

International Monetary Fund Reform: An Overview of the Issues

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CONTENTS

Summary	3
Introduction	7
<i>Mandate</i>	7
<i>Tools and Activities</i>	10
<i>Facts about the IMF and its Lending</i>	13
<i>IMF Reform</i>	17
The IMF's Role in the International Monetary System	20
<i>Surveillance</i>	21
<i>Exchange Rates and Policies</i>	24
<i>Capital Accounts and Financial Sectors</i>	27
<i>Regional Arrangements</i>	30
IMF Governance	32
<i>Quotas and Voting Power</i>	35
<i>Choice of Management and Staff</i>	41
<i>Chairs and Reform of the Executive Board</i>	43
<i>The IMF and Steering Committees</i>	46
IMF Lending Facilities	49
<i>The IMF as an International Lender</i>	54
<i>Support for Members with Large Debts</i>	59
<i>Programs for Good Performers</i>	60
<i>Support without Lending</i>	62
<i>Support for Low-Income Countries</i>	64
IMF Financial Resources	67
<i>The IMF's Need for More Resources</i>	67
<i>Augmenting the IMF's Resources</i>	69
<i>The Future of the SDR</i>	71
Concluding Remarks	73
Tables	74
References	81

Summary

The world needs a strong and effective IMF as the principal multilateral institution responsible for international economic and financial stability. A consensus on the role of the Fund and the scope of its activities in the 21st century is needed to achieve this objective. However, such a consensus does not exist today in official circles or among private observers. Consequently the IMF, once the preeminent institution of multilateral international financial cooperation, faces an identity crisis.

No single step or magic formula will restore the IMF to its prior position as a highly respected institution. Effective reform of the IMF must encompass many aspects of the IMF's activities—where it should become more as well as less involved. Over the past decade, a large number of changes in the international financial architecture and in the IMF's operations have been put in place. Those reforms have not been sufficient to restore the IMF to the center of today's international monetary and international financial system, assuming that was the intentions of the reformers.

Successful reform of the IMF must engage the full spectrum of its members. The IMF should not focus primarily on its low-income members and the challenges of global poverty. It should not focus exclusively on international financial crises affecting a small group of vulnerable emerging market economies. Instead, it must be engaged with each of its members potentially on the full range of their economic and financial policies emphasizing primarily those policies that impact the functioning of the global economy.

These three premises are the foundation for this paper and the conference on IMF reform at the Institute for International Economics for which this overview paper has been prepared.

After an introduction, the balance of the paper addresses four aspects of the IMF today: (1) The IMF's role in the international monetary system, (2) IMF governance, (3) IMF lending facilities, and (4) IMF financial resources. Under each heading, the paper provides a summary of some of the major issues and outlines some of the main reform proposals. In the process, the paper highlights some of the major issues that will be covered at the conference.

The primary purpose of this paper is to provide background for the IIE conference, but I do have views on these issues. It may aid readers at the start to know my recommendations based upon my experience in dealing with these topics for 30-plus years and in drafting this paper.

- I. The IMF, as the primary global monetary institution, must play a central role in shaping the performance of the global economy. For the IMF to be effective in this role, three steps are essential: (a) the systemically important countries, starting with the G-7, must support the IMF in this role, (b) instruments should be devised to increase the IMF's leverage over major industrial countries, and (c) the IMF must act more forcefully in discharging its responsibility to exercise firm surveillance over members' exchange rate policies, demonstrate increased consistency and clarity on its advice on exchange rate regimes and policies, and identify and pursue countries

- engaged in exchange rate manipulation, adhering to its own stated policies and procedures.
- II. The IMF's mandate should be updated with respect to members' capital account policies and financial sectors. The IMF should have international authority over international capital flows. More important, however, the IMF must have the basis on which to guide and advise members as they inevitably move toward increased capital account liberalization and seek to develop robust domestic financial systems.
 - III. The membership of the IMF should promptly address the reallocation of IMF shares (voting power) and the reallocation of chairs (representation on the IMF executive board). These linked issues of governance are symbolically and, therefore, substantively crucial to the IMF if it is to regain the trust and respect of all of its member nations. These issues are difficult because they involve history and politics. Ultimately, they only will be addressed successfully in the context of a substantial increase in the size of the Fund—total IMF quotas.
 - IV. It is time to discard the old conventions and to put in place a merit-based approach to the choice of the IMF's leadership and the management as a whole, and to buttress the merit-based approach to hiring and promoting the staff of the IMF while resisting calls to impose appointment quotas in the name of diversity.
 - V. A de facto steering committee operating outside of the Fund's formal structure has always provided guidance to the IMF. Ideally, it would be desirable to integrate the steering-committee function within the IMF's structure, for example, by giving a greater role to the IMFC or a Council. That is going to happen anytime soon. Given this reality, the preferred IMF steering committee is not the Cold War-era G-7 but the G-20, slimmed down to include one seat for the European Union. If this transformation is to be smooth and effective two steps are required: (a) the G-7 countries must yield some of their largely illusory sense of collective self-importance, and (b) the IMF bureaucracy should stop resisting an external steering process.
 - VI. It is time to call a truce in the jousting among the industrial countries about the appropriateness of large (relative to quotas) IMF lending programs to deal with capital account crises. The IMF management and staff should vigorously apply the recently established framework on exceptional access to IMF financing to govern decision making on large programs. The general membership of the Fund should support them. Aside from further tinkering around the edges, the basic framework should remain in place for at least a decade of experience.
 - VII. The stand-back approach to handling the Argentine debt restructuring by the IMF, with the support of its major members, has been a disaster. It was naïve to think that a country (whether in default or not) could reach a comprehensive and sustainable settlement with its creditors (internal as well as external) without some institution playing a coordinating role. The settlement achieved so far is neither comprehensive nor sustainable. The IMF has not achieved neutrality; in effect, from the standpoint of

the bondholders, the IMF was manipulated to side with the debtor country in default because Argentina had the upper hand in its take-it-or-leave-it offer and the IMF did not stay its actions. Prior to the Argentine case, the IMF had successfully played a coordinating role, some would say an umpiring role, in international debt matters for more than 20 years. It should resume doing so.

- VIII. The IMF should reward good economic policy performance in its lending operations. However, that standard should not become the exclusive basis for access to IMF financial assistance. Implementing this basic presumption is a challenge. Prequalification for IMF financing is a slippery concept precisely because we do not know enough to specify before hand what are the most important policy dimensions or how to calibrate them. However, the IMF should not close off debate in this area. Any large-scale application of this type of approach is likely to involve an increase in requests for IMF financial assistance unless the prequalification requirements are very tight or achieve a dramatic adjustment in structural policies.
- IX. The IMF should terminate its involvement with the Poverty Reduction and Growth Facility (PRGF) for its low-income members. The facility should be shifted to the World Bank, which has growth and poverty reduction as its primary mission. At the same time, the IMF should retain the capacity to lend to low-income countries facing short-term balance-of-payments difficulties, as necessary on subsidized, concessional terms. The World Bank should be left to itself to judge the soundness of the macroeconomic framework supporting its lending to low-income countries and to bear the financial consequences of its decisions. The IMF in its Article IV consultations with countries has ample opportunity to second-guess the World Bank. These facts should over time induce the Bank informally to seek the Fund's views.
- X. If the PRGF were shifted to the World Bank, part of the rationale for IMF nonborrowing programs—in the process of being renamed policy support instruments—with the IMF would be removed because the IMF would not normally be lending to low-income countries and thereby adding to their debt burdens. Further experimentation with nonborrowing or signaling instruments should not be excluded. However, consideration should be given to integrating them with strengthened surveillance procedures for all members, including greater candor and a strong, if not an absolute, presumption that all surveillance documents will be published.
- XI. The IMF should explore the option of market borrowing and put in place procedures for using this device against the possibility that it will not receive timely increases in its quota resources.
- XII. While a case can be made for the resumption of regular SDR allocations, that case is not likely to be convincing to the required 85 percent weighted majority of the IMF. A stronger case can be made for the United States finally to complete the ratification of the fourth amendment to the IMF Articles of Agreement to permit a special allocation of SDR. Consideration should be given to a new amendment, or altering the fourth amendment, to permit special one-time temporary allocations of SDR to

meet the IMF's own financial needs. Proposals for transforming the SDR so it can play a role in providing disguised financing for global public goods should not be seriously considered.

Four comments on these core recommendations:

First, any reader might add to the list, and I easily could extend the list as well. Successful IMF reform will involve many elements.

Second, only three recommendations would potentially involve an amendment of the IMF Articles of Agreement: recommendation II on the capital account and, possibly, recommendation III on governance and recommendation XII on the SDR.

Third, left off the list is anything that deals directly with the issue of program effectiveness. This should be a priority of IMF research. The IMF and its members should welcome research in this area and try to incorporate its lessons into the design of IMF programs.

Finally, the Fund continues to face a huge challenge of communication: getting information out promptly about its programs and priorities. The institution has made important strides in communication and transparency over the past decade, but one has the sense that it has fallen further and further behind in the race to convey the truth about its policies, procedures, and accomplishments.

Introduction

The Managing Director of the International Monetary Fund (IMF) (Rodrigo de Rato 2005b) stated “The IMF’s mandate is directed squarely at the promotion and maintenance of macroeconomic and financial stability, both in individual countries and at the international level.” Many other officials and observers use similar words to describe the Fund’s role. For example, US Treasury Secretary John Snow, addressing the Fund’s International Monetary and Financial Committee (IMFC) in April 2005, stated “The IMF’s mission is clear—to foster international monetary cooperation and balance of payments adjustment to support international financial stability and economic growth” (Snow 2005). Nevertheless, not everyone accepts this broad articulation of the Fund’s mission, and therein lies a major challenge the IMF faces: a lack of understanding and support for the organization and its core objective to promote *global* economic and financial stability.

Mandate

One reason why some challenge the view that the Fund’s mission is to promote economic and financial stability is that Article I of the Articles of Agreement of the International Monetary Fund does not contain a clear statement of the IMF’s purposes relevant to the international financial system of the 21st century. Article I speaks of (1) promotion of international monetary cooperation, (2) facilitation of the expansion and balanced growth of world trade, (3) maintenance of high levels of employment and real income, (4) promotion of exchange stability, (5) temporary provision of financial resources to correct balance-of-payments positions without resorting to measures destructive of national or international prosperity, and (6) lessening the degree of disequilibrium in the international balance of payments of members.

Article I, thus, establishes macroeconomic stability and growth as central to the Fund’s statutory purposes. However, the capital account crises that have been a major preoccupation of the IMF and much of its membership over the past decade have pointed in addition to the importance of maintaining financial stability in order to achieve macroeconomic stability and growth. The IMF Article I do not explicitly mention financial stability as an objective. Article IV does state, “a principal objectives [of the IMF] is the continuing development of the orderly economic and financial conditions that are essential for economic and financial stability.” Article IV lists obligations of members in their policies devoted toward these ends. On the other hand, Article VI enjoins members from using IMF resources “to meet a large or sustained outflow of capital” and endorses the use of controls to regulate capital movements. In today’s world these prescriptions are anachronisms, but an attempt in the late 1990s to remove these contradictions and to update the IMF Articles of Agreement in this area to enshrine the liberalization of capital movements as one of the purposes of the Fund and to establish the IMF’s authority over capital account issues foundered on the political and economic disagreements that surrounded the IMF’s handling of the East Asian financial crises.

There is an irony in much of this. On the one hand, many observers who want to scale back the IMF in dealing with international financial crises point to the exponential growth of private international financial markets to justify their position; the IMF is not needed anymore to

provide international. They certainly have some of their facts right, but the growth of these markets is only relevant to a small fraction of the nonindustrial countries that are members of the Fund, and the access of these countries to international financial markets is far from continuous. Thus, some observers see the evolution of international financial markets as a substitute for the Fund. Others see that evolution as causing increased international financial instability that the IMF should be better equipped to address.

In fact, most officials and observers do include domestic financial system stability among the core activities of the IMF along with monetary, fiscal, and exchange rate policies. They link those activities to the IMF's prevention and management of international financial crises. For example, Canadian Executive Director Kevin Lynch (2005) testified before the Canadian parliament "The Fund's mission is to prevent international financial crises if possible and, if not, then remediate them quickly and efficiently." Even critics of the IMF that advocate a narrowing of the IMF's mandate stress the importance of its role with respect to financial systems and capital movements. For example, Allan Meltzer (2005b) stated, "The IMF's responsibility should remain the maintenance of global *financial* stability," emphasis added. Charles Calomiris (2005) stated, "The legitimate current purpose of the Fund is to help to smooth capital market and exchange rate adjustments involving investment by developed countries in emerging market countries."

The IMF's membership at 184 is close to universal, only smaller than the United Nations by seven countries.¹ Despite disagreements about the scope of its mission, the International Monetary Fund is an institution of global governance. It is ultimately responsible to governments that contribute to its financing and give direction to its policies. Nongovernmental organizations (NGOs) and other national and international interest groups are not always pleased with or fully accepting of this reality because this fact deprives them of access and influence. At the same time, governmental institutions are controversial because of a lack of consensus about the appropriate role of government today.² Institutions of global governance, or institutions of international collective decision-making, generate even more controversy.³ Governments and their institutions are designed to provide public goods, for example in the international context to cope with cross-country externalities. Economists often appeal to market failures to make the case for government or international collective action. The problem is that economists do not agree about the nature of the market's failure or about whether proposed cures for those failures are likely to improve the functioning of the financial system. Moreover, political leaders don't always listen to their economic advisors.

The IMF has evolved over its 60 years. The Fund started life as the manager of the Bretton Woods international monetary system based on fixed exchange rates designed to avoid the pitfalls and internationally anti-social policies of the 1930s. Following the collapse of the Bretton Woods system and revision of its Articles of Agreement in the mid-1970s, the Fund became known as a firefighter dealing with the international debt problems of the 1980s, the

¹ The seven countries are: Andora, Cuba, North Korea, Liechtenstein, Monaco, Nauru, and Tuvalu.

² Boughton 2003 examines the evolution of the IMF and the challenges associated with both its effective operation and its continued maturation.

³ See Bryant 2003 for an admirable and informative attempt to describe efforts to establish institutions of cross-border finance and international governance as well as to prescribe pragmatic ways to move forward.

facilitator of the economic transformation of countries in Eastern Europe and the former Soviet Union at the end of the 1980s, a partner in the struggle against global poverty in the early 1990s, and an instrument in the prevention and management of capital account crises in the late 1990s.

This evolution itself has been controversial. A recent example of the Fund's evolution has been its increasing involvement in the area of abuse of the international financial system. In the late 1990s, for example, it was called upon to review the compliance of offshore financial centers with a number of internationally accepted standards. After September 11, 2001, the Fund acquired an enhanced role in the scrutiny of compliance with standards covering anti-money laundering and combating the financing of terrorism.

For some observers outside and inside the IMF, the expansion of the Fund's activities is the pragmatic response by an established and respected institution to the changing needs of its members and the changing character of the international financial system. According to this view, it is more efficient and effective to use an existing institution to meet new challenges than to create new institutions.

For others the evolution of the IMF represents nefarious mission creep, a bureaucratic effort to expand the institution's scope and influence. Thus, Michael Bordo and Harold James (2000) describe a process of supply response to perceived, but questionable in their view, market failures and the demands of IMF members to help to cope with them. They advocate a narrowing of the scope of the IMF's activities to the establishment of data standards, dealing with short-term liquidity problems, and providing information to markets via surveillance.

At the other end of the ideological spectrum, Sarah Babb and Ariel Buira (2005) bemoan what they see as an increase in the discretion exercised by the IMF management and staff, the absence of rules, and a tendency toward "mission push" by the United States and other members of the G-7. They advocate a more rules-based organization with increased transparency and accountability, increased financial assistance associated with fewer and narrower conditions, and a reworked governance and voting structure, including the elimination of the US capacity to block (veto) some decisions.

The IMF has evolved, but the role of the IMF as an institution of collective global governance has always been limited. Timothy Geithner (2004) aptly described its continuing dilemma:

The Fund, from its inception, was burdened by a mismatch between the aspirations of its architects and the authority and instruments they gave the institution to pursue those ambitions. Its authority over the policies of its members was limited. Its resources were small, and the facilities established to deploy those resources were modest relative to the problems they were designed to address.

Notwithstanding concerns within and outside the Fund about mission creep, there is broad agreement on core activities of the Fund: fiscal policies, monetary policies, and exchange rate policies. As mentioned above, the financial sector joined this triumvirate about 10 years ago,

and this has been an area of rapid expansion as well as considerable accomplishment, but not without its critics and controversies.

This extension of the Fund's core activities to the financial sector has been somewhat problematic. First, as noted, it is not well based in the Articles of Agreement. Second, the Fund shares jurisdiction in this area with the World Bank, which often has a longer-term perspective on financial sector issues, a different relationship with its members, and naturally a different set of views about what should be done and when. Third, the Fund is not a financial supervisor. The Fund was the principal drafter of only three of the dozen internationally recognized standards and codes that have been endorsed by the IMF and the World Bank in connection with their Reports on Observance of Standards and Codes (ROSCs).⁴ The Fund's principal and important role has been in the area of compliance with existing standards and codes.

In practice, of course, the IMF is now heavily involved in financial sector and related capital market issues in its analyses and its country programs. The broad membership of the Fund has grudgingly accepted this involvement, while still arguing about details. For example, how broad and intrusive should be the examinations of countries' compliance with international standards on anti-money laundering and combating the financing of terrorism? To what extent should the results of those examinations be factored into structural conditions in programs receiving IMF (or World Bank) financial support?

The United States and the rest of the G-7 continue to press the IMF in this area. US Acting Under Secretary of the Treasury for International Affairs Randal Quarles (2005) stated in recent testimony, "The IMF needs to integrate more fully capital market and financial sector analysis into the daily life of the Fund." In partial response to similar views expressed in the context of commenting on the Fund's own medium-term strategic review, Managing Director de Rato has formed a working group under the direction of William McDonough to provide an independent perspective on how well the Fund has organized its financial sector analysis.

Tools and Activities

To carry out its mission, the IMF uses three principal tools: surveillance, lending, and technical assistance.⁵ These activities contribute to the production of two basic products: policy advice and financing.

Surveillance operates at several levels. At the core are the essentially annual Article IV consultations with individual countries on their economic and financial policies and prospects, including "firm surveillance" over their exchange rate policies. These reviews cover the full range of macroeconomic policies and performance and cover microeconomic and structural policies and issues as well, such as trade policies, labor market policies, and pension systems.

⁴ The IMF has been principally responsible for drafting the standards on data transparency, fiscal transparency, and monetary and financial policy transparency. Various international standard-setting bodies had principal responsibility for drafting eight of the other nine standards, for example, in the case of the banking supervision standard, the Basel Committee on Banking Supervision, after much prodding from many quarters. The World Bank was the principal drafter of the standard on insolvency and creditor rights.

⁵ The IMF's research activities are an omitted tool from this standard list. Since the institution's founding, those activities have played a major role in establishing the Fund's policy credibility. That tool should not be neglected.

Eighty-six percent of members have agreed, at least once, to allow the resulting written assessments to be published. Ninety-six percent of members have agreed, at least once, to the publication of a public information notice (PIN) that summarizes the staff's and the executive board's views of the country's policies and performance after an Article IV consultation (IMF 2005g, table 1).⁶

Individual countries may also volunteer for reviews of their financial sectors and associated risks and vulnerabilities.⁷ In addition, members may volunteer for assessments of their compliance with the 12 principal international standards, codes and principles.⁸ The 1999 initiative to involve the IMF and the World Bank in reviews of compliance with international standards was a major component of the effort to strengthen the international financial architecture. It is intended to aid countries in their reform efforts, to aid the Fund and Bank in their work with countries, and to inform market participants. At a recent review of the initiative (IMF 2005d), executive directors were "broadly satisfied with the initiative's effectiveness" (faint praise), but expressed disappointment that market participants' use of the ROSCs remains low. However, Rachel Glennerster and Yongseok Shin (2003) find statistical evidence that the market rewards transparent countries, including those countries that comply with international standards and codes, with lower spreads. Charis Christofides, Christian Mulder, and Andrew Tiffin (2003) in a careful study reach a similar conclusion with respect to both spreads and ratings. However, the size of the effects provides limited leverage over compliance with codes. Moreover, empirical work in this area is in its infancy (Goldstein 2005a).

The Fund also conducts regional surveillance, for example of the Euro Area. It conducts global surveillance in the form of its semi-annual reviews of the global economic outlook and of the global financial system.⁹ In addition, the IMF staff prepares special reviews for meetings of various international groups such as the G-7 finance ministers and central bank governors for their meetings three times a year, for the meetings of the deputies and the finance ministers of the Asia-Pacific Economic Cooperation (APEC) forum, and for meetings of the G-20 finance ministers and central bank governors.¹⁰

IMF lending takes place through a number of arrangements and facilities. The bread-and-butter Stand-By Arrangement (SBA) is designed to provide financing for members to help them deal with short-term balance-of-payments financing problems. The Extended Fund Facility (EFF) is intended to provide financing for members with longer-term balance-of-payments and structural problems. The Supplemental Reserve Facility (SRF) is used to supplement the regular

⁶ Publication is a voluntary decision by the member country; a few countries have not permitted publication every year after first permitting publication.

⁷ The Financial Sector Assessment Program (FSAP) is conducted jointly with the World Bank. As of March 31, 2005, 47 percent of IMF members had completed FSAPs (IMF 2005g, table 1). The FSAP also forms the basis for confidential Financial Sector Stability Assessments (FSSA) that look at the vulnerability of the macroeconomy to financial shocks and the vulnerability of the financial system to macroeconomic shocks.

⁸ The resulting documents are Reports on the Observance of Standards and Codes (ROSCs). The reports consist of various modules, and a country may voluntarily agree to publish the reports. As of March 31, 2005, the reports on 75 percent of the completed modules had been published.

⁹ The associated published reports are the highly regarded *World Economic Outlook* and *Global Financial Stability Report*.

