  - R = twelve month average over a year of official Reserves (foreign exchange, SDR holdings, reserve position in the IMF and monetary gold); and
  - k = a compression factor of 0.95.

The ‘Monetary’ in IMF ?

- Money & Assets: GDP mer?
- Money is store of Value
  - Value is quantity of Goods it can buy
  - Relative value of different monies
    - Convert at PPP exchange rate
- Cross border Asset holdings
  - To the extent we are measuring relative value: Use PPP not market exchange rt

Openness in a Globalised World

- Neutral Tax-subsidy regime
  - Level of trade (% of Gdp) depends on natural comparative advantage.
  - Trade/Gdp declines with econ size (t*)
- Variations from benchmark (t*)
  - Trade (+)outlier: Potential (-) for World
  - No reward or penalty [unless due to tax, subsidy, XR distortion (-impractical)!]

Openness: Post-Financial crisis

- Financial openness (stock or flow) is even more problematic
  - Any difference in cross-border stocks /flows from neutral benchmark may be +/-ve factor for stability, depending on source and host country conditions.
- Negative financial externalities need to be taxed not rewarded with higher quotas!

Openness vs Macro Contribution

- Openness (Trade-GDP ratio)
  - Unrelated to global importance or impact
  - Irrelevant to a WTO policed globalised economy
- Global Aggregate Demand shortfall
- Contribution to net demand
  - Critical to global recovery

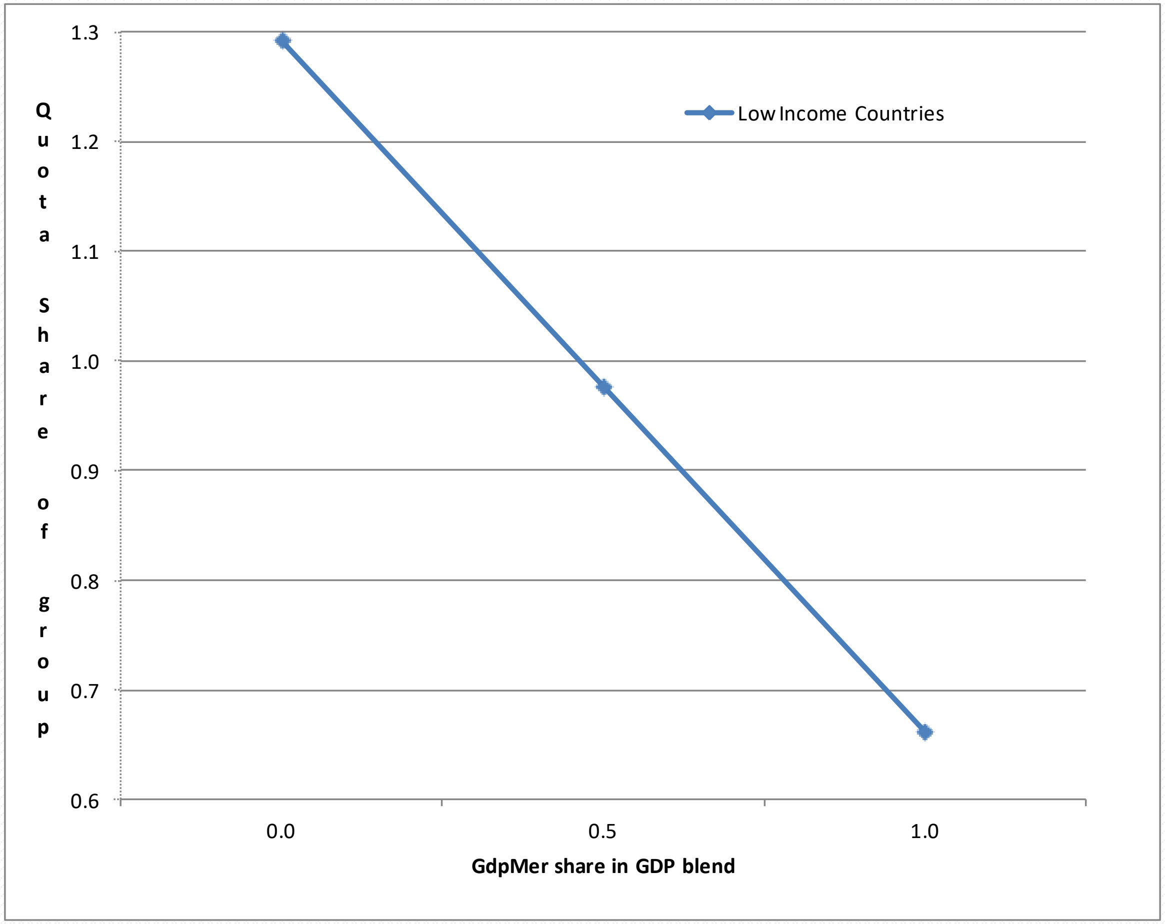
Voice of potential borrowers!

- G24 Secretariat: Technical Notes
  - Existing index of "variability" is a deeply flawed measure. Does not capture the potential demand/ need for financing BOP (liquidity) problems. Modify to improve measure
  - Weight by Population shares
- Voice of Poor: Sub-Saharan Africa, Bangladesh
  - Replace variability with Share of World's poor or share of population.