¹⁰ These documents are not published and probably they should be.

balance-of-payments financing by providing larger amounts for shorter maturities and at higher interest rates in connection with “capital account crises.”¹¹ The Compensatory Financing Facility (CFF) covers shortfalls in export goods and services earnings or rises in the cost of cereal imports that are temporary and caused by events beyond a member’s control. Under the same heading is emergency assistance associated with natural disasters and postconflict situations. Finally, the Fund has a Poverty Reduction and Growth Facility (PRGF) that makes longer-term low-interest loans to low-income countries with structural balance-of-payments problems.¹² Countries eligible to borrow under the PRGF are those that are also eligible to borrow from the World Bank Group under its International Development Association (IDA) window. The Poverty Reduction Strategy Papers (PRSP) in principle are prepared by the borrowing country as the basis for PRGF lending and are reviewed by the executive boards of both the Fund and the Bank.

The IMF also provides technical assistance to its members, normally free of charge. The technical assistance is intended to strengthen a country’s institutional capacities in the areas of the IMF’s expertise such as central banking. This major activity absorbs a substantial portion of the IMF’s financial and human resources. The activity is generally only loosely linked to IMF lending programs, actual or potential. Most of the technical assistance is financed out of the IMF’s own resources but about a third is financed by contributions from its members. In FY 2004, the IMF’s share of the cost of its technical assistance absorbed 23 percent of the gross administrative budget, or \$190 million, and about 700 person years (IMF-IEO 2005b). About 70 percent of the technical assistance goes to low-income countries with per capita incomes of less than \$1,000 per year.¹³

In addition to these three core tools, some observers include poverty reduction as a fourth, though one might more reasonably consider it a potential goal.¹⁴ The reduction of poverty in low-income countries is certainly an activity on which the IMF devotes a large amount of staff resources.¹⁵ Seventy-eight countries are potentially eligible to borrow from the IMF under the PRGF. As of May 31, 2005, 62 countries (four-fifths of those eligible) had PRGF credit outstanding from the IMF.¹⁶ The PRGF credit outstanding accounted for 73 percent of all IMF credit outstanding as of that date. Thus, poverty reduction is a major objective of IMF activity today. For example, eight of the 33 pages in Managing Director de Rato’s report to the April

¹¹ In capital account crises, macroeconomic policies are reasonably sound and current account deficits are small, but a country faces a sudden reduction or reversal in capital inflows.

¹² The PRGF was established in 1999 and replaced the Enhanced Structural Adjustment Facility (ESAF) that had been created in 1987.

¹³ An evaluation of the revenue and expenses of the IMF’s expanding operations is beyond the scope of this paper and the expertise of its author, though I touch on it in the last section on financing the IMF. Nevertheless, this is a major issue and is linked to other issues such as the amount of IMF lending and how the IMF finances its routine activities.

¹⁴ For example, Lynch (2005) stated that the IMF’s toolkit has “four core components: surveillance, lending, capacity building, and poverty reduction.”

¹⁵ The resources for PRGF lending are borrowed from countries and institutions generally at market-related interest rates. The terms of the lending to the PRGF borrowers (0.5 percent per year with repayments semiannually starting 5-1/2 years and ending 10 years after disbursement) are in turn subsidized through donations and the IMF’s own resources.

¹⁶ Table 5 shows 81 percent of PRGF-eligible countries were borrowers because we have classified India, technically PRGF-eligible, as an emerging market country in that table and others in this paper.

2005 IMFC on the IMF's policy agenda dealt with IMF support for low-income members (IMF 2005g).

Facts about the IMF and its Lending

It is useful to look at some data on the IMF's evolution as an international monetary institution. Shortly after the IMF was founded in 1945 it had 40 members.¹⁷ Thirty years later its membership had tripled to 127 members. An additional 37 members joined over the following 30 years to make up the current membership of 184.¹⁸ The membership consists of 24 industrial countries, 77 countries that are now eligible to borrow from the PRGF, 22 countries that we have classified somewhat arbitrarily as emerging market countries, and 61 other developing countries; see table 1.¹⁹

Table 2 provides a summary of the composition of the IMF's membership in 2005 and in 1975 by category of country and region of the world. By category of country, the largest increases were in what are now PRGF-eligible countries (28) and other developing countries (23). By region of the world, the largest increases were in Europe (27), principally in Eastern Europe and the former Soviet Union, Asia (12), and Africa (12).

More relevant than the evolution of the characteristics of the members of the IMF are the trends in patterns in the number of members that borrowed from the Fund over this 30-year period. Table 3 shows the distribution of the number of members with credit outstanding at the end of five-year periods from 1975 to 2005.²⁰ In 1975 and 1980, industrial countries represented about 10 percent of the countries with credit outstanding from the IMF, in contrast to zero from 1990 until today. Over the entire period, credit outstanding to emerging market countries fluctuated from 13 percent of the total number of borrowers in 1975 and 9 percent in 1980 to a

¹⁷ At the Bretton Woods conference in 1944 it was anticipated the IMF would have 45 founding members. However, the Union of Soviet Socialist Republics never joined and Australia, Haiti, Liberia, and New Zealand delayed in joining. Three of the remaining founding members later withdrew: Czechoslovakia, Cuba and Poland.

¹⁸ Twenty-five of the new members were from Eastern Europe and the former Soviet Union. Most of the remaining new members were small island nations, some of whom having just received their independence. There were also a few African countries such as Mozambique, Namibia, and Zimbabwe reflecting the final chapters of colonialism.

¹⁹ The area classification in table 1 and subsequent tables follows that found in the IMF's *International Financial Statistics*, hence the placement of some "Asian" countries in "Europe" and some North "African" countries in the "Middle East." The PRGF category of borrowers did not exist in 1975, much less in 1945. Although India is technically PRGF-eligible, we have classified it with the emerging market countries.

²⁰ Data on IMF credit outstanding, which reflect current programs as well as recently completed and in some cases suspended programs, provide a more informative picture of the pattern of the Fund's financial operations than the number or size of programs at particular dates. The data we have assembled, as best we can determine, capture all member countries that borrowed from the IMF over the 1975–2005 period, as well as prior to 1975, with the exception of Czechoslovakia/the Czech Republic. Czechoslovakia rejoined the IMF in September 1990. Soon thereafter in March 1991 it received financial support from the IMF in the form of a 14-month program. Following the Velvet Revolution in 1993 that led to the creation of two countries—the Czech Republic and the Slovak Republic—the Czech Republic took on its share of the IMF credit outstanding to it, had a new program starting in March 1993, but entirely repaid the IMF in 1994. Consequently it is not recorded as having had credit outstanding from the IMF in either 1990 or 1995. These data also do not cover countries that only had precautionary SBA or EFF and did not draw upon those arrangements: Colombia, Nigeria, and Paraguay. Colombia and Paraguay had such programs in May 2005.

high of 18 percent five years later and only 7 percent today. IMF credit outstanding to current PRGF-eligible countries rose steadily from 58 percent of all borrowers in 1975 to 73 percent today. Finally, the share of other developing countries among all countries with IMF credit outstanding has fluctuated since 1980 between 20 and 30 percent.

Equally important to understanding the IMF's evolution as a lender is the distribution of the amount of IMF credit outstanding to different categories of members at five-year intervals over the 1975–2005 period. Table 4 provides some relevant data. With respect to categories of countries (panel A), in 1975 almost half of IMF credit outstanding was to industrial countries, but that rapidly diminished to zero by the late 1980s. In contrast, IMF credit to the group identified as emerging market countries rose steadily from 27 percent in 1975 to 76 percent today.²¹ As indicated in the second memorandum item in table 4, IMF credit outstanding as a percent of total IMF quotas appears to have been remarkably stable at about 25 percent, with 1980 an outlier on the low side and 1985 on the high side. However, these ratios are affected somewhat by the timing of quota increases.

Interestingly, credit outstanding to PRGF-eligible countries reached its peak in 1980 at 37 percent of the total and is now only 14 percent. The decline over the past five years in part reflects the HIPC program of write-offs of debt to the IMF and other international financial institutions, but it is notable that by 1995, well before this phase of the HIPC program began, those countries accounted for only 22 percent of the total.

With respect to regions of the world (panel B), the share of IMF credit outstanding to countries in the Western Hemisphere rose to a peak in 1990, had declined sharply by 2000, but today amounts to almost half of the total because of large programs with Argentina, Brazil and Uruguay. The share of credit outstanding to members in Asia has had two peaks of 38 percent in 1980 and 2000, but has since declined back to 15 percent where it was in 1990. The share of credit to European countries declined after 1975, rose again over the 1990s with special lending programs for new members from Eastern Europe and the former Soviet Union, and has recently declined. Finally, the share of credit to African countries moved steadily downward after 1980.

Table 5 provides a final summary of the pattern of IMF lending activity over the past 30 years. The data show for each year the number of countries in each category (panel A) or in each regional group (panel B) with credit outstanding from the Fund as a percent of the (changing) total number of countries in each category or in each regional group. What is most striking is the remarkable stability (and slight decline since 1985) in the share of the total number of countries with IMF credit outstanding; that share rose by 16 percentage points between 1975 and 1985 and subsequently has declined by 12 percentage points. Over the entire period, industrial countries have declined from 27 percent with credit outstanding in 1975 to zero since the late 1980s. The proportion of PRGF-eligible countries with credit outstanding rose after 1975, and has remained near 80 percent ever since. Emerging market countries reached a peak in these terms in 1985, and their percentage has been on a downtrend subsequently. The peak for other developing

²¹ Contrary to the impression left by some official rhetoric in recent years about limited lending to large borrowers, total IMF credit outstanding to emerging market countries (the principal large borrowers) as of May 31, 2005 was SDR 42.2 billion compared with SDR 34.3 billion at the end of 2000.

countries was in 1995 reflecting borrowing by new members in Eastern Europe and the former Soviet Union.

Given these data on IMF credit outstanding by categories of countries, it is not surprising that a high proportion of African members of the IMF have had credit outstanding from the IMF since 1980. The proportions of Western Hemisphere countries and Asian countries with credit outstanding from the Fund have been declining since 1985. The European pattern reflects the IMF's high level of involvement with its new European members. Finally, a remarkable feature revealed by the data in the table is the consistent low-level of involvement by Middle Eastern countries with the IMF in terms of the of IMF credit outstanding to them.²²

An interesting question is how will or should the data presented in tables 2-5 evolve going forward. The answer will depend on the extent of (a) volatility in global economic and financial conditions, (b) vulnerability of different categories or groups of countries to those fluctuations as well as the strength of their own policy regimes, and (c) willingness of the IMF to lend.

One can be hopeful for continued favorable global economic and financial conditions. However, neither the national nor the global business cycle has been outlawed and global economic and financial conditions are unlikely to remain as benign as they have been over the past few years.

On vulnerability, a strong case can be made that a number of emerging market and other developing countries have successfully implemented macroeconomic and microeconomic structural improvements that have reduced their vulnerability to external or internal shocks. Moreover, these two groups have substantially increased their holdings of international reserves. From 1994 to 2004, the 22 emerging market countries listed in table 1 increased their combined holdings of foreign exchange reserves by more than 300 percent. The average increase was 384 percent.²³ These countries as a group increased their foreign exchange reserves from eight times their combined IMF quotas in 1994 to 24 times them in 2004. The other developing countries increased their reserves by more than 275 percent. The average was 308 percent.²⁴ These countries as a group increased their reserves from three times to nine times their quotas.

Thus, as reviewed extensively in chapter III of the BIS Annual Report (2005), many of these countries have put themselves in positions where they have taken out a considerable amount of self-insurance against future global economic and financial disruption and the possible need to borrow from the IMF, though uncovered risks definitely remain.

²² Evidence on the lack of close involvement of members from the Middle East with the IMF is that (a) only 43 percent of those members have ever agreed to the publication of their Article IV consultation reports compared with 86 percent for the IMF's membership as a whole and (b) only 29 percent of ROSC modules completed for these countries have they allowed to be published compared with 75 percent for the total membership although the average number of modules completed per country (3.0) is close to the IMF average (3.4) (IMF 2005g, table 1).

²³ Excluding China and Russia, which had the largest increases, the average increase was 234 percent. The average increase in foreign exchange reserves for the eight emerging market economies in Asia was 450 percent with the most dramatic increases in China (1,000 percent), Korea (640 percent), and India (500 percent).

²⁴ These data are for only 48 of the 61 "other developing countries" listed in table 1 because data are not available on the foreign exchange reserves of the other 13 countries in 1994 and/or 2004.

The jury is still out on the third factor—the willingness of the IMF to lend. Certainly, many observers and a number of key members of the IMF believe that the IMF should substantially curtail the scale of its lending to emerging market and other developing countries with normal, if not continuous access, to international capital markets. If these countries qualify for IMF loans, the size of those loans should be sharply restricted relative to their quotas. This view, if it prevails, could well lead to a further increase in self-insurance with respect to improved policies and further increases in international reserves.²⁵ The result might be a significant further reduction in IMF credit outstanding to countries other than the PRGF-eligible countries.

With respect to the PRGF-eligible countries, a substantial number of observers and a few members of the IMF have the view that IMF lending should be sharply curtailed or should be shifted to the World Bank while IMF programs of technical assistance and policy advice in the form of nonborrowing programs should continue.

In addition to these trends and attitudes, a number of East European countries are now under the political, economic, and one would presume financial umbrella of the European Union (EU). If they are in need of financial assistance over the next decade, they will not turn first to the IMF for it. Many Asian countries are strongly averse to borrowing from the IMF given their experience in the late 1990s and are actively involved in transforming the Chiang Mai Initiative into an Asian Monetary Fund—a more kindly and understanding version of the Washington institution (Henning 2002).²⁶

Thus, it is possible to imagine an IMF in the future that only occasionally embarks on new lending programs. Those programs may be limited to a few emerging market and developing economies in Latin America that have not built up large reserve cushions. At most the Fund will become a development institution doing very little lending. At worst it might wither away or be closed down as some observers have recommended.²⁷

On the other hand, it is too easy to say that the IMF will continue to exist but that it will become an institution that lends to an increasingly limited group of countries, with the membership of the institution sharply differentiated between lenders and borrowers. Industrial

²⁵ Eduardo Borensztein (2004) presents a number of indicators of potential demands for IMF resources over the next 20-50 years. He argues that the heavy borrowers from the Fund today, in terms of total amounts borrowed, are the middle-income countries. He further argues that the share of those countries in the total membership of the IMF should rise over this period, in particular over the next 20 years. Finally, he calculates that if China and India qualified for a package of IMF financial assistance as large as that received by Mexico in 1995 (6.3 percent of GDP) at the point where their estimated levels of income were similar (in 2018 and 2032 respectively), the financial demands on the IMF would dwarf the Fund's likely resources.

²⁶ Evidence of the disaffection of Asian developing countries from the IMF is (a) only 76 percent of them have ever allowed their Article IV reports to be published (compared with the IMF average of 86 percent), (b) only 5 of the 29 countries or 17 percent have had FSAPs (compared with the IMF average of 47 percent), (c) only 38 percent have had ROSC modules completed (65 percent for the IMF as a whole), the average number of modules is 1.6 per country (IMF average 3.4), and only 57 percent of completed modules have been published (IMF average 75 percent) (IMF 2005g, table 1).

²⁷ Among those who have advocated closing down the IMF are Meltzer (1995) because of the moral hazard he believes is associated with IMF lending, George Schultz, William Simon, and Walter Wriston (1998) on the grounds that the IMF is no longer needed, and Milton Friedman (2004) arguing that the Fund (and the Bank) have done substantially more harm than good.

countries have not borrowed from the IMF for decades, and it is difficult to imagine that they will ever again, but Boughton (2005) reminds us that the revolving character of the IMF continues to be relevant to understanding its role. He reports that from 1980 to 2004, 44 countries have moved from a situation of being net lenders to the Fund to finance IMF lending operations to becoming net borrowers from the Fund and back again to becoming net lenders. He reports that as of 2004 58 of the 129 countries that he classifies as developing countries—excluding industrial countries and market borrowers—had positive net financial positions in the IMF.²⁸ Of these 15 were net creditors to the Fund.²⁹

IMF Reform

Whither the IMF? How should it be reformed? There has been no dearth of ideas. Ten years ago, the Bretton Woods Commission (1994) emphasized in its conclusions that the IMF should play a larger role in the international monetary system, seeking greater exchange rate stability and better coordination of economic policies. It also advocated concentration on sound macroeconomic policies in its lending programs and reduced IMF duplication of the functions of the World Bank. Finally, it called for improved governance, including adjustment of quota shares in line with “the changed realities of relative economic importance in world trade, capital flows, and GNP,” and increased openness and doing a better job at explaining its mission.

In the late 1990s, in the wake of, first, the Mexican crisis and, later, the East Asian financial crises, the Russian default, and the Brazilian crises, there was a flurry of reports and proposals for IMF reform by public and private groups. Barry Eichengreen (1999) provides a nice summary of the debate on reform of the international financial architecture as of the late 1990s along with some proposals of his own. Robert Rubin and Jacob Weisberg (2003) provide an insider view of the initial evolution of the debate on the international financial architecture.³⁰

A report of a study group sponsored by the Council on Foreign Relations (1999) included seven priority items for IMF reform: (1) The IMF should lend on more favorable terms to countries that take effective steps to reduce their crisis vulnerability. (2) Emerging markets with fragile financial systems should discourage short-term capital inflows. (3) The private sector should promote fair burden-sharing in work-out situations, including the adoption of collective action clauses, and IMF lending to countries in arrears to the private sector should be subject to tight conditions on “good faith” negotiations with those creditors. (4) Emerging market economies should not adopt exchange rate regimes with pegged rates. (5) The IMF should abandon large rescue packages and adhere to its normal lending limits. (6) Both the IMF and World Bank should focus on their core responsibilities and limit operations in the other institution’s domain. (7) A global conference should meet and agree to priorities and timetables to strengthen national financial systems. Note that six of these seven prescriptions, and implicitly a seventh (number 6) relate almost exclusively to the IMF’s role vis-à-vis emerging market economies.

²⁸ Their reserve tranche positions, consisting of reserve assets they have paid into the IMF, were positive.

²⁹ Their reserve tranche positions were larger than the reserve assets they had paid into the IMF because they had lent their currencies through the IMF to other countries.

³⁰ “International financial architecture” was the lofty phrase that US Treasury Secretary Rubin first used in a speech in 1995 that sought to set out US thinking on the subject of reform of the IMF and the international financial system.

One of the most prominent and influential reports with regard to Washington opinion was that of the International Financial Institutions Advisory Commission (IFIAC 2000), also known as the Meltzer Commission. The central set of its recommendations focused on IMF lending in crisis situations, which the IFIAC agreed should continue. However, the majority view was that after a transition period such lending should be limited only to countries that had prequalified for such lending on the basis of a short list of criteria. Moreover, that lending should be short-term lending at a penalty interest rate. The IFIAC also recommended closing the PRGF, but that recommendation was understood to encompass its possible transfer to the World Bank.³¹

In response to some of the reports and recommendations that were appearing at the time, and in part to anticipate the recommendations of the IFIAC, US Treasury Secretary Lawrence Summers (1999) delivered a speech in London on IMF reform. He made six basic points and proposals: (1) The IMF should promote the flow of better information to markets. (2) The IMF should focus on financial vulnerabilities as well as macroeconomic vulnerabilities. (3) The IMF should be selective in providing its financial support, inter alia, because “The IMF cannot expect its financial capacity to grow in parallel with the growth of private sector financial flows.” (4) The IMF should improve its engagement with the private sector on capital market issues by setting up a capital markets advisory group and rationalizing its approach to private sector involvement in the management of financial crises. (5) The IMF should refocus its support of growth and poverty reduction in the low-income countries. (6) The IMF needs institutional reform in terms of transparency and openness and also in its governance structure. On the last point, Summers said the IMF “should move over time toward a governing structure that is more representative and a relative allocation of quotas that reflects changes under way in the world economy—so that each country’s standing and voice is more consistent with their relative economic and financial strength.”

Substantial movement, many observers would say progress, has been made on most of the areas highlighted by Summers. Where there has not been movement, for example, in the area of IMF governance, the issues are still very much alive.

US Acting Under Secretary Quarles (2005) summarized the progress that has been made on IMF reform in recent years, understandably emphasizing a break with the past more than the record supports. He said that limits and criteria for IMF lending have been clarified. He noted that the IMF is now focused more directly on its core macroeconomic areas of expertise including financial sectors. He said that more attention is being given to short-term financing. He highlighted the increase in IMF transparency and work on codes and standards for the financial system. He noted the progress on crisis management with many countries embracing the use of collective action clauses (CACs) in their international borrowing instruments.³²

³¹ John Williamson (2001) summarizes the major reports issued after the first round of debates along with some ideas of his own. See also the review of reform proposals in Goldstein (2003).

³² Collective action clauses were proposed by informed observers (Barry Eichengreen and Richard Portes 1995), endorsed by the official sector (G-10 1996), but resisted by the private financial sector, immediately following the 1995 Mexican crisis. This reform took almost ten years and a great deal of dedicated analysis and persuasion to bring to fruition.

Looking forward, Quarles identified the importance of the IMF's strengthening surveillance and crisis prevention, promoting strong policies without lending (nonborrowing programs), and effectively supporting low-income countries. He also noted that Secretary Snow beginning in October 2004 had "emphasized that change is needed to address the growing disparity between the IMF's governance structure and the realities of the world economy."

Some observers have other lists of priorities. Boughton (2004) highlights four key reforms: (1) strengthening surveillance and early warning systems; (2) lending programs should be designed to restore market access and growth; (3) appropriate direction of policy advice and financial support for low-income countries; and (4) improving the equity and effectiveness of IMF governance.

Timothy Lane (2005) identifies five key open issues for the IMF: (1) consensus on the IMF's role in the prevention and management of crises in emerging market economies; (2) the scope of IMF conditionality; (3) the seriousness of the phenomenon of prolonged use of IMF resources (borrowings outstanding) and what to do about it; (4) the IMF's involvement with low-income countries; and (5) governance issues.

Goldstein (2005a) puts forward a list with a somewhat different focus and orientation: (1) stronger injunctions against exchange rate manipulation; (2) better identification and control of currency mismatches in emerging market countries; (3) even greater emphasis on debt sustainability in IMF surveillance; (4) improving the quality of compliance evaluations with international standards and codes; (5) giving greater weight to early warnings of currency, banking and debt crises; and (6) limiting lending in "exceptional access" cases to cases that are truly exceptional.

Boughton, Lane, and Goldstein recommend rather disparate approaches to IMF reform. As indicated earlier, some observers favor narrowing the IMF's focus, for example, to the developing countries other than those with normal market access, perhaps on a precommitted basis, or to only financial sector issues in those countries. Alternatively, the IMF's focus might be narrowed principally to emerging market countries and the sustainability of their debts and their vulnerability to disruption.

Meanwhile, the IMF itself has embarked upon a medium-term strategic review with the aim of developing a medium-term strategy—a medium-term strategic review (MTSR).³³ The review is internal, but under the guidance of the executive board and ultimately the IMFC. On the basis of published reports (de Rato 2005a, IMF Survey 2005, and IMF 2005g), it would appear that this review will cover five broad topics: (1) the effectiveness and impact of surveillance; (2) the IMF's analysis of financial sectors and international capital markets; (3) the IMF's lending activities; (4) the Fund's role in low-income countries; and (5) various aspects of IMF governance, including internal management issues and voice and participation in the institution by a broader range of countries. A preliminary report on the IMF's MTSR will be released before the IMFC meets on September 24, 2005, but the final review and the full development of a medium-term strategy is likely to extend into 2006, in part, because the

³³ This exercise was originally a G-7 initiative.

McDonough Working Group on the IMF's analysis of financial sectors and capital account issues is not scheduled to complete its work until the end of 2005.

One topic that has been missing from most recent agendas for IMF reform, with the exception of the report of the Bretton Woods Commission more than a decade ago, is the IMF's role in the management of the international monetary and financial system, in particular with regard to exchange rate misalignments and global economic imbalances.³⁴ At the April 2005 IMFC statements by representatives of the G-7 countries and the European Union, by finance ministers Breton, Brown, Eichel, Goodale, Junker, Siniscalco, Snow, and Tanigaki, paid lip service to the objective of achieving greater macroeconomic and financial stability insofar as their own macroeconomic policies are concerned. However, in their comments on the IMF's strategic direction, none articulated a role for the IMF in this area. Instead, they implicitly presented a view that the IMF's primary role should be restricted to nonindustrial countries, preferably the nonemerging-market countries. The logical inference is that the IMF should become just another development institution.

The next section of this paper critically examines the role of the IMF in the international monetary system.

The IMF's Role in the International Monetary System

Mervyn King (2005) summarized succinctly the view that the IMF should have a major role in addressing the proper functioning of the international monetary system:

The international monetary system should be seen not as a series of bilateral relationships, but as a multilateral arrangement, albeit one where a small number [larger than the G-7] of key players can usefully communicate with each other. I think we need to rethink the role of the IMF in the international monetary system. . . . I am not convinced that the future of the Fund is primarily as an occasional international lender of last resort for middle-income countries suffering financial crises.

Without putting words in King's mouth, his remarks suggest an IMF role that is broad and should contribute more than it does today to substantial cooperation, if not coordination, on national policies affecting the international economy and financial system. Others are highly skeptical about international macroeconomic policy coordination and by implication the role of any international organization in fostering such coordination. For example, Siebert (2005) at a conference on the IMF states, "The best that governments can do is to follow an atmospheric coordination, i.e., exchanging information on the situation and the paradigm to be used."

³⁴ Most observers use the terms "international monetary system" and "international financial system" interchangeably. My preference is to reserve the first term for the conventions, rules, and structures associated with official actions and policies and to reserve the second term for the broader set of conventions, rules, and structures that involve private sector participants as well, with the second encompassing the first. However, in this paper I, too, use the terms interchangeably.

This section examines the IMF role (1) in surveillance, (2) with regard to exchange rates and policies, (3) in capital account and financial sector issues, and (4) with respect to regional arrangements. All four aspects are central to an effective role of the IMF in the international monetary system. In general, if the IMF is to play these roles effectively, it has to be more of an umpire and not just an advisor and sometime lender.

Surveillance

It is widely agreed that surveillance and the associated process of policy coordination and cooperation is one of the central roles of the IMF. Effective surveillance can help to solve the type of coordination problems that undermined the health of the global economy in the 1930s that led to the founding of the IMF at the end of World War II. Under the Bretton Woods system, coordination was forced through the fixed exchange rate system (gold exchange standard). With the forced abandonment of that system in the 1970s, surveillance remains as an instrument to deal with imbalances in the global economic and financial system.

The disagreement today is how surveillance fits into the IMF's overall mission and whether surveillance has anything to do with the health of the international monetary system. Thus, the IMFC (2005) concluded:

Surveillance is a central task of the IMF and determined efforts are required to enhance its effectiveness and impact, building on the conclusions of the Biennial Review of Surveillance. Surveillance should become more focused and selective in analyzing issues, in an evenhanded way across the membership. Regional and global surveillance should play an increasingly important role, and be better integrated with bilateral surveillance.

The IMFC's conclusions, while mentioning the important role of regional and global surveillance, which presumably has something to do with the functioning of the international monetary system, do not provide much guidance for what the IMF should be doing. The conclusions do point to the three levels of surveillance: national, regional, and multilateral. Presumably, it is principally in its multilateral surveillance role that the IMF becomes concerned with the functioning of the international monetary system. To the extent that the policies and performances of individual countries or groups of countries affect the health and smooth functioning of the system, national and regional surveillance are also relevant.

The relevant questions with respect to the IMF and the international monetary system include what is the scope of such surveillance and what variables and policies should it cover? Should it more aggressively engage with countries on their exchange rate policies? How can it be made more effective in altering exchange rate and other policies? Should the IMF have a larger role to play in policy coordination? How can it perform its current role better? Or should it have a different role?

Currently many of the concerns and criticisms of the role of the IMF in the international monetary system are connected with the perception that global economic imbalances are a threat

to international economic and financial stability and the IMF should be doing more about them. Of course, the IMF has hardly been silent on these issues, featuring them in successive reports on The *World Economic Outlook* and issuing special analyses of the general issue, or aspects of it such as US fiscal policy. Managing Director de Rato (2005b) devoted more than half of his remarks to the issue of global imbalances.

Global imbalances and the policies that support their continuation largely, but not entirely, involve the major economies: the United States, the Euro Area, and Japan. However, many informed and sympathetic observers despair about making any progress in this area. For example, Geithner (2004) comments, the Fund “will never be decisive . . . in persuading the G-3 to avoid policies that create the risk of abrupt changes in financial market conditions or exchange rates.”

The basic problem, as described by David Peretz (2005) and many others, is that the IMF lacks leverage over the policies of countries that do not need, and especially those that never anticipate ever having a need, to borrow from the Fund. In addition, these countries either do not agree that their policies risk adverse global effects, or, if they agree, they are unable for domestic political reasons to do anything to affect their policies.

Even for those who agree that there is a need, effective remedies are not easy to design. Some of the candidates might be:

1. **Increased transparency.** This is a general prescription for many of the problems of the international financial system, but it applies with some vigor to global surveillance. José De Gregorio et al. (1999) advocate increased transparency with regard to the IMF’s internal operations along with increased independence for the executive board and the staff.³⁵ Their focus is principally with regard to IMF relations with emerging market countries, but one could argue they should be relevant to the larger economies that potentially affect the health of the international monetary system. Barry Eichengreen (2004a) repeats his recommendation that all IMF surveillance documents should be released to the public, rather than leaving discretion with each country.
2. **Increased candor.** The IMF (management and staff) has become more candid in recent years in its pronouncements on risks to the international financial system and the links between those risks and the policies of the major economies. However, both Michel Camdessus and Jacques de Larosière (Camdessus et al. 2004) point to the need for G7 countries to listen more carefully to what the IMF is saying and for greater focus on systemic interactions in the process of multilateral surveillance. Increased candor probably should be coupled with increased IMF humility. When the IMF staff or management predicts a disaster and the disaster does not occur, there should be an explanation of why—changes in circumstances or wrong policy prescriptions.
3. **Specify remedies.** IMF reports on countries that are systemically significant often suggest appropriate changes in policies. IMF reports on the risks facing the global

³⁵ Publishing promptly detailed minutes of executive board meetings, decisions through voting, and publication of voting records.

economy do the same. However, those suggestions are general in nature—tighten fiscal policy, avoid financial bubbles, intensify structural adjustment. The IMF might go several steps further and specify as precisely as possible the size if not the content of the policy adjustments it would require if the policy excesses of the countries involved were to lead to a need to borrow from the IMF. This approach could be applied even in cases where such an eventuality was highly unlikely. The more specific the IMF was in its advice, the more specific the country would have to be in rejecting that advice.

4. **Ratings.** It has been proposed, and to date rejected, that the IMF should ratings of countries. Again, this proposal normally is advanced in the context of IMF surveillance of countries that might reasonably be expected to borrow from the IMF, but why should there not be a rating system that applies to countries whose policies have systemic significance?
5. **Scorecards.** Geithner (2004) endorses for emerging market countries “a process with more frequent, publicized [IMF] staff assessments of performance against a medium-term framework designed by a member country.” That approach could be extended to all systemically important countries, including important industrial countries.
6. **Change the paradigm.** Multilateral surveillance and the associated surveillance of the systemically important members of the IMF is process driven. Even when multilateral surveillance is subjected to independent evaluation, that evaluation is likely to be process oriented. The IMF’s Independent Evaluation Office is currently evaluating IMF multilateral surveillance. The draft issues paper (IMF-IEO 2005c, 11) identifies two objectives “(i) contributing to transparency by showing how multilateral surveillance works in practice and (ii) identifying areas, *if any*, where improvement can be made to make multilateral surveillance more effective.” (Emphasis added.) This is not a very ambitious work program.

What may be needed is to change the paradigm of IMF surveillance. The Fund might start from the needs and objectives of the international monetary system, work back from that assessment to what it implies about the policies of the systemically important countries, and use the framework to evaluate actual policies. A reasonable, but not the only, place to start this evaluation might be exchange rates. A widespread view is that (a) excessive exchange rate stability or (b) excessive swings (or excessive instability) in exchange rates among the major currencies contribute to imbalances that threaten global prosperity. A framework of this type is John Williamson’s (1985) target zone proposal that he has articulated and advocated for many years in a number of different forms and formats; see also Williamson (2000). An alternative framework might start from an evaluation of global saving and investment. This starting point would be likely to produce norms similar to those associated with Williamson’s target zones or reference rates.

If the IMF were to adopt a new paradigm to use in conducting its multilateral surveillance, the first step would need to be to develop a consensus on that paradigm. The development of such a consensus need not initially involve the major countries. A

substantial subset of other members of the IMF, if they were sufficiently likeminded could initiate the debate. The IMF management and staff also could instigate it.

Given the central role of surveillance as one of the Fund's principal tools and how surveillance relates not only to global economic and financial stability but also to the design and desirability of individual lending arrangements, a number of officials and observers (Brown 2005 and Ubide 2005 to name two) have suggested that the surveillance function become fully independent of the lending and other IMF programs including for the large countries and presumably with respect to regional and global surveillance.³⁶ The IMF as an institution might consist of two subsidiaries, the surveillance subsidiary and the program subsidiary, both reporting to the management (managing director and deputy managing directors) and the executive board. Alternatively, the IMF could be split into two separate institutions. This would be an expensive solution in terms of staff resources and could sow confusion if the two bodies reached different conclusions, which would be reasonable because most important cases come down to a matter of judgment not analysis.³⁷ Goldstein (2005a) would address the surveillance of emerging market economies by more intense concentration on "early warning" surveillance, compared with routine Article IV surveillance.

An unfortunate side effect of the emphasis on the link between IMF surveillance and IMF lending programs has been that the role of IMF surveillance with respect to global economic and financial stability is often viewed as a second-class activity. Moreover, many critics and observers fail to make the distinction between IMF surveillance before a country has a program, for example, with Thailand and Korea in 1996-97, and IMF surveillance after a country has some type of formal program, for example, with Argentina from the start of the 1990s through 2001.³⁸

Exchange Rates and Policies

Exchange rates and exchange rate policies are an important subtopic in surveillance and the associated role of the IMF in the international monetary system. The vagaries of floating exchange rates have produced much hand wringing including from some prominent people. For example, one sample from Paul Volcker (1998) is:

We still hear the siren song that somehow floating exchange rates will solve the problem. That seems to me a strange and sad refrain. The wide swings in the exchange rate of the world's two largest economies, Japan and the US, has been a critically important factor contributing to the instability of East Asia generally. How can there be a 'correct' rate, fixed or floating, for Thailand or Indonesia or the Philippines when the exchange rates of their major trading partners are diverging sharply? How can it be rational for some Asian countries to be

³⁶ US Treasury Secretary Snow (2004) told the IMFC that the United States is open to the idea.

³⁷ One argument that motivates advocates of separating the lending and surveillance functions of the IMF is the perception that Fund staff and management have a bias toward lending to help countries and that this bias clouds their perspective on the advisability of doing so. The counterargument is that if this is a correct depiction, then it reflects a management failure rather than a structural failure.

³⁸ The section on IMF facilities below touches upon the related issue of the link between IMF surveillance and a possible insurance facility in the IMF.

advised to float their currencies while others are urged to stand firm in fixing their exchange rates, even while their competitive positions are deteriorating?

More recently, two former IMF managing directors have commented on the issue. Camdessus (Camdessus et al., 2004):

I still cannot reconcile myself to a degree of instability of exchange rates—every 10 years or so we observe swings of up to 50 percent in the exchange rates of the major reserve currencies—that is so costly for the entire system, so disruptive for vulnerable countries, and acceptable only to (if not welcomed by) those whose job it is to provide profitable cover against those fluctuations.

And de Larosière (Camdessus et al. 2004), coming from a somewhat different perspective:

I also believe the international monetary system is slipping into a semifixed à la carte system where some countries choose their exchange rate peg (often undervalued) to take the best advantage of their export capacities. The question is what should the IMF do about this situation?

Morris Goldstein (2005a) has an answer to de Larosière's question. The IMF can and should pursue much more aggressively countries that engage in "currency manipulation" by pegging their exchange rates for extended periods of time at undervalued levels while piling up foreign exchange reserves and frustrating the international adjustment process. Bergsten (2005) echoes his colleague.

Managing Director de Rato in his report to the IMFC (IMF 2005g) called for a "deeper treatment of exchange rate issues" and noted that the executive board had held a seminar on operational aspects of moving toward greater exchange rate flexibility. However, the staff paper prepared for that discussion (IMF 2004a) was decidedly cool to regimes of floating exchange rates. It stressed that four ingredients are needed successfully to make the transition: (1) deep and liquid foreign exchange markets, (2) a coherent intervention policy, (3) an appropriate alternative nominal anchor such as inflation targeting, and (4) adequate systems to review and manage public and private sector exchange risks. If those are the tests for success with a flexible exchange rate regime, few countries with floating exchange rates are successful practitioners because most of them would fail one or more of those tests. This is not helpful IMF staff guidance.

It is not surprising that the IMF staff was so timid in its paper because the executive board for which it works and many national authorities for whom the executive directors work are deeply divided on these issues. Judging by the report of the executive directors' discussion (IMF 2004d) as well as ample other evidence, many policymakers are far from convinced that exchange rate flexibility is ever desirable. Adding more cautions to those advanced by the staff, for example, the executive directors (a) voiced the familiar refrain that no single exchange rate regime is appropriate for all countries in all circumstances, without adding the qualification that it can be very costly to change regimes; (b) called for more work on moving toward greater

exchange rate stability, for example by joining regional exchange rate arrangements; and (c) stressed the need to develop a global monitoring system for hedge funds if floating is to be successful, implying incorrectly that hedge funds are the most important source of speculation and exchange rate volatility in the international financial system.³⁹

If further evidence is needed to buttress the view that the IMF institutionally does not think consistently and coherently about exchange rates and exchange rate policies, consider two IMF reports on East Asian exchange rate arrangements that were completed in the fourth quarter of 2004. In the concluding statement of the Article IV mission to Korea (IMF 2004f) the staff “strongly supports the official policy of allowing the won’s external value to be determined in the market, with intervention limited to smoothing operations.” However, it was only shortly after this statement was released on October 28 that the Korean authorities scaled back their massive intervention operations and allowed the won to appreciate sharply over the balance of the year. The IMF staff praised a nonpolicy!

In contrast, in the documents associated with the Article IV consultation with Hong Kong conducted at essentially the same time (IMF 2005e), the staff assessment is that the authorities’ “response to appreciation pressures over the past year has enhanced the resilience of the LERS [linked exchange rate system, i.e., peg to the US dollar]. The LERS remains robust and the staff continues to support the authorities’ commitment to it.”⁴⁰ In February 2005, the executive board (IMF 2005e) echoed the staff view, “They reiterated their support for the authorities’ commitment to the LERS.” One might reasonably ask how and why a hard peg between the Hong Kong dollar and the US dollar makes any economic sense; the two countries certainly are not an optimum currency area. Wouldn’t a peg to the Chinese yuan make more sense over the long term? Doesn’t the Hong Kong dollar’s peg to the US dollar militate against an early, substantial adjustment of the Chinese yuan against the US dollar? One would hope that the IMF staff and executive board discussed the issue of the long-term viability of the Hong Kong dollar’s peg and also the short-term what-if issue for Hong Kong of a substantial revaluation of the Chinese yuan. However, such discussions are not hinted at in the public documents. Their absence illustrates the tension between candor and transparency in IMF surveillance.⁴¹

³⁹ The Independent Evaluation Office of the IMF will be conducting a review of the IMF’s advice on exchange rate policy (IMF-IEO 2005d). The review of IMF surveillance over exchange rate policies will touch on two sets of issues (1) members’ choices of exchange rate regimes and (2) the level of exchange rates in terms of competitiveness, exchange rate sustainability, and exchange rate manipulation. The focus will be the post-1998 period. From the perspective of the international monetary system the second set of issues, in particular exchange rate manipulation, is most relevant.

⁴⁰ The LERS at the time was asymmetric in the sense that it was softer on the upside. Subsequently, the regime has been hardened and become symmetric.

⁴¹ A third example is Malaysia. According to IMF 2005a, the IMF staff concluded that in September 2004 the ringgit was undervalued by 3 to 5 percent in real effective terms, clearly an underestimate in the context of the prevailing global imbalances. In contrast, in the case of China the IMF staff has not even gone so far as to say that the yuan is undervalued. Moreover, it was only the executive directors (most of them) not that staff that called for IMF engagement with the Malaysian authorities about their policy alternatives with a view toward moving toward greater (than zero, bilateral) exchange rate flexibility.

Capital Accounts and Financial Sectors

IMF surveillance in practice also extends to members' capital accounts including the size and composition of their external debts and the potential for capital account crises. These crises, in turn, are often closely linked to financial sector development and stability, an area in which the IMF has been assigned a major surveillance role along with the World Bank. In addition, capital controls are a major ingredient supporting exchange rate manipulation. From a global perspective all aspects are integral to the IMF's role in the international monetary and financial system.

As noted in the introduction, IMF work on the financial sector and capital account issues is not fully grounded in the Articles of Agreement. Possibly for that reason as well as others, the IMF's analysis of these issues is widely regarded as not satisfactory. Although the IMF executive board (IMF 2005c) commended the IMF staff on the "continuing success" of the FSAP program, it is well known that many observers think it has serious shortcomings. One point of controversy is that publication of the resulting ROSC modules is voluntary.⁴² A second is that a major systemically important country (the United States) has not had a FSAP.⁴³ Moreover, until 2002 Japan successfully resisted a FSAP review of its ailing financial system. For more than a decade previously the Japanese financial system was widely seen as a threat to Japanese economic and financial stability as well as to global economic prosperity if not financial stability. Many would argue that this episode clearly indicates a weakness of the IMF in dealing with threats to the stability of the international monetary and financial system that originated in the malfunctioning financial sector of a major economy.

The IMF Independent Evaluation Office is conducting a review of the FSAP program, including its links with Article IV surveillance as well as the design and implementation of the FASP. As noted earlier, the managing director has assembled the McDonough Working Group to provide an assessment of the IMF's work on the financial system and capital markets as an input to the IMF's strategic review.

Aside from the issue of authority, three basic issues are involved in the dissatisfaction with the IMF's work on capital account and financial sector issues. First, the culture and work of the IMF is dominated by macroeconomists and that emphasis carries over into the work of the area departments, which are ill equipped to analyze, or uninterested in, financial sector and capital market issues, reflecting either understaffing or staff with the wrong skills. Second, substantial IMF staff resources are devoted to the treatment of these issues, but the institutional payoffs are not associated with good analyses of particular problems. Instead, the major rewards are forthcoming for provocative overall assessments that are provided to the executive board and the general public. Third, when it comes to country surveillance in these areas, not only is it not well integrated with other aspects of surveillance but also it is, if anything, too comprehensive and lacking in prioritization.

⁴² Sixty percent of the countries with completed ROSC modules have allowed a total of 75 percent of the results to be published.

⁴³ The only other G-7 country that had not had a FSAP is Italy, which is currently undergoing a review. The only other non-G-7 G-10 country that had not had a FSAP is Belgium.

Turning to the broader but related issue of capital account policies, as is well known, the membership of the IMF debated during 1996–97 whether the IMF Articles of Agreement should be amended (1) to update and clarify the role of the IMF with respect to capital account transactions, (2) to establish capital account liberalization as an objective for IMF members, and (3) to establish the IMF’s jurisdiction with respect to capital account matters.⁴⁴

This initiative foundered on the fallout from the East Asian financial crises. Many commentators that should know better, including in the financial press, demonized the G-7 and the management of the IMF for this initiative. The facts are quite different. Stanley Fischer (1998) summarizes the case quite well:

The increasing importance of international capital flows is a fact that needs to be better recognized in the laws and agreements that help bring order to the international economy and to the process by which individual countries liberalize their capital accounts. The proposed amendment to the IMF’s Articles of Agreement will serve this purpose and the international community as well.