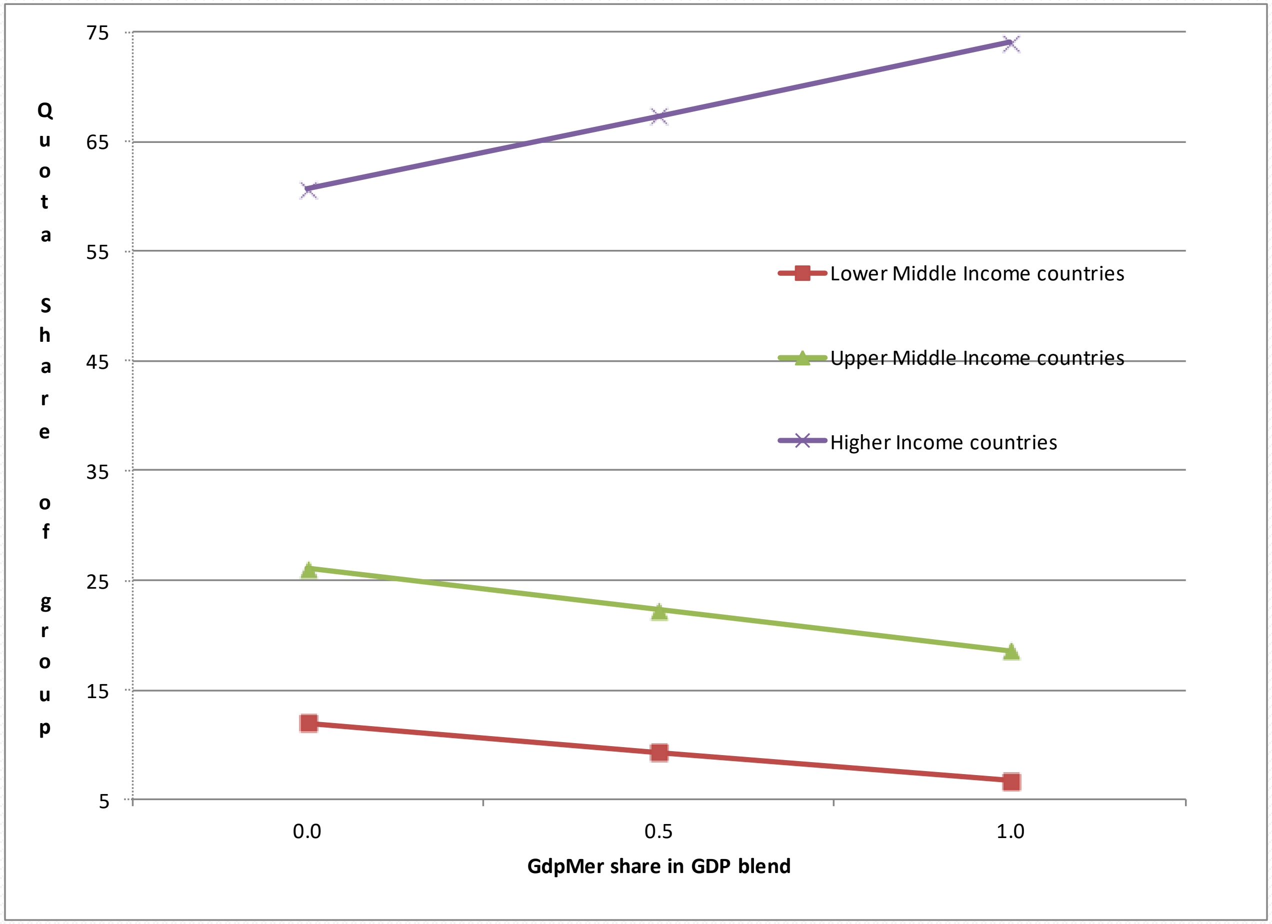
Table: Variation of Quota share with GDP PPP share (in GDP blend)

Group	GDPPPP share (in GDP blend)				
	0.0	0.4	0.5	0.6	1.0
Low Income Countries	0.66	0.91	0.98	1.04	1.29
Lower Middle Income countries	6.7	8.8	9.3	9.9	12.0
Upper Middle Income countries	18.6	21.5	22.3	23.0	26.0
Higher Income countries	74.1	68.7	67.4	66.0	60.7

Variation of LIC Shares with GDP Blend



Variation of LMIC, UMIC and HIC Shares with Blend



Formula With Voice of People:

Quota Share = 0.15*Population Share + 0.85*GDP blend

	Pop	Blend	0.15Pop+0.85Blend	
Group	Share	Share	New	Diff
Low Income Countries	11.7	0.9	2.5	1.6
Lower Middle Income countries	36.0	8.8	12.9	5.4
Upper Middle Income countries	30.6	21.5	22.9	4.2
Higher Income countries	21.7	68.7	61.7	-11.2

CONCLUSION

- Implications for Quota Formula
  - Simplicity, Transparency and Equity
- Economic Importance in World Economy:
  - Gdp Share in Global economy (80%);
    - Majority weight of GdpPPP in blend
- Voice and Vulnerability of people
  - Population shares (15%) or share of global poor
- Country Representation:
  - Incorporate basic vote into formula (5%)