The statement attached to the Interim Committee’s communiqué of September 21, 1997 issued in Hong Kong is quite balanced and circumscribed. It speaks of the growing importance of private capital movements and the necessity to ensure the orderly liberalization of capital flows. It states that the IMF is uniquely placed to assist this process and asserts the Committee’s view that the Fund’s new mandate in this area should be “bold in its vision, but cautious in its implementation.” The executive board in its work on the proposed amendment was called upon to make liberalization of capital movements one of the purposes of the Fund and to extend the Fund’s jurisdiction over the liberalization process, but to do so with safeguards, transitional arrangements, flexible approval processes, and in recognition that in the new world of liberalized capital movements “there could be a large need for financing from the Fund and other sources.” As noted, the executive board did not complete its work.

Part of the controversy that emerged in the wake of the East Asian financial crises, the Brazilian crises, the Russian crisis, Turkey’s crisis, and the Argentina debacle concerned not the aborted effort to amend the IMF Articles Agreement with respect to capital account liberalization but the extent to which the Fund had been pushing capital account liberalization willy-nilly. The report of the IMF-IEO (2005a) did not confirm this accusation. It finds no evidence that the IMF used its leverage to push countries to move faster than they were willing to go in liberalizing their capital account transactions. Fund staff did in general encourage those countries that wanted to do so to move ahead without paying sufficient attention to the risks involved and proper sequencing of the liberalization and the interaction with domestic financial sector development.

This lack of attention to sequencing and financial sector development was caused in part by the absence of an official IMF position on capital account liberalization that allowed

⁴⁴ Capital account liberalization covers two broad areas: (1) cross-border access via direct investment and the ability to provide services by institutions that operate in the financial sector and (2) capital account flows or financial transactions. The first area is within the jurisdiction of the World Trade Organization (WTO). The concern of some was that in the absence of a clear definition of the jurisdiction of the IMF over the second area, the WTO would further expand its mandate to cover this area as well.

individual staff members the latitude to espouse their own disparate views when it came to advising members on these issues. The IMF-IEO report recommends increased clarity on these matters and greater attention to supply-side aspects of international capital flows involving principally the industrial countries and efforts, for example, to limit herd behavior on the part of investors.⁴⁵

Where is the IMF likely to go with the issue of the IMF's role in capital account liberalization? Peretz (2005) advocates revisiting the consensus of 1996–97 and reviving the idea of an amendment to the IMF Articles of Agreement on this topic.⁴⁶

Jack Boorman (2004) also advocates revisiting this issue on jurisdiction grounds vis-à-vis the WTO. He also sees continuing potential for pressure on IMF resources from poorly designed and implemented liberalization programs. However, he cautions that first the IMF and its membership would need to clear the air on several issues. (1) What was the IMF advising member countries with regard to capital account liberalization in the early and mid 1990s? The IMF-IEO appears to have dealt with this issue, although critics, being critics, no doubt will not be satisfied. (2) The IMF needs to integrate the lessons of the past decade with respect to capital account liberalization into its regular operations. This process seems to be underway, but far from complete to the general satisfaction of most members. (3) The motivation of the amendment needs to be made clear. In Boorman's view the motivation should be "to fill a regulatory gap in the international institutional structure and, by making liberalization a purpose of the Fund and giving the Fund authority, to coordinate this activity better within the Fund and, perhaps, even provide the resources needed to carry out the associated responsibilities."

The IMF's executive board has discussed more formally reopening the issue of an amendment to the IMF Articles of Agreement with respect to capital account liberalization in the context of the Fund's medium-term strategy. Managing Director de Rato reported to the IMFC (IMF 2005g, 7), "most Directors did not wish to explore further at present the possibility (raised in 1996-97) of giving the Fund authority over capital movements, although a number of them felt that the Fund should be prepared to return to this issue at an appropriate time."

At the IMFC meeting on April 16, 2005, finance ministers from two G-7 countries, Gordon Brown from the United Kingdom and Domenico Siniscalco from Italy, expressed support for greater IMF activity in this area. On the other hand, Burhanuddin Abdullah (2005), Governor of the Central Bank of Indonesia (speaking for a number of ASEAN countries), was firmly negative:

On the issue of capital account liberalization, we are of the view that the Fund should not play a 'central' role in this area. Past and recent experiences have clearly demonstrated that capital account restrictions are justified in some cases. At the same time, countries are already proceeding along the liberalization path, as they see fit, and as warranted by their own set of economic and financial

⁴⁵ Williamson (2005) addresses many of these issues in more detail than does the IMF-IEO report, and various IMF *Global Financial Stability Reports* have emphasized these issues.

⁴⁶ His position is not altogether surprising as he was a British official at the IMF in the 1990s, and the UK government was a principal advocate for change at that time.

circumstances. Therefore, the role for the Fund should be to ensure effective surveillance and that the necessary supporting infrastructure, especially adequate financial resources and appropriate financing instruments, are in place to help countries faced with capital account vulnerabilities or difficulties.

The Fund's role with respect to capital account liberalization is an important issue that the IMF will have to address because it is central to the IMF mission in the 21st century. It is also closely linked to the IMF's involvement in financial sector issues. However, the members of the IMF have their work cut out for them if they are to achieve consensus on how the Fund should address these important topics.

Regional Arrangements

A final important area of the IMF's interface with the international monetary and financial system involves the Fund's relations and interaction with other formal or informal international organizations.

On the more formal side, first, are the Fund's relations with its sister Bretton Woods institution, the World Bank, where, despite frequent protestations to the contrary from the leadership of the two organizations, it is widely believed that turf battles are frequent and cooperation and coordination fall short of what a rational person would view as desirable.⁴⁷

Second, relations with the Bank for International Settlements (BIS), at present, are generally considered better than in the past largely because the BIS is seen less and less as a rival to the IMF.⁴⁸

Third, relations with the WTO are uneven, but, as noted, one motivation for amending the IMF Articles of Agreement with respect to capital account liberalization was to establish the capital account as the IMF's turf at least with respect to financial flows and to prevent the WTO from extending its authority.

Fourth, the IMF has generally cordial relations with the OECD, with its more limited membership; here the competition is largely in the area of research and ideas.

Finally, the IMF's involvement with the regional development banks has been limited except in crisis situations where the Fund itself or its major shareholders have sought to bring

⁴⁷ Turf battles and coordination are problems within the institutions as well.

⁴⁸ A resolution passed at the Bretton Woods conference in 1944 called for the dissolution of the BIS, as did the US legislation approving the Bretton Woods agreements. Partly reflecting these sentiments, the Federal Reserve did not take up its seat on the BIS board until September 1994 (Charles Siegman 1994). Since then the BIS has considerably expanded its membership and the scope of its activities, celebrating its 75th anniversary in 2005. However, the BIS no longer is involved in financing or helping to finance international rescue operations as it did from its inception through the late 1980s; it played a limited window-dressing role in contributing to the Mexican package in 1995. Thus, the BIS and its central bank members collectively are not in direct competition with the IMF except in the area of ideas, for example, assessments of the global economy and critiques of crisis management. The BIS does provide a home for, and some of the resources to support the secretariat of, the Financial Stability Forum (FSF), which some within and outside the IMF see as a rival to the IMF as an institution of global financial governance.

those institutions, in particular the Inter-American Development Bank and the Asian Development Bank, into consortiums helping to provide financing to ameliorate external financial crises and to deal with the underlying policy challenges in member countries. On the other hand, the regional development banks have been known to support countries where the IMF has problems with their macroeconomic policies. The Asian Development Bank is also perceived to be a strong supporter of the establishment of an Asian Monetary Fund as an alternative to the International Monetary Fund.

With respect to less formal organizations and nascent efforts to promote regional cooperation, the Fund's involvement is decidedly more ambiguous. For example, it is asserted (Zeti 2004) that it was Michel Camdessus who initially suggested in November 1996 in Jakarta that the East Asian economies get together and establish a process of regional surveillance along with a facility for mutual financial assistance.⁴⁹ When this proposal resurfaced less than a year later as a Japanese grandstand proposal for an Asian Monetary Fund (AMF) that would have been of no use in dealing with the East Asian financial crises because it would not come into existence for years, Camdessus was on the side of those who opposed the proposal. However, the proposal is not dead; it lives on in the form of the Chiang Mai Initiative and nascent Asian Bond Fund, and it has considerable support not only within the region but among people, including some within or close to the US government, who think that regional arrangements should shoulder a greater share of the general burden of emergency financing, in particular, and policy advice as well.

The question is what should be the IMF's posture vis-à-vis such regional arrangements? Raghuram Rajan (2005a) has floated the idea that the IMF might seek the promotion of regional subsidiaries. If the regions with the mini-IMFs don't like being subsidiaries of a global institution in Washington dominated by the G-7 countries, how should the IMF seek to structure its relationship with independent organizations with essentially the same mandates to maintain economic and financial stability except in a regional context? Can one be confident that future external financial crises will have asymmetrical effects on countries in the region, facilitating mutual assistance, or will the crises continue to have symmetrical effects, rendering the possibility of such assistance nugatory? Can the global monetary system function effectively with more than one set of understandings, conventions and rules, for example about the trade-off between financing and adjustment or about the ultimate goal of capital account liberalization? In other words, is the global standard IMF conditionality or something weaker? These are big issues that the general membership of the IMF will not be able to continue to duck.

More prosaically, how should the IMF position itself vis-à-vis various efforts at regional integration? The European project has been ongoing for five decades. In East Asia, Africa, and Latin America integration efforts are more recent. The IMF now conducts formal regional surveillance exercises with respect to the Euro Area, the Central African Economic and Monetary Community, the West African Economic and Monetary Union, and the Eastern Caribbean Currency Union. In an era of scarce resources, the IMF might well want to scale back its surveillance activities with respect to the individual members of those regional arrangements while concentrating on the larger units. At the same time, it might be expected to publish the

⁴⁹ The official published text (Camdessus 1996) does not support this interpretation.

documents that it produces in connection with its participation in peer-review processes such as the G-7 and various regional groups.

One particular topic that should be on the IMF's agenda in its role in the international monetary system is the prospect that the euro may emerge as a serious rival to the US dollar as the principal international currency and international reserve currency. In recent years, the amount of verbal and, perhaps, financial speculation about international reserve diversification has increased dramatically. I have written about this issue (Truman 2005b). I have proposed an international reserve diversification standard that builds on the disclosure requirements with respect to international reserves (the "reserve template") in the IMF's Special Data Dissemination Standard (SDDS). Under this proposal, all major reserve holders would be expected regularly to disclose the currency composition of their foreign exchange reserves. In addition, they would be required to declare a benchmark, or adhere to a general benchmark, for the currency composition of their reserves. If they changed their benchmarks they would commit to doing so only gradually over a period of, say, five years.⁵⁰ This would be a market-oriented approach reserve diversification in contrast with earlier proposals to create an IMF substitution account to facilitate the relocation of reserves from dollars into SDR last considered in 1979–80 (Boughton 2001, 936–43).

IMF Governance

The International Monetary Fund is an international institution established by an international agreement that is embedded in the legal systems of each member.⁵¹ The institution is owned by and responsible to its member governments. Those governments, in turn, are responsible to their own citizens either in broad terms or more narrowly in the case of elected governments. Accountability, transparency, and legitimacy are at the core of the IMF existence vis-à-vis both its member governments and the world at large regardless of how various governments or interest groups may agree or disagree on how those principles should be applied.

At the same time, the Fund is an institution of global cooperation and, I would argue, global governance, even though many observers reject that term. As such the IMF is held responsible for its policies, actions, and inactions by international public opinion and the various groups that seek to influence or affect those opinions. This reality creates tension and controversy.

The emergence of a larger number of systemically significant countries over the past 60 and, in particular, the past 30 years along with technological change that facilitates the instantaneous, global transmission of information—complete, incomplete and distorted—has forced the IMF itself and its members to recognize the need for governance changes. Governance and balance in governance is important to the smooth functioning of the international financial

⁵⁰ It would follow that marginal increases or decreases in foreign exchange reserves, as the result of intervention, should be allocated immediately according to the benchmark.

⁵¹ In the United States the governing law is the Bretton Woods Agreements Act first passed in 1945 and subsequently amended. Although in principle the international law incorporated in the IMF Articles Agreement should take precedence over domestic law, in the few cases that have been decided in national courts the IMF Articles have not always received that treatment.

system as a whole because if the IMF is respected, all countries have increased incentives to play by its common rules.

IMF governance is a broad topic. A principal issue is the quotas of individual members. A second important issue involves the process of choosing the senior management of the institution. Third, IMF governance involves relationships between the governors of the IMF (who meet once a year but can be asked to vote by mail), the IMFC subset of governors (meeting twice a year), the executive board drawn from national capitals, the management, and the staff. A fourth important subtopic is the executive board itself with respect to its powers, the qualifications of its members, the number of members, and the distribution of seats among the members of the IMF. The technical qualifications and geographic origins of the IMF staff might be regarded as management issues, but for some they are governance issues. Finally, under governance, one needs to consider how the institution as a whole relates to ad hoc groups, in particular groups of countries, for example, the G-7 industrial countries, the G-10 larger group of such countries, the G-11 group of developing countries, the G-20 combination of systemically important industrial and nonindustrial countries, as well as regional groups such as the European Union. In addition, self-appointed NGOs, academics, and other observers of the IMF's operations are quick to offer criticisms.

It is fair to argue, as did Williamson (2001, 109), that one should first decide what the Fund should do before addressing its governance. In principle, it should matter with respect to the governance of the Fund whether it is to be a smaller institution than it is today with limited lending and other responsibilities, a larger institution with an expanded mission and scope for lending, or remain the same. The view of the horse before the cart is more pertinent to an institution that is just being established. The IMF has been around for more than 60 years, and the issue is how (whether) it should be reformed, recognizing that reforms are likely to be evolutionary.

Accepting that IMF reform may well be evolutionary, most observers agree that the IMF governance is a central element in any successful reform process that has any hope of restoring the Fund's global relevance.⁵² The topic emerged with a vengeance in the East Asian financial crises when the affected countries felt that their problems were not addressed as generously and understandingly as they deserved, in part, because the East Asian countries did not have the power and representation in the Fund that they merited based on their economic importance.⁵³

More recently, the Monterrey Consensus (UN 2002a) encouraged:

The International Monetary Fund and World Bank: to continue to enhance participation of all developing countries and countries with economies in

⁵² As noted above, Summers (1999) commented on this topic in the context of a broader discussion of IMF reform as did the 1994 Bretton Woods Commission.

⁵³ An alternative explanation for the level of support in the East Asian financial crises is that under the influence of its European members who were critical of the scale of support that had been extended to Mexico, Fund management and staff were hesitant to propose large-scale lending. In fact, IMF commitments to Indonesia, Korea, and Thailand average 3.8 percent of GDP compared with 4.6 percent for Mexico, but IMF plus bilateral commitments averaged 9.0 percent of GDP compared with 9.6 percent for Mexico (Roubini and Setser 2004, 125). This is not necessarily the right metric because it makes not adjustment for need or circumstances, but it suggests that the Asian complaint and the European conspiracy view are not broadly supported by the data.

transition in their decision-making, and thereby to strengthen the international dialogue and the work of those institutions as they address the development needs and concerns of these countries.

That encouragement has led to a number of discussions in the Development Committee (Joint Ministerial Committee of the Board of Governors of the Bank and the Fund on the Transfer of Real Resources to Developing Countries) on how to enhance the voice and participation of developing and transition economies in the Fund and the Bank.

The leaders who gathered at Monterrey were not alone in the view that governance should be on the agendas of the Bretton Woods institutions. In one form or another, the topic was mentioned by 23 of the 60 commentators in September 2004 on how the structure of the Fund and the World Bank should be changed (Emerging Markets 2004); this was, by far, the most common of any of the responses.

The issues involved have been highlighted in reports of the managing director to the IMFC and in the IMFC's communiqués.⁵⁴ The G-24 ministers have been more strident (G-24 2005):

Ministers note that the BWIs' [Bretton Woods institutions] governance structures have not evolved in line with the increased size and role of emerging market, developing, and transition countries in the world economy. Moreover, the role of small and low-income countries in the decision-making process is extremely limited. Ministers stress the need for concrete actions to reduce the democratic deficit and enhance the voice and participation of developing countries in decision-making at the IMF and World Bank, as called for in the Monterrey Consensus. They express disappointment that no progress has been made on this issue. The current under-representation of developing countries in the IMF and the World Bank executive boards undermines the legitimacy and effectiveness of these institutions.

Aside from the symbolism and power politics involved, IMF governance involves complex tradeoffs between the legitimacy and operational efficiency of the Fund in conducting its business (Cottarelli 2005). Choices have to be made if there is to be progress on overall IMF reform. The IMF will not be able to continue successfully without adjustments in its governance structures. Lane (2005) links action on various governance issues to the resolution of tensions within the Fund concerning such contentious issues as how best to deal with emerging market crises, the proper scope of IMF conditionality, the phenomenon of prolonged use of IMF resources, and the IMF's relationship with low-income countries.

The balance of this section looks at four aspects of IMF governance: (1) shares of IMF quotas, (2) choosing IMF management and staff, (3) reforming the executive board, in particular,

⁵⁴ "The IMF's effectiveness and credibility as a cooperative institution must be safeguarded and further enhanced. Adequate voice and participation by all members should be assured, and the distribution of quotas should reflect developments in the world economy" (IMFC 2005).

the distribution of seats (chairs) on the board, and (4) the IMF's relations with various international steering groups.

Quotas and Voting Power

IMF quotas are the principal issue in IMF governance because quotas are the building blocks for many aspects of the IMF and its operations. A country's quota directly translates into voting power because the number of votes a country has in the Fund is based primarily on the size of its quota.⁵⁵ What matters is not the total number of votes, of course, but the relative size of quotas because formal voting is generally by weighted majority with most issues requiring only a simple weighted majority; a few issues require either 70 percent or 85 percent majorities.⁵⁶ The United States with the largest quota has 17.08 percent of the votes, and therefore has can block (veto) change on the last set of issues.⁵⁷ In addition, a member's quota fixes how much that country may be called upon to lend to other members through the Fund. It also determines more loosely how much a member can borrow from the Fund.

The size of the Fund in terms of total quotas in the Fund must be reviewed at least every five years. Some of those reviews have been prolonged beyond five years.⁵⁸ Roughly half—8 of 13—of the reviews have resulted in an increase in the size of the Fund.⁵⁹ Currently the IMF is in its 13th quota review cycle. It is scheduled to be completed by January 2008. Aside from determining the overall size of the Fund, a review that involves an increase in overall quotas can affect the relative size of quotas and therefore a country's voting power.

Negotiations over IMF quotas have traditionally been informed by formulas that involve (1) GDP at current market prices (an indicator of economic size and a country's capacity to contribute to the Fund), (2) official international reserves (an indicator of a country's capacity to contribute to the Fund), (3) current payments (an indicator of openness as well as of potential need to borrow from the Fund), (4) current receipts (another indicator of openness as well as of potential need to borrow from the Fund), and (5) the variability of current receipts (another indicator of potential need to borrow from the Fund). These five variables can be measured, often with difficulty, over periods of varying length and combined according to a variety of different weights.⁶⁰

Starting with the Eighth Review of Quotas in 1983, five different formulas have been used to generate calculated quotas. Calculated quotas often differ substantially from actual quotas because of the tension between actual historical quotas and differences in the pace of

⁵⁵ A member has 250 basic votes regardless of the size of its quota and one vote per 100,000 SDR of its quota.

⁵⁶ Amendment of the IMF Articles of Agreement requires a weighted majority of 85 percent of and the positive votes of 60 members.

⁵⁷ The US quota in the IMF is SDR 371,493 hundred thousand. As August, 2005 its quota share was 17.40 percent.

⁵⁸ One review was concluded inside the five-year window.

⁵⁹ New members of the Fund are given quotas commensurate with the size of quotas of existing members (often a complex negotiation), which increases the overall size of the Fund while reducing the quota and voting shares of existing members.

⁶⁰ In many cases, data has to be estimated. In addition, in recent discussions and calculations the last variable is calculated as the variability of current receipts and net capital inflows.

countries' economic development.⁶¹ An adjustment factor is applied to each formula so that it yields the same overall total. A country's calculated quota is the larger of the original "Bretton Woods formula" and the average of the two smallest of the four remaining formulas, appropriately scaled. In most quota reviews that result in an increase in total quotas, the increase in a country's individual quota is composed of some combination of its current quota share, an adjustment to bring some or all countries closer to their calculated quota shares, and occasionally ad hoc adjustments for countries whose quotas are way out of line. Everything is scaled to the new overall size of the Fund.

In the latest publicly available estimates, a distribution of quota shares based on calculated quotas would boost the share of advanced countries 6.7 percentage points relative to actual quota shares and reduce the shares of developing countries 3.9 percentage points and transition economies 2.8 percentage points (IMF 2004g).⁶² However, within the group of developing countries the calculated quota share for the subgroup of Asia (including Korea and Singapore) would be 4.6 percent points higher than its actual share of 10.3 percent.

Moreover, within each category of countries, a distribution of IMF quotas based on calculated quotas would bring about large adjustments in relative voting power. In the 2004 estimates, the US share would rise 2.4 percent, Germany's would rise 15.3 percent, but France's would decline 13.1 percent. Among developing countries, China's share would rise 55.5 percent, India's would decline 47.3 percent, and Venezuela's would decline 67.4 percent, but Mexico's would rise 57.4 percent and Korea's 177.4 percent, which would make it the 11th largest quota in the Fund. Among transition economies, Russia's share would decline 52.3 percent, but the Czech Republic's share would be boosted 18.4 percent. The size of these differences reflects a combination of inertia that anchors shares in historical relationships to each other and of differential rates of economic and financial development.

Vijay Kelkar, Praveen K. Chaudhry, Marta Vanduzer-Snow, and V. Bhaskar (2005) dramatically point to some of the voting power anomalies associated, in their view, with the current quota structure.⁶³ They note that the combined votes on the IMF executive board of Brazil, China, and India are 19 percent less than the combined votes of Belgium, Italy and the Netherlands at the same time (2000-2001) that their combined GDPs at market exchange rates are 23 percent higher, their GDPs at purchasing power parity (2000 PPP estimates) are four times higher, and their populations are 29 times higher. Note, however, that the percentage difference between the combined calculated quota shares of the two groups of countries, based on data through 2002 (IMF 2004g), would be unchanged from the percentage difference in their combined actual quotas.⁶⁴

⁶¹ The historical relationship dates back to the Bretton Woods conference in 1944 where a formula was used as a guideline for establishing initial IMF quotas but the formulas' results were only indicative. A political agreement was required to set the quotas for the important countries and establish their relative quota shares.

⁶² In these calculations, the current quota share of advanced countries (for these purposes industrial countries plus Cyprus and Israel) is 61.6 percent, the share of developing countries is 30.9 percent, and the share of transition economies is 7.5 percent.

⁶³ Vijay Kelkar has coauthored a number of papers on IMF governance; see references.

⁶⁴ The calculated quota shares of Italy and the Netherlands are larger than their current actual quotas, outweighing the implied decline in Belgium's quota; at the same time, the large increase in China's calculated quota is partially offset by large decreases in the calculated quotas of India and Brazil.

The quota formulas themselves are subject to the same conflicting forces of inertia and of differences in the pace of countries' economic and financial development.⁶⁵ Consequently, many members of the IMF advocate changing the quota formulas to simplify the formula, preferably to one standard with no more than four variables, and to update the variables. Not surprisingly, this is not an exact science.

In 2000, an outside committee chaired by Richard Cooper (IMF 2000) recommended a simplified formula based on two variables: GDP (the potential ability to contribute to the Fund) and the variability of current receipts and net long-term capital flows (an alternative measure of the potential need to borrow from the Fund), with the coefficient on the former twice that on the latter composite. This proposal did not attract a lot of support inside or outside of the IMF.

Others (such as Kelkar with his various coauthors) have suggested replacing GDP at market prices and current exchange rates with GDP on a PPP basis, which *ceteris paribus* would tend to boost the quota shares of developing countries. Bryant (2004) proposes including population in the formula along with GDP. Introducing this variable would also increase the voting power in the IMF of developing countries as a group, but would benefit poorer developing countries relative to the voting power of richer developing countries.

Even technical adjustments in the way the quota formulas have been estimated can matter; Buira (2005, 27) reports that excluding intra-area trade for the calculated quotas of the 12 Euro Area members of the IMF would reduce their calculated quota shares by 11.4 percentage points.⁶⁶ On the other hand, the latest estimated calculated quotas reported by the IMF (2004g) would boost the combined quota share of the Euro Area by 4.5 percentage points relative to their combined share of actual quotas. Thus, if EU and Euro Area quotas are to be reduced, as many have called for, either the quota formula will have to be changed or the interpretation of the inputs will have to be substantially modified, for example with respect to intra-EU trade.

A large group of small countries is particularly interested in adjusting the number of basic votes for each member of the IMF—250 votes per country. It is pointed out (Buira 2005 and Kelkar et al. 2005 -- both sets of coauthors) that basic votes represented about 11 percent of total votes in 1945 and represent 2 percent today. The number of basic votes per member has been unchanged and the number of members of the IMF has increased substantially, but the increase in the overall size of quotas has swamped the latter effect. (An amendment of the IMF Articles of Agreement would be required to change the number of basic votes each country would receive.) Kelkar calculates that if there were an increase in basic votes that restored their share of total votes to 11.3 percent and if the remaining 89.7 percent of quota shares were distributed on according to GDP on a PPP basis, the voting share of developing countries would rise by 11.5

⁶⁵ Dirk Messner et al. (2005) propose increasing the weight of developing countries' votes in the IMF and at the same time revising the IMF Articles of Agreement so that the voting shares would be recalibrated every 10 years. The problem, of course, is that the formula used to increase the weight of developing countries could also lead to a reduction of their weight at the time of recalibration.

⁶⁶ Lorenzo Bini-Smaghi (2004) has a similar result, a reduction in calculated quotas of 11.7 percentage points, and a reduction in voting power of 9.1 percentage points for the Euro Area. For the EU-25, Bini-Smaghi estimates that the reduction in calculated quotas would be 15.1 percentage points, and the reduction in voting power 12.6 percentage points, from which the US voting power would receive a boost of 4.2 percentage points.

percentage points, with the group shares of developing countries in Africa, Asia and the Western Hemisphere all rising, and the voting share of advanced countries would decline 10.8 percentage points. Moreover, the US voting share would increase 2 percentage points, more than preserving the US veto.⁶⁷

On the other hand, adjusting the number of basic votes each country receives would not do much for most groups of countries. Ngaire Woods and Domenico Lombardi (2005) point out that the voting share of the largest 24-country African constituency would rise from 1.99 percent to only 2.81 percent. Merely adjusting basic votes is a “feel good” solution to the problem of voting power in the IMF, and a high cost solution because it would require an amendment of the IMF Articles of Agreement. Woods and Lombardi propose a more radical reform involving expanding the double-majority approach where certain decisions require various weighted majority votes plus various majorities of members. This could increase the scope to block specific changes, but could well make it more difficult to implement change except as part of a carefully assembled package of proposals. However, it would potentially increase the leverage of the sub-Saharan African countries whose two constituencies include 43 countries, 24 percent of the total membership of the Fund.

Because the United States has more than 15 percent of the votes, it can block (veto) certain major decisions of the IMF; very few affect the ongoing operations of the IMF. Nevertheless, many observers feel that the US veto gives the United States undue leverage over the day-to-day decisions in the IMF.⁶⁸ However, the United States could only voluntarily lose its veto because it could always block any amendment of the IMF Articles or quota increase that had the effect of reducing the US voting share below 15 percent.⁶⁹ Most proposed adjustments in the quota formula, aside from those introducing a heavy weight on population or international reserves, would not adversely affect the US quota share. While a case can be made that it is in the US interest to reduce its quota share voluntarily so that it no longer can be accused of having undue influence over the Fund, such an action is far from likely except in the context of a very large package of IMF reforms that the United States strongly supports.

A potentially more promising route would involve the establishment of a single EU or Euro Area constituency that would also have more than 15 percent voting power, creating a “contestable” veto power with identical quotas for the United States and the European Union. If their voting shares were both about 18 percent of the overall total, this would free up about 13 percentage points to reallocate to other countries reflecting their relative economic

⁶⁷ The US voting share would decline about 1.5 percentage points but remain above 15 percent if the contribution of basic votes to total votes were restored to the 1945 level. This decline would be more than offset by the switch to quota shares based only on PPP-based GDP.

⁶⁸ The basis for the presumption is understandable, but I have witnessed too many cases where the IMF has not followed US wishes to worry a great deal about such problems. What is true is that the United States historically has cared about the IMF as an institution and about its day-to-day operations.

⁶⁹ In principle, it might be possible to admit by majority vote enough new members with large enough quotas to drive the US voting share below 15 percent, but that would take an increase in IMF quotas of more than 14 percent via such a process. There are not enough non-member countries in the world to generate such an increase where each new member’s quota is constrained by the size of the quotas of comparable countries, based on the five quota formulas scaled to the current size of the IMF.

development.⁷⁰ Alternatively, both the United States and the EU could agree to reduce their voting power below 15 percent as part of a grand bargain on IMF reform, whose outlines at this point are decidedly blurred, which would free up an even larger share of quotas and votes for reallocation.

Notwithstanding the political and technical complexities, the issue of the relative size of quotas and voting power is central to reforming IMF governance. Boorman (2004) argues that the Europeans must take the lead. I have argued (Boyer and Truman 2005 and Truman 2005a) that the United States has some leverage, albeit in the nuclear category, of the European position. Every two years, the United States has an opportunity to block the continuation of the executive board at its current size of 24 seats, rather than the 20 called for in the IMF Articles, because the vote to continue to raise the number of seats to 24 requires an 85 percent (weighted) majority.

Europe holds the key to progress in this area, and the pressure is rising. Abdullah (2005) expressed in unusually strong terms the frustration on this issue felt by East Asian countries:

Finally and most importantly, we stress the criticality of addressing serious shortcomings in the Fund's governance structure, as well as a lack of sense of ownership of some members. In order to enhance the effectiveness and legitimacy of the Fund, all members of the institution must feel a sense of ownership. They must feel well represented and that they have a say in decisions taken by the Fund. As such, all members should have adequate voice and participation.

In this regard, our constituency strongly believes that countries' quota shares have to be reviewed and updated so that they reflect countries' relative positions in the world economy. A viable solution could be a rebalancing of quotas within the existing total whereby countries that are over-weighted could voluntarily transfer quota shares to countries that have grown quickly due to successful economic performance and are now grossly underrepresented. Without advancement in such an important area, the Fund's credibility will continue to be undermined due to the monopolistic behavior of large countries with veto power. In particular, the Fund runs the serious risk of losing its relevance in Asia unless the Fund effectively engages Asian countries by addressing this issue of the lack of voice and effective participation in the decision making process. The influence, credibility, and legitimacy of the Fund are contingent upon these changes. In this light, the upcoming 13th General Review of Quotas will provide an opportune time to achieve this objective, which should not be delayed any further. The ultimate goal is to see a Fund that performs important functions for the benefit of all member countries and cherishes the practice of consensus building in reaching Board decisions.

The ASEAN + 3 (China, Japan and Korea) finance ministers in May 2005 pledged to work together on this issue. The trilateral finance ministers (China, Japan and Korea) made a similar statement at the same time. The Japanese Finance Minister Sadakazu Tanigaki (2005) had already spoken eloquently about this topic in April, "The IMF needs to listen and understand

⁷⁰ EU countries currently have 32 percent of IMF votes.

the frustration and concerns Asian countries feel toward it and make serious efforts to address these concerns. Unless the IMF responds effectively to the above, it could irrevocably lose relevance in Asia and ultimately in the world.” He cited two concerns: first, Asian countries’ status in the IMF in terms of the distribution of quotas, board members, and staff, and second, whether the institution is making sufficient efforts to prevent, manage, and resolve capital account crises.⁷¹

The United States has taken a forward-leaning position on this issue. At the IMFC meeting in April 2005, US Treasury Secretary Snow (2005) stated:

We believe the time is ripe to start considering how to address these inter-related issues [IMF representation should evolve along with the evolution of the world economy and the world economy is now ahead of the evolution of the IMF]. The IMF’s liquidity is at an all-time high. But the fact that the IMF does not need an increase in its resources need not impede change. A rebalancing of quotas from ‘over-represented’ countries to the ‘under-represented’ within the existing total could yield substantial progress. This will not be an easy task, but it can be achieved with boldness and vision to help modernize the Fund.

These are clearly complex issues, and careful consideration and consultation is needed to address the full range of concerns. This is important to preserving the global character of the IMF, so that all countries feel they have a rightful stake in the institution.

US Acting Under Secretary Quarles (2005) reiterated the US position in June 2005, including a statement “progress should not, and indeed need not, be linked to an increase in the IMF’s quota resources.” Given the rancorous history of IMF quota negotiations, the US position is naïve at best and cynical at worst. This is the case even if the US position is driven by strategic considerations and US government officials recognize that in the end an adjustment in quota shares will only occur in the context of an increase in the overall size of the Fund. The reason the US position looks as if it is just for show is that individual member countries must consent to any reduction in their quotas. It is highly unlikely that any country will voluntarily reduce its quota so that the amount can be transferred to another country. Moreover, the European countries collectively have more than enough votes to block any increase in total IMF quotas resulting in a reallocation of quota shares that does not satisfy them.

The common EU position on this issue at this point is not forward leaning. Jean-Claude Juncker (2005) stated EU position at the April IMFC:

EU countries support this process [of strengthening the participation of developing countries] and welcome the steps that have been taken so far by the IMF and the World Bank to strengthen the voice of developing and transition countries as well as the renewed focus from IMF management on the importance

⁷¹ Tanigaki did not put forward in his written statement the proposal, which had been attributed in the press to the Japanese government in advance of the meeting of the IMFC, that ASEAN +3 quotas in the IMF should be increased from 13 percent to 20 percent.

of this issue. At the same time it is important to discuss further measures, such as initiatives to further build policy capacity in developing countries, further enhancement of delegation office capacity and overall general measures such as an increase in basic votes.

Readers will note that Junker did not mention reducing the quotas or quota shares of EU members of the IMF. Such an offer will have to wait at least until the hard bargaining begins.

Choice of Management and Staff

The processes used today to choose the managing director of the Fund and the president of the World Bank satisfy few observers, with the important exception of key senior officials and political leaders in the United States and in Europe. The executive boards of the two organizations in principle elect the heads of the organizations. In practice, with a few variations around the edges, the existing convention, by agreement between the United States and (a growing) Europe is that the Europeans propose the managing director of the IMF by an ad hoc internal process and the US president proposes the president of the World Bank. The executive boards subsequently deliberate and elect the individuals proposed. This convention dates back to the start of the institutions. It has been widely criticized for decades, but it persists. Since 1999 two new managing directors of the IMF and one new president of the World Bank have been chosen on the basis of the convention.

Miles Kahler (2001) put forward the most comprehensive proposal for change in this area. His proposal calls for (a) the abandonment of the US-European convention, (b) a selection process based upon developed criteria, (c) expanding the list of candidates to include internal candidates, (d) placing the selection process squarely, rather than indirectly, in the hands of ministers, (e) development of a long list of candidates and later a veto-proof short list of candidates, and (f) reinforcing the process via a two-term limit and a review process at the end of the first term.

Many others advocate change. In the wake of widespread dissatisfaction with the process that resulted in the choice of Horst Köhler as the IMF managing director in 2000, the executive directors of the Bank and the Fund formed working groups to reform the selection processes for the heads of the two organizations (Kahler 2001, 77-78). Those groups did not recommend discarding the US-European convention. Instead, they recommended other changes to the selection process that would involve a more transparent process of choosing the heads of the organizations. The two executive boards endorsed the report in April 2001 as guidance for the process, and IMFC noted the report in its communiqué. However, these efforts had no visible influence on the processes that subsequently led to Rodrigo de Rato's succeeding Horst Köhler in 2004 and Paul Wolfowitz's succeeding James Wolfensohn in 2005.

In an interview as he left the World Bank, Wolfensohn (*New York Times*, May 25, 2005, C5) endorsed a selection process for the Bank in which the president would be selected from a range of candidates in a transparent way, "I would personally wish that one could make these appointments on merit." Horst Köhler (IMF Survey 2004), when he left the IMF, expressed his support for a more transparent selection process that is not limited to a particular country or

region while acknowledging that there will always be an element of politics in the process. Peretz (2005, 27) advocates modifying the process for selecting the managing director of the IMF by taking it out of the hands of member governments and charging a group of “wise men [and women]” to come up with a range of possibilities and appointing the best person for the job regardless of nationality. He also noted that reform of the selection process for the head of the IMF depends on reforms in the selection process for choosing the head of the World Bank and the World Trade Organization, which did modify its procedure somewhat in 2005. The issues involved apply as well to choosing the heads the OECD, the BIS, and the regional development banks.⁷²

Questions about the selection of the managing director of the IMF extend to the selection of the deputy managing directors and the diversity of the staff. The first deputy managing director of the IMF, based on the US-European convention, comes from the United States. Until the mid-1990s, the managing director only had one deputy managing director (DMD). When Stanley Fischer was selected, the number of deputy managing directors was expanded to include two others. To date, two of the DMDs have come from Japan, two have come from Latin America, one has come from India, and one from Africa.

Many members of the IMF complain about a lack of diversity within the senior staff and the staff as a whole. They argue those positions tend to be occupied by people from what are now viewed as “creditor countries,” providing such countries with undue influence over IMF policies and decisions on programs of financial support. With respect to skills, most observers believe that IMF staff hiring and promotion is merit-based; most of the technical skills involved are universal not national or regional. The issue of influence by the governments of the staff’s country of origin is more complex.

The concerns are three. The first concern is about the power and influence of IMF technocrats who are viewed as economists trained in a particular analytical tradition. Most people familiar with disputes among economists and the lack of a Washington Consensus find this concern overblown while not disputing the technocratic foundation of much of the IMF’s work and the influence of technocrats in the organization.

The second concern is geographic diversity. A concern for diversity need not distort a merit-based appointment and promotion process. However, it can well have that effect. Today, the IMF imposes informal limits on hiring nationals from some countries. Despite its very competitive salaries favoring nationals of countries other than the United States, it often has difficulty attracting qualified applicants to Washington.

The third concern is over political influence. Only a fool would argue that politics never enters into decisions by IMF staff and, in particular, by management, but many observers (Bird 2003, Bird and Rowlands 2001, Cottarelli 2005, and Leo Van Houtven 2002) conclude that there is limited evidence of systematic political influence in IMF decisions. Some scholars have found

⁷² The president of the Inter-American Development Bank traditionally comes from Latin America, and the president of the African Development Bank comes from Africa. However, the president of the European Bank for Reconstruction and Development comes from Western Europe (with the number two position reserved for a U.S. national), and the Japanese nominate the president of the Asian Development Bank.

some evidence of political influence (Robert Barro and Jong-Wha Lee 2002). However, their findings are sensitive to specification of the time period and the definition of evidence of influence. As described in Woods and Lombardi (2005), the IMF faces a large number of different types of decisions with the result that at times there may be a strong consensus on those issues; at other times, shifting coalitions of countries push particular programs or views.

Chairs and Reform of the Executive Board

The executive board of the International Monetary Fund is charged with the supervision of the activities of the institution. The executive directors are appointed or elected by member governments. They are paid by the Fund. As such their roles are somewhat ambiguous. Are they to represent the views of the governments that chose them or the interests of the institution as a whole when those interests diverge? Does the role of the Board need to be strengthened (Van Houtven 2004)? Should its scope and powers be broadened Rajan (2005a)? Should its size be increased to reflect the increased membership of the Fund or should its size be reduced or seats reallocated to make it more efficient or representative?

Peter Kenen et al. (2004), Peretz (2005) and Rajan (2005a) either favor or are favorably inclined toward a nonresident executive board, with senior officials from capitals meeting regularly, but certainly not the current three days a week, to make important decisions. This reform would tend to strengthen the role of the staff and management of the Fund at the same time that it receives more overt political direction on key issues.

De Gregorio et al. advocate a board independent of governments in the model of independent central banks. Lane (2005) sensibly criticizes this view. He argues that independent central banks have reasonably well defined objectives focused more or less precisely on price stability. Evaluation of the performance of the IMF involves determining whether the institution's advice was sound and whether it was appropriate for the Fund to lend to particular countries in particular circumstances. Those are questions that require judgment *ex ante* and later invite second-guessing without agreed quantitative tests that can be applied.

Kelkar et al. (2005, two and three co-authors) advocate an intermediate solution in which each executive director would serve fixed six-year terms and would be responsible to its parliament or parliaments.⁷³ Some observers favor other steps to increase the transparency and accountability of the executive board. For example, Woods and Lombardi (2005) favor the prompt publication of executive directors' votes and the positions they take as well as evaluations of their performance against standards set by the countries that elected them.

The IMF executive board at present has 24 members. Some, for example Boorman (2004) think the board is too large; Peretz (2005) calls for a reduction to 15 seats. Woods and

⁷³ Kelkar et al. (2005) and Woods and Lombardi (2005) single out the United States for setting a good example with respect to the accountability of its executive director because she is nominated by the President and confirmed by the US Senate, and she can be called to testify before the Congress. (Some other executive directors testify before parliaments, for example Lynch (2005).) She is also obligated to serve at a reduced salary partly as a consequence of her exposed political position. Moreover, she serves at the pleasure of the president and conventionally is replaced soon after a change in US administration.

Lombardi (2005) favor a more even distribution of countries and seats. They advocate that the three executive directors elected by single countries (China, Russia, and Saudi Arabia) should take more countries into their constituencies. They estimate that the resulting reallocation of countries and constituencies could reduce the size of each one to no more than ten countries. As a subsequent step, if other countries choose to be represented by one of the five appointed executive directors, the number of countries in each constituency could be reduced further to no more than eight.⁷⁴ The result, they speculate, might be that the elected executive directors would become more independent of their national governments.

If IMF constituencies became more equal in size and voting power, that would not solve the issue of the redistribution of voting power. Boyer and Truman (2005) and Truman (2005a) have advocated addressing the issue of chairs (IMF representation) and shares (the distribution of votes) as part of a process focused primarily on the members of the IMF that are also members of the European Union. At present the 25 EU countries appoint or play a major role in the election of 10 of the 24 IMF executive directors, 42 percent of the executive board. Among the ten, they currently supply six executive directors and eight alternate executive directors, 29 percent of the total. In five cases they supply both. In brief, the European Union is over-represented on an executive board that traditionally reaches decisions via consensus; the European voices are too many and as a consequence receive too much weight. EU members also directly control 32 percent of the votes in the IMF.⁷⁵ Indirectly through the inclusion of non-EU countries in their constituencies or the presence of EU countries in non-EU-majority constituencies, the European Union potentially can influence an additional 12.5 percent for a total of almost 45 percent.

Rationalizing the allocation of shares and chairs within the IMF in principle involves two separable issues, one having to do with shares and the other having to do with chairs. In practice, both issues will almost certainly have to be addressed at the same time even if progress toward the ultimate goals of these reforms involves different timetables. Shares will have to be reallocated toward those countries where their relative economic size has outstripped the relative size of their quotas, generally the large emerging market economies or LEMs. Such a shift would tend to support the financial stability of the organization.

The reallocation of chairs is a more complicated process. Boyer and Truman (2005) and Truman (2005) advocate a multi-step process. First, non-EU or nonaspiring EU members would join other constituencies, and EU members such as Ireland, Poland, and Spain would join EU-constituencies. This would probably reduce the number of EU or potential EU executive directors and alternate executive directors from a potential of 10 each to 6 or 7 each. Non-EU executive directors and alternate executive directors in reconstituted constituencies would occupy the freed up seats. As a second step or series of steps the EU chairs would be consolidated into one chair; this would allow for the establishment of new constituencies or for a smaller executive board. The complexity of working out this realignment to the reasonable satisfaction of most IMF members should not be underestimated. No country should end up not being represented, and large countries should resist limiting the size of their constituencies to the minimum number of votes necessary to claim a seat.

⁷⁴ The authors are vague about whether such a change would require an amendment of the IMF Articles of Agreement, but that almost certainly is the case.

⁷⁵ The 10 new members of the European Union that joined in May 2004 only have 2.1 percent of the votes.

Kahler (2001) also advocates a consolidation of EU chairs in the IMF. Kenen et al. (2004) do so as well. However, Kenen et al. would stop the process, as the situation now stands, at two chairs, one for the Euro Area and one for non-Euro Area EU-member countries.

Many observers from a European perspective (Bini-Smaghi 2004, Kiekens 2003, and Woods and Lombardi 2005) see the consolidation of EU representation into a single chair as a positive step in Europe's interests. Horst Köhler (IMF Survey 2004) expressed support for an ever-closer political union within Europe and saw consolidating EU chairs in the IMF as consistent with that vision. Since the Vienna European Council meeting in December 1998, EU members have sought to upgrade the coordination of their positions in international fora, the IMF in particular. From the bottom up, EU executive directors meet in Washington with representatives of the ECB and the European Commission as the EURIMF. Further up the line, a staff group (SCIMF) involving national capitals as well as the ECB and the Commission works up common positions for subsequent review and approval by the Economic and Financial Committee (EFC) of deputies and final review and approval by the Council of EU Finance Ministers (Ecofin).⁷⁶ However, partly because of the presence of non-EU members in some constituencies and the presence of other constituencies where EU members are not dominant, and partly because of the desire for some EU members to go their own ways on some IMF issues, this process of coordination has not produced uniform EU positions on all issues.

As noted earlier in connection with the issue of the distribution of IMF quotas in the IMF, the Europeans properly should take the lead in this area. To date, they are not so inclined, if one can judge by what Junker (2005) said to the IMFC. To break this logjam, the United States has its nuclear option.⁷⁷ However, an important question is whether the United States sees it in its interest to deal with a single European entity. Truman (2005a) argues in the affirmative and that the United States in general should push for closer European integration. However, not all US officials and observers agree. Each camp can interpret the constitutional issues that arose in the late spring of 2005 as favoring their initial positions.

If the Europeans were to consolidate their representation in the IMF, such a step would have strong implications for the IMF as an institution, including other aspects of its governance.⁷⁸ To cite one aspect, if the European Union were to assume a consolidated chair as a single country, which some argue would require an amendment of the IMF Articles of Agreement, and the EU quota were the largest in the IMF, then according to the current Articles, the headquarters of the IMF would have to be moved to Europe. Such a move might cause considerable disruption, but that possibility would be one that would have to be addressed as part of an overall bargain.

⁷⁶ See Bini-Smaghi (2004) and Woods and Lombardi (2005).

⁷⁷ In principle, any group of countries with more than 15 percent of IMF voting power has similar leverage to force a reallocation of chairs within the IMF. However, the direct consequences of failure would be larger because if the size of the executive board were reduced to 20 seats without a consolidation of European seats, the instigators might find themselves without any representation on the Board.

⁷⁸ See Géraldine Mathieu et al. 2003.

The IMF and Steering Committees

A basic question with respect to IMF governance is from where does the institution receive its direction? Today, as a formal matter, the IMF management runs the Fund. The executive board supervises the management and staff. The IMFC is formally an advisory body that in effect provides some overall guidance.⁷⁹ The Board of Governors acts in the areas where the Articles require it to act.

In practice, none of these groups acts as a true steering committee for the IMF. One might well argue that the IMFC should play this role. However, despite efforts in recent years to bolster its role, it has failed as a body that either generates consensus or provides broad innovative direction to the Fund. That role has been played by outside steering committees. Only a trained political scientist can explain this failure, and her colleagues would probably disagree. This observer's explanation is that the IMFC's effectiveness is constrained by two factors: (1) The continuing formality of its meetings complete with speeches that are prepared in advance and released to the public. (2) The substantial control over the IMFC's agenda and discussion that is exercised by IMF management and staff.

Throughout its history, the IMF management and staff itself has not been a source of innovation or direction for the international economic and financial system. The G-10 negotiated the Smithsonian Agreement, and the IMF's involvement in that negotiation lost the managing director his job. The ad hoc Committee of Twenty (C-20) dealt as best it could with the subsequent reform process. The IMF has not been able, or allowed, to play a major role in shaping cooperation on major international macroeconomic policy issues.⁸⁰ The reasons for this weakness are complex. The IMF has been ineffective, in part, because its most powerful members wanted it that way. The IMF also is an institution that is dominated by its staff, which means that it is cautious with respect to innovation. At the same time, the IMF has not been able, despite repeated efforts, to sponsor effective dialogue outside of a narrow interpretation of the scope of its responsibilities.

Over the past 30-plus years, the steering committee of the IMF was first the G-10 with a strong US lead, next the G-5 countries, and more recently the G-7 countries.⁸¹ Of course, the G-7 finance ministers and central bank governors seek to steer the international financial system and the global economy, not just the International Monetary Fund, but in the process they have been the steering committee for the IMF as well.

⁷⁹ French finance minister Thierry Breton (2005) proposed the revival of the proposal to institute the Council as a body representing the Board of Governors with formal decision-making power in the IMF. Such a step would tend further to weaken the IMF executive board and strengthen the role of the IMF management and staff. However, that proposal was reconsidered and set aside in the late 1990s, when the Interim Committee, intended as a precursor of the Council, was transformed into the IMFC.

⁸⁰ The IMF has played a major and sometimes innovative, if controversial, role in connection with some specific issues, for example, the debt crises of the 1980s and the transformation of the economies of Eastern Europe and the former Soviet Union in the 1990s

⁸¹ The G-5 includes France, Germany, Japan, the United Kingdom and the United States. The finance G-7 includes also Canada and Italy. (The G-8 includes Russia but it is principally a political group.) The G-10 includes Belgium, the Netherlands, Switzerland and Sweden as well as the G-7.

Bergsten (2004), Boyer and Truman (2005), and Truman (2005) have called upon the G-20 to replace the G-7 in its role as the steering committee for the international financial system and the IMF.⁸² As noted earlier, Summers (1999) called for the G-20 to play an operational role in the international financial system, but to date its operational role has been strictly circumscribed by tacit agreement within the G-7.

King (2005) stresses the need to expand the group of countries that discusses exchange rate and other macroeconomic policy issues beyond the G-7. He might stop at a G-7 group plus a few other countries, such as China and India or the five countries (Brazil, China, India, Mexico and South Africa) that joined the G-8 at their leaders' summit in Gleneagles, Scotland in July 2005. During 2005, Brazil, China, India, and South Africa participated in two meetings of the finance G-7. However, although they were invited as more than breakfast or luncheon guests, the finance ministers and central bank governors of those countries were not full participants in the meetings in the sense that they were involved in the full agenda of issues, including drafting the final communiqué where the G-7's conclusions, agreements, and directives are enunciated.

The G-20 is a more natural group to play a significant role as a global steering committee in light of the changing and broadening list of countries of systemic importance, a list that extends beyond Brazil, China, India, and South Africa for many issues such as energy, issues of global adjustment, and governance more generally.⁸³ Central bankers actively participate in G-20 meetings along side of finance ministers; this feature contributes to its permanence as well as to its technical expertise on international economic and financial issues, but the consensus would have to be broader. With a group as large as 20, it is natural that there would be sub-caucuses on specific issues. If the G-20 is to have more influence, a permanent secretariat might be desirable along with the use of working groups and more frequent deputies' meetings to follow up on ministerial decisions.

As a steering committee for the IMF, the G-20 countries have about 63 percent of the current voting power in the IMF and almost 80 percent of the voting power when including all the votes in the constituencies of which they are members. If European representation in the G-20 were collapsed into one membership, that should further improve the effectiveness of the group and either contract its size to a G-16 or permit a slight expansion to 18.⁸⁴

Paul Martin (2005) has called for a L-20—a G-20 at the leader's level of prime ministers and presidents—that builds on the finance group that already exists.⁸⁵ The G-20 group of countries is not without challenge as the steering committee for the global financial system. Kenen et al. call for the creation of two new groups: (1) a G-4 involving the United States, Euro Area, Japan and China to coordinate exchange rate matters and (2) a Council for International

⁸² The industrial-country members of the G-20 are the G-7, Australia, and the country holding the EU presidency, when not a European G-7 country; the non-industrial country members are Argentina, Brazil, China, India, Indonesia, Korea, Mexico, Russia, Saudi Arabia, South Africa, and Turkey.

⁸³ Anyone can quibble about the G-20's membership on the margin, but it comes closer to meeting the test of including the systemically important countries than often is the case with political compromises.

⁸⁴ Paretz argues that the IMF needs an agenda setting body of no more than 15 members that regularly meets at both the deputy and finance minister level.

⁸⁵ His advocacy follows proposals by Colin Bradford and Johannes Linn (2004) and work by the Centre for Global Studies (2004).

Financial and Economic Cooperation (CIFEC) with five permanent and 15 term members. They argue that the CIFEC would have greater legitimacy, accountability, and representativeness than the existing finance G-20, but the argument is not very persuasive on the first two points, given that the G-20 already exists, and on the third point any ad hoc group will be perceived by some nonparticipants as being nonrepresentative. They also propose that the CIFEC have a mandate to cover economic issues other than the IMF, which is also the case for the G-7 and G-20.

More of a threat to the IMF as an institution, as well as to the G-20 as the steering committee for the international financial and monetary systems that provides guidance for the IMF, would be the proposal by Kemal Dervis and Ceren Özer (2005) to create a new United Nations Economic and Social Security Council (UNESC) with six permanent and eight nonpermanent members that would exercise the votes of their constituencies. The votes would be an equally weighted combination of population, GDP, and contributions to the UN budget for global public goods. There would be no vetoes, but supermajorities would be required for some issues. The UNESC would (a) provide a strategic governance umbrella for international institutions, including the IMF, (b) appoint the heads of those institutions, including the IMF, using transparent search procedures, and (c) mobilize resources for those institutions.

A similar, but less well-developed, idea is contained in the Report of the Secretary-General's High-Level Panel on Threats, Challenges, and Change (UN 2004). In part, these rival plans reflect turf battles between foreign ministries and finance ministries; each ministry wants the institution in which it calls the shots to be dominant. In part, these plans reflect dissatisfaction with the orientation and governance of the Bretton Woods institutions.⁸⁶ It can also be argued that these proposals are intended to pull the Bretton Woods institutions into one common system for global governance.

The principal inference to be drawn from all this ferment with respect to a steering committee for the international financial system including the IMF is that in the immediate future that steering committee will not be drawn from the institutional structure of the IMF itself. If the choice is between the finance G-7 and G-20, it is difficult to imagine that the rational choice would not be the latter group appropriately reconfigured to include only single representation of the European Union. However, that may not prove to be the choice. Political leaders have a sometimes disruptive and counter-productive tendency to reach out to create new institutions to address a renewed perception of recurrent global problems.

At the same time, political leaders frequently do respond to broader political pressures both those manifested through NGOs at the national or international level and those articulated by academics. This truth underlines the challenge of communication that the Fund faces in today's world of instantaneous global transmission of information, misinformation, and disinformation.

⁸⁶ Messner et al. (2005) propose the creation of a Council for Global Development and Environment (CGDE) in the United Nations partly as a funding vehicle and also "with an enhanced mandate and sufficient legitimacy to counterbalance the independence of the Bretton Woods institutions from the UN System." The Fund and the World Bank are associated with the United Nations by mutual agreement, but they are not formally part of the UN System.

IMF Lending Facilities

The traditional conception of IMF lending activities is that they should strike a balance between adjustment and financing. The borrowing country receives sufficient financing to allow it to take adjustment measures that minimize adverse effects on national or international prosperity. On its part, the country takes sufficient adjustment measures to ensure that it will be able to repay the Fund.⁸⁷

As outlined in the introduction, the IMF currently lends through five types of facilities: Stand-By Arrangements (SBA), an Extended Fund Facility (EFF), a Supplemental Reserve Facility (SRF), a Compensatory Financing Facility (CFF), and a Poverty Reduction and Growth Facility (PRGF).

In recent years there has been a trend toward streamlining the various facilities, revising them to reflect the changing realities of the international financial system—flexible exchange rates and more extensive private capital flows—and reducing their number in effect so that they can operate off of one overall platform with multiple models or variations. For example, in the wake of the tsunami that hit countries in December 2004, the executive board did not create a new facility, it approved an amendment to its “policy” on emergency lending to members in postconflict situations, which was adopted in 1995 and extended in 2001 to provide subsidized lending to such countries that are PRGF-eligible, to include subsidized lending to countries hit with natural disasters. In March 2005, the executive board approved a Trade Integration Mechanism (TIM) as a policy associated with EFF or PRGF borrowing that permits countries to borrow to finance balance-of-payments shortfalls associated with multilateral trade liberalization.

However, not all facilities involve actual lending. For example, the IMF long has had precautionary SBA or EFF lending arrangements under which the country has the right to borrow, but states its intention not to do so. The underlying idea is that this type of program provides confidence to private sector international lenders to the country by providing an IMF “seal of approval” of its policies. In the past, the Fund has also experimented with a variety of signaling devices and intensified monitoring mechanisms short of precautionary lending programs, and consideration is again focused on a new type of nonborrowing program, a policy support instrument, that could be used by PRGF-eligible members; see below.

Going the other way, from intensions not to borrow to promises to lend, in 1999 the IMF instituted a Contingent Credit Line feature into the SRF under which a specified amount of financing automatically become available to countries that had been preapproved. Despite tinkering with the feature, no one signed up for approval, and the CCL was not renewed in November 2003. However, as described below, variations upon this general theme are under

⁸⁷ This second half of the bargain is known as IMF “conditionality.” It is frequently pointed out by critics of the IMF’s operations today, for example Bird (2003) and Babb and Buira (2005), that the concept of conditionality is not to be found in the original IMF Articles but was gradually insinuated into IMF policies, largely under the influence of the United States, which wanted to limit the size of IMF programs financed largely from the IMF quota, and was not codified until the 1969 amendment to the Articles of Agreement and was not supported by guidelines about how conditionality was to be applied until the late 1970s.

active discussion in the form of financial insurance for countries that have met preestablished conditions.

One fundamental issue is which countries are likely to borrow from the IMF in the future. The data underlying tables 3, 4 and 5 reveal that 136 of the current 184-country membership of the IMF have borrowed from the IMF over the past 30-plus years; see table 6.⁸⁸ Three additional countries have had one or more programs under which they did not borrow, for a total of 139 members, or 76 percent of the total membership. The countries include 38 percent of the industrial countries and 81 percent of all other IMF members, including 91 percent for the 77 PRGF-eligible countries, remembering that we have not classified India in the last category.

It is reasonable to assume that none of the industrial countries in the classification used in this paper will need to borrow again from the IMF, and the same may hold for a handful of other countries that we can assume have continuous access to international capital markets or are so wealthy that they do not need it. Note that these countries, by assumption, face no international pressures to adjust, with the United States a leading example. However, about 80 percent of the IMF's membership, about 150 countries, are potential borrowers either because their access to international capital markets is subject to interruption or because they have little or no such access.

As noted in the introduction, a number of potential borrowers from the IMF have taken steps to self-insure against the possible need to borrow external financial resources from the IMF by improving their macroeconomic policy frameworks, strengthening their financial systems, and building up their international reserves. However, the global economic environment has been remarkably benign over the past few years with near-record global growth, low inflation, strong commodity prices, and a sustained period of abnormally low nominal and real interest rates in the United States, Euro Area and Japan. These conditions will not persist. As Goldstein (2005b) details, the evidence is ample that a significant number of emerging market countries could experience financial crises over the next five years because, in part, their self-insuring has been incomplete. For example, for many countries, sovereign and external debt levels are unsustainable and the benign global economic conditions could become less benign in a hurry.

The question is not only which countries *will want* to borrow from the IMF in the context of the next global economic downturn or period of adjustment of macroeconomic imbalances but also which countries *should* be eligible to borrow from the IMF. For some observers and critics the answer to the second question is linked to the quality of IMF surveillance; effective surveillance in a crisis-prevention mode should lead to a reduced need to borrow. At the extreme, a smaller number of observers and critics would limit borrowing from the IMF to those countries that had previously received good report cards from the Fund. The report cards might contain a short list of subjects or a very long list of subjects.

⁸⁸ Most of the countries listed in table 6 had formal IMF programs; a few may have borrowed their first credit tranches, which do not require formal programs. Many of the borrowing countries have been "prolonged users" of IMF resources through successive borrowing programs. Sometimes such prolonged use may be appropriate, but it also raises questions about IMF program design, policies, and incentives. The IMF has acted in recent years to adopt new policies to take a closer look at and exert constraints on the phenomenon of prolonged use of IMF resources.

The view that the scope of borrowing from the Fund should be and can be sharply reduced flies in the face of two realities. The IMF is an organization with a near-universal global membership; those members are not going to leave other injured members, whether their injuries are self-inflicted or not, by the side of the road for the vultures to feed upon as carrion. Reinforcing this first reality is the fact, persuasively argued by Daniel Tarullo (2005), that the IMF is a political institution established by governments that must respond to political forces, including forces of financial need. This reality, in his view, is fully consistent with the professionalism of the staff and the dedication of the management and shareholders to the global public good.

Therefore, we can reasonably expect a pick-up in borrowing from the IMF over the next five years. What will be the content of the adjustment programs—the associated conditionality? At an abstract level, the policy conditions associated with borrowing from the IMF should be tailored to the nature and the origins of the shocks, disturbances, or policy miscalculations that give rise to the need to borrow from the Fund. For the 13 countries experiencing financial crises, from Mexico in 1994 to Brazil in 2002, the range of economic and financial conditions prior to the crises is large; Nouriel Roubini and Brad Setser (2004, 28-29).⁸⁹ Considering just two country-specific dimensions—sovereign debt and external positions—Mexico (1994) and Thailand (1996) had large current account deficits and small stocks of sovereign debt—external plus internal. Russia (1997) had a large stock of sovereign debt and a current account surplus. Ecuador (1998) had a large current account deficit and a large stock of sovereign debt. These are just two dimensions to which could be added currency mismatches, the exchange rate regime, the condition of the financial system, and many more. Global economic and financial conditions provide an additional overlay.

Critics from developing countries, for example Buira (2003), observe that the principal IMF response to the myriad of circumstances that may contribute to a country's need to seek IMF financial support has been a complex elaboration of conditions on borrowing with a bias toward prompt external adjustment combined with limited financing built on optimistic assumptions about the restoration of access to financing from global financial markets.

In partial response to the first criticism about an excess of policy conditions, the IMF in 2002 adopted revised conditionality guidelines that emphasize country ownership of policies, parsimony in conditions, policies tailored to circumstances, appropriate coordination with other multilateral institutions, and clarity in the conditions themselves (IMF 2005h). Notwithstanding well-intentioned efforts to limit the scope of conditionality, each country's program in the end is different because its economic and financial circumstances differ, and the setting of policy conditions requires judgments, which means relying on discretion rather than rigid rules.

On the other side, critics argue that current practice results in “insufficient ambition” in IMF prescriptions for economic policy changes and reforms; IMF staff and management rely too heavily on the preferences and judgments of the national authorities (Geithner 2004, 4). Almost all observers agree that the fundamental challenge lies in determining what changes in policies will be effective in addressing a country's specific needs. Too little research has addressed this

⁸⁹ The full list of countries includes Mexico, Thailand, Indonesia, Korea, Malaysia, Russia, Brazil, Ecuador, Pakistan, Ukraine, Turkey, Argentina, and Uruguay.

complex and vexing issue. However, it is clear that simple rules, for example “it is mostly fiscal,” do not do the trick. Moreover, it has yet to be established, but nevertheless is highly improbable in my view, that simple tests of degrees of ownership or political commitment to programs or of the strength of institutions can explain much of the variance in policy performance under IMF programs.

The second criticism—the limited scale of financing based on false assumptions about the restoration of market access—challenges the hypothesis of the catalytic role of Fund programs: a strong economic program, with its policy content endorsed by the IMF, even if the actual size of the Fund’s financial support is small, will be associated with a prompt recovery of market access. Careful theoretical and empirical examinations of this hypothesis (Carlo Cottarelli and Curzio Giannini 2002 and Ashoka Mody and Diego Saravia 2003) support the conclusion that the catalytic effects of IMF programs are limited. One important reason is that each country’s case tends to be different if not unique.

If the IMF cannot rely upon the catalytic effects of its modest financial support for a country’s program of economic adjustment, then what should be the scale of IMF lending to countries? Answers to this question are usually couched in terms of a country’s IMF quota, but such responses are complicated by inconsistencies in the size of countries’ IMF quotas relative to their economic and financial development, as noted in the section on IMF governance. In the face of capital account crises, associated by definition with a cessation or reversal of access by borrowers in the country in the public and/or private sector to international capital markets, answers are further complicated.⁹⁰

If a country faces an illiquidity crisis, which is often difficult to distinguish *ex ante* from an insolvency crisis, it is likely that its IMF program will have to be over-financed *ex ante* if the country is to emerge from its crisis with a minimum of adverse economic and financial effects on the country and the international financial system. Some would qualify this last statement and argue that the country can always declare a standstill on its external financial payments via capital controls and exchange restrictions. In recent years, no country has resorted to such extreme measures on a comprehensive basis in the context of a liquidity crisis.⁹¹ Comprehensive controls were used in the Argentine case when it turned into a solvency crisis, but based on that case it is questionable whether the standstill option would meet the test of minimizing economic and financial effects on a country in a liquidity crisis.

The IMF has long had a policy of limiting a member’s access to borrowing from the Fund to 100 percent of quota for one year and 300 percent of quota in total, but the Fund could approve exceptions. In recent years, with the advent of capital account crises, exceptional access has been approved in a small number of cases.⁹² Those cases have been controversial within the

⁹⁰ The cessation or reversal of capital inflows (a sudden stop as described by Guillermo Calvo 1998) can be associated with latent or actual developments in internal policies, the external economic and financial environment, or both.

⁹¹ The Korean case and the Brazilian case are examples of limited exercises in this direction. Roubini and Setser (2004) advocate greater use of such tools.

⁹² One response to the capital account crises of the 1990s was to create the SRF under which countries can borrow larger amounts for shorter maturities at higher interest rates. These surcharges were later generalized in two forms: (a) the level of borrowing and (b) the time-period covered by the borrowing. Surcharges now apply to EFF and CFF

Fund, among its members, and in the views of outside observers. In response, the IMF in 2002 and 2003 adopted and revised an exceptional access framework (EAF) that established certain analytical and procedural presumptions that should be applied to these cases.⁹³ Some question the IMF's conscientiousness in applying this policy (Goldstein 2005a and Roubini and Setser 2004).

It is important not to exaggerate the relevance of exceptional access to IMF lending overall. Since 1994 only nine members of the IMF have been granted such access, albeit a number of them on several occasions. As of July 28, 2005, only three of the 14 current SBAs and EFFs involve exceptional access, those for Argentina, Turkey and Uruguay. Only two other countries that previously had exceptional access to IMF resources had IMF credit outstanding on May 31, 2005—Brazil and Indonesia. Fourteen other emerging market and other developing countries had credit outstanding to the IMF as of that date. Korea, Mexico, Russia, and Thailand had repaid the IMF.

On the other hand, when the executive board approves exceptional access, the resulting program potentially ties up a substantial amount of the IMF's lending capacity because of the size of the programs. Some would argue that this situation argues for an expansion of IMF financial resources; others counter that doing so would increase inappropriately the number of programs with exceptional access. This subject is considered in more detail in the next section of this paper.

This introductory discussion of IMF facilities suggests the following basic questions. What should be the role of the IMF as an international lender? Should the IMF develop special programs to assist developing countries that are not experiencing financial crises but have large sovereign debts? Should special lending programs be developed for countries that are "good performers" as part of the array of IMF facilities or as the IMF's only facility? To what extent should the IMF offer or promote nonborrowing programs of policy support without financing? Should the IMF continue to offer special borrowing arrangements for low-income countries? The balance of this section elaborates on some of these questions and provides some answers to them. It covers (1) the IMF's role as an international lender, (2) in particular, its role with respect to members with large sovereign debts, (3) its lending to good performers, (4) programs of IMF support without the use of IMF financial resources, and (5) IMF programs with its low-income members.

borrowing as well as SRF borrowing. Their interaction is complicated, and they have given rise to concerns about, and presumptive evidence of, arbitrage across facilities (IMF 2005b).

⁹³ The analytical presumptions are (a) exceptional balance of payments pressures normally associated with a capital account crisis, (b) a rigorous analysis demonstrating debt sustainability, (c) a strong presumption of an early return to the capital markets, and (d) a strong program of policy adjustment accompanied by the political and institutional capacity to implement the program. The procedural presumptions are (a) an elevated burden of proof on IMF management and staff in presenting the recommended program, (b) early consultation with the executive board as the program is developed, and (c) required ex post evaluation of the program within a year after its end. (IMF 2003.) These elements have subsequently been tweaked somewhat in their application, but the basic framework remains as described. The framework is to be applied to IMF programs that involve exceeding the normal access limits of 100 percent of quota per year and total outstanding credit from the Fund of more than 300 percent of quota.

The IMF as an International Lender

This paper is not the place to review the voluminous literature on the role of the IMF as an international lender to countries and whether it should be a lender of first, last, final or highly limited resort. A sample of three recent contributions with differing views is Roubini and Setser (2004), Paul Bedford et al. (2005), and ECB (2005).⁹⁴ The debate appears to be far from over. It revolves around three issues: limits on access to IMF financial resources, private sector involvement in the financing, and the IMF's role in debt restructurings. A background issue is the changing nature of the international financial markets, making international credit more available to some countries, but not necessarily on a continuous basis.

With regard to access limits, one central issue involves distinguishing cases of illiquidity from cases of insolvency (in the special case of countries, which cannot be subjected to bankruptcy proceedings or the functional equivalent) and whether the IMF has a role to play in preventing the former type of cases turning into the latter. Although improved debt sustainability analyses and a greater understanding of the insidious effects of currency mismatches have aided in distinguishing liquidity cases from solvency cases, there is no consensus about the scale of IMF lending in such circumstances. Some favor strict absolute limits on IMF lending regardless of the circumstances, others favor constrained discretion close to if not identical with the current EAF, and still others see little merit in any limits.

To the extent that one favors large-scale (exceptional access) lending by the IMF in reasonably well-defined circumstances, the analytical issues that the advocate must address are whether doing so involves an unacceptable increase in moral hazard with respect to the debtor or the creditors and whether more IMF lending improves a country's longer-term prospects by addressing the immediate problem or worsens them by piling up more debt (Rajan 2005b).

On the moral hazard issue, most observers agree that debtor moral hazard, while a theoretical possibility, is not a serious problem in light of the short-term political consequences of most crises.⁹⁵ On creditor moral hazard, again few disagree with the theoretical possibility, and many agree that it could be a serious issue. Olivier Jeanne and Jeronimo Zettelmeyer (2004) construct a model that demonstrates that IMF lending creates no moral hazard as long as the Fund lends at actuarially fair interest rates and the borrowing country seeks to maximize the welfare of its taxpayers. Supporters of the moral hazard view of IMF lending must challenge these assumptions. However, within the context of the Jeanne-Zettelmeyer model, IMF lending may lead to large capital flows and better terms. Disagreement remains with respect to interpreting the empirical evidence associated with IMF lending over the past decade.⁹⁶ Even if one accepts that there is concrete evidence of a moral-hazard effect of IMF lending, has that moral hazard created a serious distortion to international lending in the direction of favoring such

⁹⁴ IMF staff have been active contributors to this literature. See for example, Giancarlo Corsetti, Bernardo Guimaraes, and Nouriel Roubini (2003), Olivier Jeanne and Charles Wyplosz (2001), Olivier Jeanne and Jeronimo Zettelmeyer (2002), and Steven Morris and Hyun Song Shin (2003),

⁹⁵ A more reasonable concern is the risk of supporting programs that are too timid in their policy content or may not be adequately implemented contributing to further crises.

⁹⁶ Jeanne and Zettelmeyer (2004, 15) survey the empirical literature and conclude, "Without exception, the tests performed in this literature are incapable of distinguishing whether the effects of the IMF on market variables (to the extent that any are found) are a sign of moral hazard or simply an indication that the IMF is doing its job."

lending to developing countries in the context of many other distortions? That is the crux of the issue.

At the abstract level of ex ante IMF policy, few would disagree with the characterization offered by Managing Director de Rato (2004, 4) early in his term and since then often repeated, “we clearly also need a Fund that can say ‘No’ selectively, perhaps more assertively, and, above all, more predictably than has been the case in the past.” What is notable about this statement is not its clarity but the qualifications: selectively, more assertively, and more predictably. De Rato’s view does not differ substantially from that of his predecessor Horst Köhler (Camdessus et al. 2004), “The IMF is not a lender of last resort in the traditional sense; it isn’t capable of providing an unlimited amount of financing. Once a crisis hits, the IMF needs to be able to act quickly, and its involvement must be predictable to ensure that the private sector can play its part.”⁹⁷

How should the IMF strike the balance? Goldstein (2005a, 399-400) would move the pendulum further toward making it more difficult for the IMF to say “Yes.” He would amend the Articles of Agreement to require supermajorities to approve exceptional access. He would also amend the Articles to require the managing director to sign off “explicitly” that any decision to grant exceptional access meets the requirements of the IMF’s policy; at present there is only a strong presumption that any decision submitted to the executive board by IMF management is consistent with the IMF’s conditionality guidelines and other policies, including access policy. Surprisingly, not only Rajan (2005b) but also Babb and Buira (2005) favor tighter rules and less discretion. Rajan believes that discretion favors the borrower, and Babb and Buira believe that the borrower tends to be disfavored.

The relation between IMF lending and private sector in crises has been controversial at least since the 1980s. Contrary to the conventional wisdom, this is an area of evolution not revolution. Thus, Jacques de Larosière (Camdessus et al. 2004) opines:

The IMF cannot, and should not, provide *all* the financing for balance of payments problems; it has to count on private flows to do the bulk of the financing (heavy lending by the IMF to a few countries has become a serious issue for the institution and the system). Moreover, the IMF must develop a close relationship with the private sector and not turn a blind eye to it. . . . This was the rule in the 1980s. It still should be.

Roubini and Setser (2004) propose a comprehensive framework to address the role of the IMF in financial crises, the scale of its lending, and the participation of private sector creditors: (1) distinguish promptly between liquidity and solvency situations, (2) adopt appropriate adjustment measures to match external financing with the nature of the crisis, (3) use large-scale IMF financing in a variety of circumstances, including in conjunction with coercive debt restructurings as necessary, (4) avoid the trap of countries (for example, Russia and Turkey) that are too strategic to fail, and (5) recognize that the IMF has a central coordinating role in the management of crises. Roubini and Setser recommend that the IMF create a crisis lending facility with lending limits of 300 percent of quota for one year and total lending of 500 percent

⁹⁷ Recall that Summers (1999) also argued that the IMF has to be selective in providing its financial support.

of quota, which they regard as more realistic than the traditional limits of 100/300 percent of quotas. However, they would allow these limits to be overridden using prespecified criteria.

The ECB (2005) task force favors the “effective” use and “predictable” commitment of all parties in debt crises (sovereign debtor, creditors, IMF, and creditor governments) to use available instruments (bond exchanges, rollover agreements, standstills, and, with less effect, capital controls and private contingent credit lines) with domestic creditors also bearing a part of the burden. They conclude from their review that crisis management practices have largely followed a case-by-case approach. In somewhat of a contradiction, they nevertheless favor efforts to improve the predictability of the process, including by reinforcing good relations between a debtor country and its creditors according to the Principles for Stable Capital Flows and Fair Debt Restructuring in Emerging Markets (also known as the Code of Conduct) that first was agreed to in the fall of 2004 between a group of emerging market countries and a group of representatives of private sector creditors; a slightly revised version was issued in March 2005.⁹⁸

The central banks of Canada and England with support from a number of other commentators and institutions in the past have favored absolute limits on access to IMF financing in conjunction with standstills on debt repayments as the appropriate mechanism to deal with external financial crises and the issues of moral hazard and predictability.⁹⁹ Paul Bedford et al. (2005), commenting more recently in a Bank of England publication, place greater emphasis on market-based mechanisms for facilitating sovereign debt restructurings with further improvements in bond contracts beyond the widespread adoption of collective action clauses (CAC) and wider adoption of the Code of Conduct. They also favor more rigorous and informed application of the IMF’s framework for exceptional access to IMF financial resources and a review of the IMF’s policy on lending into arrears (LIA), when a member country has arrears to external private sector creditors. With respect to LIA, they want the IMF to publish its debt sustainability analysis but not to specify the financial parameters of its program until the debtor has reached agreement on them with its private sector creditors. If the IMF were to adopt to this last proposal, it would amount to a partial reversion to its policy in the early 1980s when programs were not approved by the IMF until a critical mass of creditors had agreed to the financing presumptions in the program, which at that time were initially agreed between the country and the IMF.¹⁰⁰

⁹⁸ The IMF (2005f, 14) asserts that the draft principles in the Code of Conduct “are broadly consistent with many of the expectations from Fund policies aimed at the prevention and resolution of financial crises.” Among the identified exceptions are: (a) linking continuation of trade and inter-bank lines to continued debt service by the sovereign debtor, (b) requiring the debtor to engage with a creditor committee, (c) the absence of consideration of voluntary standstills on litigation, (d) the resumption of partial debt service as a sign of good faith on the part of the borrower, and (e) the presumption that if a country’s sovereign debt to the private sector is sought to be restructured the debtor must at the same time seek to restructure debt with all bilateral official creditors (reversing Paris Club comparability). The same document (IMF 2005f, 16) welcomes the Code of Conduct, but dryly observes that “many market participants were not aware” of the Code or Principles and others argued that it was yet to be tested and lacked precision on a number of points.

⁹⁹ While the two central banks have not formally adopted policy positions on these issues, their leaders have tacitly endorsed the approach espoused by Mark Kruger and Andrew Haldane (2001) two senior members of their respective staffs.

¹⁰⁰ That practice was changed in 1989 to one of IMF lending into arrears (LIA) to banks because over time the previous policy of requiring a “critical mass” of private sector support gave the creditor banks too much leverage in the context where the debtors generally were meeting their obligations. The IMF’s LIA policy was extended in 1998 to bondholders.

A more radical change advocated by some (mostly IMF bashers on the right) in the context of the Argentine case would be to eliminate the IMF's de facto preferred creditor status—the presumption that the IMF will be paid in full even as other creditors are not. This would not only fly in the face of the logic of the IMF as a lender of final resort but also would effectively kill political support for the IMF in many industrial countries as some advocates of such a position would like.

It should also be noted that many of the proposed approaches to countries' external financial crises presume that those crises principally involve sovereign debt issued under international law, for example the IMF's proposed Sovereign Debt Restructuring Mechanism (SDRM). This has been the exception rather than the rule. Of the 13 major country cases through 2002, only Argentina principally involved sovereign debt, and possible the contagion case of Uruguay. Moreover, by the time 76 percent of the designated portion of Argentina's sovereign debt was restructured in mid-2005, domestic law governed more than half of its sovereign debt de facto or de jure. I wrote (2001) immediately after the SDRM proposal was initially floated that the proposal was too much (for the international financial system to accept at the time) and too little (it might be useful in a few cases, but only on the margin). My forecast was unusually accurate. The SDRM was cut back and put on the shelf. It did vastly accelerate the adoption and acceptance of CACs.

The Argentine case, of course, ultimately involved a sovereign default, widespread defaults on private sector obligations to foreign and domestic creditors (including banks), a collapse of the domestic banking system, and restrictions on capital flows, domestic access to foreign exchange, and access to bank deposits. Thus, in reconsidering the appropriate role of the IMF as an international lender in this context, one should also reconsider the IMF role in crisis prevention with respect to balance sheet mismatches, the appropriateness of capital controls at least in crisis prevention, and other approaches to modulate booms and busts in international lending.

Finally, the IMF's role as an international lender is linked to its role in restructuring situations. If the IMF determines before or after a crisis breaks that a country faces a solvency crisis, the Roubini-Setser approach would call for a debt restructuring, perhaps a coercive restructuring accompanied by IMF lending to ease the burden on the country.¹⁰¹ We have already seen that Bedford et al. (2005) want the IMF to stay out of the way and let "market mechanisms" operate.

In my view, the flaw in arguments that the IMF should not interfere with the market is that in crisis or near-crisis situations market mechanisms will likely break down, and the system does not have a natural replacement to play a coordinating role. Collective action clauses in sovereign bond contracts governed by international law are not a substitute where a large proportion of the debt does not take that form. Even where international bonds dominate, clauses promoting inter-creditor coordination can be expected to have a limited impact because they do little to alter the leverage between the debtor and the creditors as a group. Once the debtor has

¹⁰¹ Roubini and Setser do not exclude standstills, rollovers, or restructurings in the case of liquidity crises as well with the IMF playing a coordinating role.

defaulted, the creditors have essentially no leverage to force action. In the Argentine case, where the stakes were high, legal efforts have so far failed (Anna Gelpern 2005).

It follows that it is reasonable for the IMF, as a collective institution, is to address this market failure by playing a coordinating role. This is the view of Roubini and Setser (2004), and I fully agree with them. The resulting restructuring inevitably will have a political dimension, which is not surprising since one of the parties is a government and because of the necessarily political foundations of the IMF (Tarullo 2005). Moreover, one cannot duck the fact that the IMF has a financial interest in the outcome even if it has de facto status as a preferred creditor.¹⁰² The issue is whether the alternative to the former traditional procedures would produce superior outcomes. I have my doubts.

In the case of Argentina after 2001, the IMF with the general support and often the vigorous encouragement of the G-7 countries abandoned its practice of more than 25 years of acting as a coordinator and umpire in debt settlements. That practice evolved during the debt crises of the 1980s, when Jacques de Larosière led the IMF, through the capital account crises of the 1990s, when Michel Camdessus was its leader.¹⁰³ In contrast, Argentina's 2003 IMF program did not establish any parameters for the country's offer to its bondholders—an omission that Argentina exploited. Only belatedly did IMF management and the G-7 articulate a verbal formula describing a successful restructuring. It was defined as a restructuring that was "sustainable" and "comprehensive." Since the restructuring left Argentina with a public sector debt ratio of more than 75 percent of GDP, one can doubt whether the result is sustainable. Since 24 percent of the relevant debt was not treated, it is certainly not comprehensive. By its own criteria, the IMF's noninvolvement produced a failure. Argentina may have failed as well. The perception is that greater IMF involvement would have provided a better deal for bondholders. In fact, IMF involvement might have produced an endorsement of deeper debt reduction.

Could the IMF have played a more forceful role? Of course it could have done so even though the Argentine government expressed no interest in the IMF playing such a role. The IMF was bluffed into supporting Argentina's economic program and effectively a partial rollover of Argentine obligations to the IMF. The Fund and its larger members had a choice. They failed to insist upon either of the two related conditions that Geithner (2004) recommends in such situations: a credible medium-term adjustment program and a credible and monitorable framework for achieving a viable debt restructuring.

Notwithstanding these criticisms, many have applauded the IMF's nonrole in the Argentine debt restructuring. The US government was a leading supporter of that posture. To date, US government officials have expressed no regrets, though Quarles (2005) both praised the progress to date and argued that more work needs to be done with respect to the residual defaulted debt. Meltzer (2005a) praised the IMF for its noninvolvement and argued that its

¹⁰² As noted earlier, many critics of the IMF call for the abandonment of its preferred creditor status. Roubini and Setser (2004, 253-54) successfully demolish their arguments.

¹⁰³ IMF policy was not perfectly suited to every case, but it evolved. Some argue that the slow evolution of the 1980s and the delayed establishment of the policy of lending into arrears prolonged the debt crises of that period, which were global and not limited to Latin America. My view from the trenches was that the responsible officials of few countries wanted debt reduction much before it was on offer in the Brady Plan.

policy was “a big step forward.” Reuters reported on July 29, 2005 that de Rato insists that the Fund should have no role in the negotiations between the Argentine government and its creditors. Only time will tell how he is going to square his statement with the view that Argentina must have a strategy to deal with the remainder of its defaulted debt as part of any new IMF program. The IMF played a much more active role in the rescheduling of the external debts of the Dominican Republic in 2004; perhaps, it has begun to learn its lessons.

Only time will tell about many aspects of the Argentine case. To date the largest sovereign debt default in history has passed without definitively answering any legal and policy questions surrounding it (Gelpern 2005). Argentina has faced rather limited legal consequences from its default and its bond exchange. Gelpern sees the associated documentation as progressive not revolutionary. The next act in this debt drama again involves Argentina and the IMF despite the IMF’s posture to date of noninvolvement. Will the IMF management and a majority of its members once again blink and approve a program with Argentina without a plan to achieve comprehensive and sustainable settlement of its defaulted debt? If the answer is yes, this will only reinforce the principal conclusion so far from this sorry experience: once a country has defaulted, the country—not its creditors—has most of the leverage. As a result of the IMF’s noninvolvement posture, it effectively allowed itself to be manipulated by the defaulting country into a posture perceived as against the country’s creditors without articulating its position. Time will tell whether this result, if it stands, enhances the stature of the IMF as part of the international financial architecture.

Support for Members with Large Debts

Countries that successfully emerge from financial crises and IMF programs with large stocks of sovereign debt (internal and/or external) and countries with large stocks of sovereign debt, for example, above 30 percent of GDP, that have not experienced financial crisis are particularly vulnerable to internal and external shocks that precipitate a crisis or another crisis. What should the IMF role be with respect to such countries?

One alternative is to monitor the countries and their performance via Article IV consultations, coaxing and cajoling them to adopt policies that place debt ratios on a convincing downtrend. Those countries that have emerged from a crisis might face a higher than normal bar in obtaining additional IMF financial support at least until they have paid down a substantial fraction of their earlier IMF loans. Those countries that have yet to face crises would be dealt with the same way as the first group of countries except that the bar to IMF lending might be lower.

At the other extreme, following Roubini and Setser (2004), the IMF could actively encourage and financially support debt restructurings that promise significant reductions in debt stock. Such preemptive restructuring would be difficult to sell to the market, but the long-run benefits to the countries might well offset the short-term costs. In effect, this was the approach attempted under the Brady plan restructurings of commercial bank debt in the early 1990s.¹⁰⁴

¹⁰⁴ The Brady restructurings resulted in limited if any reductions in debt stocks as valued by the market at the time, but the gap between face value and market value was recognized, and repayments were reprogrammed.

An intermediate alternative has been suggested by Dervis and Özer (2005): establishment in the IMF, in cooperation with the World Bank, of a Stability and Growth Facility (SGF) to help emerging market economies with strong economic policies and large sovereign debt ratios to achieve sustainable growth while at the same time working down their debt ratios and protecting them from financial crises unrelated to their current economic policies. In effect, the IMF would provide potential compensatory financing against external debt shocks, creating demand for a bigger IMF.

Dervis and Özer suggest that countries such as Brazil, Ecuador, Indonesia, the Philippines, Turkey, and Uruguay might now qualify as long as their policies were judged *ex ante* to be strong enough. The proposal involves elements of both prequalification in terms of economic policies and insurance against unforeseen shocks. In principle, it would allow countries that experience, for example, a sharp drop in exports because of a global economic slowdown to run counter-cyclical fiscal policies or at least not pro-cyclical fiscal policies in the context of a decline in domestic economic activity.

Many questions would have to be answered before such a facility was established. One important question would be the likely need for additional IMF financial resources and how those resources might be assembled, which is the topic of the next section.

IMF Lending Programs for Good Performers

The SGF proposal outlined above is one variant on a number of proposals that would involve repositioning IMF lending programs for countries that are “good performers.” It does not require much imagination to sketch out other variants on this theme.

The first set of questions in connection with such proposals involves the definition of “good performance.” What objective indicators would be used to establish good performance? Candidates might include fiscal positions, average marginal and effective tax rates, debt positions of the government and country, exchange rate regimes or performance, international reserves, inflation rates, condition of financial sectors, to name a few possibilities. Identifying good performers could be linked to IMF Article IV consultations or other IMF surveillance activities. Countries could automatically qualify, or could apply for certification. Recertifying and decertifying countries presumably would involve the same procedures, but how those procedures would operate and with what frequency is another important question involving political issues as well as internal IMF bureaucratic issues.

A second set of questions would involve the conditions or context in which access to the facility could be activated. Would they be prespecified and objective as well? This would imply that access would be essentially automatic. Alternatively, the executive board might be expected to review evidence assembled by the IMF staff and endorsed by the management before funds were released.

A third set of questions is whether IMF lending should be limited to countries that had qualified by meeting a (large or small) set of conditions. The IFIAC (2000) majority endorsed the IMF playing a quasi-lender of last resort essentially exclusively to emerging market

economies that had met a short list of four preconditions (Williamson 2001): (a) freedom of entry and operation for foreign financial institutions, (b) well-capitalized commercial banks, (c) regular, timely and comprehensive publication of the maturity structure of sovereign and guaranteed debt, and (d) an unspecified indicator of fiscal probity.¹⁰⁵ Nothing was included with respect to the size of sovereign debt stocks, current account deficits, exchange rate regimes, inflation rates, or a number of other variables many would consider relevant to economic and financial stability. Bergsten (2005), who was a dissenting member of the Meltzer Commission with respect to this point, points out critically that the suggested criteria would have permitted continued IMF lending to Argentina in the summer of 2001 but would not have permitted the Fund to lend to Brazil in 2002. Goldstein (2003, 238-44) also presents a detailed critical analysis of the IFIAC proposal.

The CCL provided a country in principle with an opportunity to seek preapproved financial support and a limited amount of automatic access. However, even this modest step in the direction of an insurance facility was tightly circumscribed. Many influential members of the IMF, in particular many European members, opposed the concept because they wanted slower disbursements and stronger policy conditions. No IMF members chose to apply for a CCL. The result was that the CCL was not renewed in 2003.

However, the idea of some type of IMF insurance facility is not dead. Most of the new ideas differ from the CCL in that the CCL used an application mechanism and under most of the insurance type of schemes countries would be prequalified without formally applying. Daniel Cohen and Richard Portes (2004) have made such a proposal. Tito Cordella and Eduardo Levy Yeyati (2005) have as well. Eichengreen (2004a) expresses support for an Enhanced Monitoring Facility that appears to be a cross between the CCL and a full-blown insurance facility. Rajan (2005a) can be interpreted as endorsing consideration of such a facility as part of an IMF move toward greater reliance on rules than discretion.

Ralph Chami, Sunil Sharma, and Ilhyock Shim (2004) analyze the theoretical case for an IMF coinsurance arrangement and find it lacking in the face of information asymmetries and time-consistency weaknesses. On the other hand, such flaws affect most other elements of macroeconomic policymaking and policy is made.

At the more practical level, Geithner (2004) laid out five key elements of a credible IMF insurance mechanism: (1) a policy framework that can be counted upon to restore confidence, (2) a scale of financing calibrated to need (potentially substantial), (3) flexibility to respond to external circumstances and the borrower's policy effort (implying scope for the frontloading of large amounts of financing), (4) use in the context of restructuring efforts, and (5) a more credible capacity for the IMF to withstand arrears in repayments. The Geithner elements clearly involve aspects of the IMF's operations that extend beyond relatively narrow issues of prequalification.

What are the prospects for a new effort in this area reaching fruition? UK finance minister Brown (2005) expressed some sympathy for the idea. His French counterpart Breton

¹⁰⁵ In extremis, a threat to the stability of the global financial system, the IFIAC said the IMF should be able to lend to other countries that had not prequalified.

(2005) supported it. The G-24 (2005) expressed cautious support for exploring the idea of a precautionary facility as long as it was adequately financed to deal with capital account crises. This is an idea whose time may not have come, but it is not dead either.

Support Without Lending

The IMF has long wrestled with the issue of how to support countries with strong or strengthening economic policies that do not need financial support or cannot afford financial support because of the financial cost of borrowing even from the IMF.¹⁰⁶ In effect, the IMF by approving such an arrangement would be providing a signal to the market or to other investors and donors. The IMF now has, and in the past has experimented with, similar instruments taking the form of (a) precautionary arrangements that permit a country to borrow but such borrowing is not expected,¹⁰⁷ (b) staff monitored programs that involve no IMF resources and often have been used as precursors to regular programs, and (c) enhanced surveillance or monitoring by the staff or executive board sometimes in connection with programs that have recently ended.

One issue with respect to such mechanisms is how they should be linked with normal surveillance mechanisms, for example, Article IV consultations. Wouldn't the IMF just become another rating agency (Boorman 2004), and what would be its value added? Another issue is whether the signal to the market or to other investors and donors tends to absolve those receiving the signal from doing their own due diligence—another type of moral hazard. A third issue involves the black-or-white character of off-on signals, when the true situation almost always involves shades of gray. A related very important issue is the implication of turning off a signal once it has been turned on. This, in turn, relates to the standards that are to be applied: Are the standards higher or lower than for a regular stand-by arrangement or a precautionary stand-by arrangement or for a low-access arrangement even though the standards in the latter cases in principle are the same as in the former? Are standards in signaling mechanisms the same as those associated with upper-credit-tranche SBA and EFF arrangements or are they lower?

A final set of issues involves whether the signaling mechanism would be voluntary and whether it would be limited to one category of countries, for example, low-income countries or emerging market countries, or be available for all categories of countries. If the use of the mechanism were voluntary, would there be any volunteers? How should their volunteering be interpreted?¹⁰⁸

¹⁰⁶ See IMF 2004e reporting on the executive board's discussion of this topic in September 2004 and related documents.

¹⁰⁷ As of July 28, 2005 three of the 14 operational SBA or EFF were precautionary; those for Colombia, Croatia, and Paraguay. Often the proportion has been larger.

¹⁰⁸ The answer to the first question appears to be yes. The Nigerian government has indicated its interest in utilizing such a mechanism as the basis for obtaining a write down and rescheduling of its bilateral official debt. The Paris Club has indicated its willingness to accept such a policy support instrument as the basis for such an agreement with Nigeria. The Paris Club press release of June 28, 2005 states that Nigeria would be receiving *exceptional treatment* in the interest of resolving Nigeria's long-standing arrears to Paris Club creditors. Normally, Paris Club agreements are predicated upon an IMF stand-by arrangement or the equivalent. We will see if the exception becomes the rule. It is noteworthy in terms of the second question that Nigerian government officials have been quoted as saying that this form of IMF support will not involve conditions on Nigerian policies.

A special type of IMF support for a country, where IMF resources would not be involved, is a mechanism whereby the Fund provides an instrument to help a member cope with a positive external shock such as a surge in the price of a commodity that represents a large share of its export earnings. The facility would assist the country to avoid the “Dutch Disease” of currency appreciation that undermines export competitiveness and pro-cyclical fiscal policies.

Kristin Forbes (2005) has proposed such a mechanism for dealing with a positive external shock. Her proposal bears a family resemblance to the CFF, which provides countries a modest amount of access to IMF financing with low conditionality in the context of negative external shocks. The terms for access to the CFF have been tightened in recent years, which has contributed to sharply reduced use of the facility compared with the 1970s and early 1980s. Buirra (2005, 23-24) suggests that a more representative governance structure at the IMF might lead to a reversal of these trends.¹⁰⁹

At the IMFC meeting in April 2004, US Treasury Secretary Snow (2004) re-opened IMF consideration of a mechanism (a policy monitoring arrangement) through which the IMF could provide support for members without lending:

To strengthen its policy role, we favor the development of a new form of engagement for countries that do not have a financing need. Under this proposal, the IMF could assess an economic program prepared by the country itself and signal its view to donors, MDBs [multilateral development banks], and markets. Such a nonborrowing vehicle for close engagement would benefit both poor countries and emerging market countries, as it will show that a country has clear ownership of its policies and is strong enough to stand on its own feet.

In April 2005, the G-7 and the IMFC indicated their support for the US proposal in the context of the IMF’s engagement with low-income (PRGF-eligible) countries. Part of the rationale is that these countries cannot afford to borrow even on highly subsidized PRGF terms and the proposed mechanism would be analogous to a grant of policy endorsement without financial resources.

At the April 2005 meeting of the IMFC, German Finance Minister Eichel (2005) indicated his support for the establishment of a policy monitoring arrangement to assist countries in graduating from IMF financial support as long as the terms involved upper-credit-tranche conditionality and regular reviews by the executive board. Canadian Finance Minister Goodale (2005) also expressed support for the idea to strengthen surveillance relationships with developing countries in general, those with higher incomes as well as low incomes per capita.

Acting Under Secretary Quarles (2005) reported to the US Congress on progress in promoting the US initiative with respect to nonborrowing IMF programs. In his remarks, he left open the possibility that the mechanism would be available to all members of the IMF, not just to

¹⁰⁹ It is of some note in connection with the CFF and related facilities that the G-8 finance ministers meeting in London on June 11, 2005 agreed “the IFIs have a role in helping address the impact of higher oil prices on adversely affected developing countries and encourage the IMF to include oil prices in the development of facilities to respond to shocks.” However, to date, nothing has happened.

low-income members. Time will tell whether the mechanism will be generalized, but it is widely expected that such a “policy support instrument” that does not involve IMF lending will be in place for low-income countries by the time of the 2005 IMF Annual Meetings.

Support for Low-Income Countries

IMF support for low-income countries, defined for these purposes as PRGF-eligible members, takes many forms.¹¹⁰ They participate, of course, directly and through their representatives in all IMF activities. They all are covered by IMF surveillance. They receive technical assistance from the IMF. By definition they are eligible to borrow from the PRGF and to receive related forms of highly subsidized financial support. In principle, they are also eligible to borrow from other facilities including the CFF, the EFF, and regular SBA. Those low-income countries that are also in the category of Heavily Indebted Poor Countries (HIPC) have, since 1999 been potentially eligible for partial reduction of their debts to the IMF and other international financial institutions, and a subset of them are now expected to be in line for 100 percent reduction of their debts to the IMF.¹¹¹

It was not always the case that low-income countries had special IMF facilities. In 1975, when 49 of the current 77 PRGF-eligible countries were members of the Fund, 28 of them had credit outstanding to them from the Fund on regular financial terms. For the most part the absolute poverty of these countries was no lower in 1975 than it is today. At that time, the international community was less sensitive to the build up of their external debts, more optimistic that low-income countries would be able to grow out of their debts, or more concerned that special facilities distorted the universal character of the Fund.

Another important change over the past 30 years has been the progressive shift of the IMF from balance-of-payments lending into longer-term, structural adjustment lending, which accelerated in the late 1980s (Bird 2003, 2-10). First, the IMF in 1975 established a Trust Fund with some of the proceeds from its gold sales to lend to low-income countries. In 1976 the EFF was created. In early 1986, a Structural Adjustment Facility (SAF) replaced the Trust Fund. In 1987, the SAF was transformed into an Enhanced Structural Adjustment Facility (ESAF). However, “Structural adjustment” had a bad ring to it. Moreover, the NGO community criticized the ESAF because, with some reason, it saw structural policy conditions being imposed on countries merely so that they could qualify for loans that were largely employed to refinance old loans from the IMF. Thus, the ESAF morphed into the PRGF where, in principle, the borrowing country through the participatory drafting of its PRSP has a greater say in the policy conditions. This process is described as an effort to improve ownership and performance. To some observers it is a manifestation of IMF and World Bank policy failure.

The transformation of the nature of IMF lending to low-income countries into structural lending, by one name or another, has meant that the IMF increasingly has become involved with policy issues that had been principally the responsibility of the World Bank. Similarly, the Bank

¹¹⁰ In September 2004, de Rato (2004) stressed the IMF’s partnership role in supporting its low-income members.

¹¹¹ The G-8 proposal for 100 percent reduction of debts of certain HIPC borrowers from the IMF has implications not only for those countries but also for the IMF’s involvement with them and potential for the IMF’s financial structure because of the involvement of the IMF’s gold.

has become more involved in and conscious of the macroeconomic and financial policies of countries receiving World Bank loans. Consequently, the Fund and the Bank have been called upon to collaborate more intensively and with mixed results.¹¹²

Three issues are on the agenda for IMF reform with respect to its support for low-income members: Should the IMF continue to lend to these members? Should the IMF's involvement in PRGF lending be terminated? If IMF participation in PRGF lending is terminated, what type of lending arrangements for low-income countries, if any, should take its place?

The Bush administration, aggressively following up on initiatives of the Clinton administration with respect to the development agenda for low-income countries (HIPC relief and greater reliance on grants), has included on its expanded agenda a number of elements involving the IMF's support of such countries. Snow (2004) at the April meeting of the IMFC advocated that the IMF continue to lend to poor members but only for balance-of-payments needs; development needs should be met by development banks and bilateral donors, not the IMF; the IMF should marshal grants to support strong performers and those facing macroeconomic setbacks; and low-income countries with strong fundamentals should move beyond PRGF borrowing to nonborrowing engagement with the IMF.

The US-supported elements are part of an ongoing debate about the IMF with respect to low-income members. The basic argument for continued intensive IMF involvement with its low-income members is that good macroeconomic policy is crucial to economic development, growth, and the reduction of poverty. The management and staff of the IMF are not inclined to back off from engagement with its low-income members. In their view, the IMF is the accepted international arbiter of such policies and must be continuously engaged in their support and evaluation. Furthermore, if the IMF is to play its role effectively, it needs to use its "own money" as leverage.

In April 2004, before the IMFC meeting, the executive board (2004b) expressed its continued support for the IMF's "important role in low-income member countries in terms of surveillance, policy advice, financing and technical assistance." Most directors preferred the continued availability of small PRGFs. Many directors did not support precautionary PRGF arrangements—an alternative to nonborrowing support.

The spring 2005 IMFC communiqué devoted five paragraphs exclusively to the IMF and its support for low-income countries, demonstrating little appetite to disengage from lending to low-income members. French Finance Minister Breton (2005) explicitly said that the existing PRGF is a suitable tool for the IMF as a universal institution to use to support low-income countries.

With respect to collaboration between the Fund and World Bank on country programs and conditionality, the IMF executive directors (IMF 2004c) concluded that the evidence

¹¹² This collaboration and the issues that give rise to the need for it are not limited to the low-income countries. Structural issues are part of IMF-supported programs with most members, and the Bank has become increasingly, some would say excessively, conscious of the macroeconomic and financial context of lending to all of its borrowers.

supported renewed support for the existing operational framework for such collaboration. At the same time they stressed that there was no room for complacency with respect to country ownership and tensions over the coverage of conditionality and the scope and pace of reforms.¹¹³

All observers do not accept the status quo with respect to the IMF's role in the PRGF. Meltzer (2005a), consistent with the majority recommendation of the 2000 report of the IFIAC that he chaired, states simply that the PRGF should be closed. The Council on Foreign Relations (1999) report implied as much in its recommendation that the Fund and Bank should refocus on their respective core activities. Bergsten (2005), a member of the IFIAC, would prefer to transfer the PRGF to the World Bank, because its primary mission is poverty reduction. David Bevan (2005), commenting on a choice between (a) the status quo, (b) dropping the balance-of-payments façade associated with IMF lending to the low-income countries through the PRGF and adopting a more realistic IMF program of 25-year financial support, and (c) the IMF's getting out of the business of long-term loans, favors the third option. One wonders if the prospect of 100 percent IMF debt reduction for a subset of the HIPC borrowers from the IMF under the PRGF will not and should not lead to a reassessment of this issue by the IMF's membership as a whole, leading to the third option.

If the PRGF were transferred to the World Bank, a question would remain whether the IMF should get completely out of the business of lending to low-income countries. Some say yes. Others argue that the possibility of lending to meet traditional, short-term, balance-of-payments needs should not be excluded. That appears to be the position of Canadian Finance Minister Goodale (2005) who expressed support for limiting the PRGF to providing "rapid assistance to alleviate short-term external payments distress" for low-income members of the IMF. This is a reasonable position, and such lending to very poor countries might also be subsidized.

What about ensuring sound macroeconomic policies in low-income countries? One approach would be that the IMF should continue to conduct its surveillance of the policies—macroeconomic and financial sector policies—of its low-income members. The World Bank (IDA) should take account of the IMF's views. Where the Bank staff agrees with those views it should say so in its documentation and where it does not it should also explain its views. Continued Article IV consultations and ex post evaluations of IDA lending should over time induce more de facto coordination than occurs de jure today. The Bank would learn from its mistakes and pay for them. (One problem some might reasonably argue is that the shareholders that would pay are also the shareholders in the IMF.) As part of such a "deal," the IMF might take over from the Bank full responsibility for countries' financial sector policies.

All of these issues are yet to be resolved.

¹¹³ The underlying document was based on a survey of Fund mission chiefs and Bank country directors. No doubt some of them were forthright in their responses, but one wonders if there were not incentives to support the status quo.

IMF Financial Resources

The IMF is an international financial institution. Like other financial institutions it is in the business of making loans consistent with its charter and policies, in other words, under appropriate circumstances and with appropriate conditions and protections. The determination of appropriate circumstances and appropriate conditions and protections is one place where selectivity enters the picture.¹¹⁴ Appropriate conditions include the potential for private sector involvement in financing a country in crisis.¹¹⁵ A natural question is whether the IMF has enough financial resources to carry out its responsibilities now and for the immediate future.

If the answer to this first question is that it does not now have adequate resources to discharge its responsibilities or it is likely to run short over the next five to ten years, then a follow-up question is how best should the IMF augment its resources? Should it look toward another increase in quotas? Should it rely more heavily on borrowing from members through standing arrangements such as the General Arrangements to Borrow (GAB) and the New Arrangements to Borrow (NAB) or through ad hoc means? Alternatively, should it look to borrow in the market or should it seek to mobilize the latent profits on its holdings of gold?

Finally, where do SDR fit into the IMF's activities and its financial operations in the 21st century? Is it important to ratify the Fourth Amendment of the Articles of Agreement?¹¹⁶ Looking forward, should the SDR be put on the shelf, should regular allocations be resumed, should existing allocations be cancelled, or should the mechanism be transformed so it can provide some type of global public good rather than just increasing global liquidity? This section examines: (1) the IMF's need for additional resources, (2) how its resources should be augmented, and (3) the future role of the SDR.

The IMF's Need for More Resources

Does the IMF need more financial resources right away today or tomorrow? The answer is almost certainly no.

As of July 28, 2005, the IMF's one-year forward commitment capacity, the metric it now uses to measure its capacity to make new financial commitments, was about \$133 billion, easily the highest level in its history, and essentially twice its lending capacity at the end of 2002.¹¹⁷ In addition, the IMF has about another \$50 billion available from its standing borrowing arrangements, the GAB and the NAB. An alternative traditional measure of IMF lending capacity, the IMF's liquidity ratio, is 2¼ times what it was at the end of 2002.¹¹⁸ This dramatic

¹¹⁴ On circumstances and conditions, see also the discussion and information in the introduction to this paper.

¹¹⁵ Selectivity also enters the picture with respect to crisis prevention, surveillance, and possible prequalification for IMF lending.

¹¹⁶ That amendment provides a one-time allocation of SDR in order to put members of the IMF that joined after the first 1970-72 and/or second 1979-81 general allocations of SDR on a roughly equal footing with other members.

¹¹⁷ The IMF defines its "one-year forward commitment capacity" as its usable resources (holding of currencies of members in strong enough external positions that their currencies can be lent to other countries *plus* the IMF's holdings of SDR) *minus* lending commitments *plus* repayments to the Fund over the next year *minus* a generous prudential balance.

¹¹⁸ The liquidity ratio is the ratio of net uncommitted resources to liquid liabilities.

improvement reflects in part the repayments and early repayments to the Fund by Russia and Brazil and, in part, benign global economic and financial conditions that have meant that there have not been any large net new demands on the IMF.

Quotas are the traditional source of IMF resources to lend although borrowing from members from time to time has been used as a supplement. The second memorandum item in table 4 provides the IMF's credit outstanding as a percent of total quotas for seven dates over the past 30 years. The average is 26.6 percent, and the figure for May 31, 2005 was 26.0 percent. Table 7 provides a longer-term perspective on IMF quotas relative to a number of other indicators of the development of the global economy. We estimate that as of the end of 2005, total IMF quotas relative to reserves will have fallen to the lowest level in the past 35 years; this reflects in large part the build up in foreign exchange reserves by a large number of countries since the end of 2000. On the other hand, total IMF quotas relative to GDP at market prices are within the range of the past 30 years, and total quotas relative to international trade in goods and services are only slightly below their range over that period.¹¹⁹

The last line in the table provides a projection of what these three ratios would look like in 10 years if there were no increase in IMF quotas (except an assumed 25 percent boost to their dollar value in connection with depreciation of the US dollar against the SDR) and using compound growth rates for the period 1990 to 2005. Quotas would continue to decline substantially relative to foreign exchange reserves and decline relative to international trade compared with the range over the past 30 years. For GDP, the ratio drops to the low recorded in 1990. Using GDP on a PPP basis, the ratio falls 20 percent below its equivalent 1990 value.

Those who want the IMF to discharge its current responsibilities more effectively, for example, lending larger amounts in connection with capital account crises, tend to favor a substantial increase in IMF quotas in connection with the 13th quota review (Buirea 2005, Kelkar et al. 2005, and Ortiz 2005). Those who envision enlarged responsibilities for the IMF tend to think the IMF will require a substantial increase in IMF resources to discharge them (Ubide 2005 and Rajan 2005b). Japanese Finance Minister Tanigaki (2005) has expressed support for a quota increase, and his Korean colleague Finance Minister Lee (2004) did so in stronger terms.

On the other hand US Treasury Secretary Snow has stated that the United States sees no need to increase IMF quotas at this time in part because it is desirable to limit the growth in the size of the Fund in order to discourage large-scale IMF lending. Former US Treasury Secretary Paul O'Neill (2002) told the IMFC in September 2002, as the 12th quota review was coming to a

¹¹⁹ As is almost always the case, different calculations by different authors can suggest somewhat different conclusions. For a longer period, Buirea (2005) estimates that the size of the Fund declined from 58 percent of trade in 1945, to 15 percent in 1965 before the great inflation and the collapse of the Bretton Woods system, to an estimated 4 percent "at present," presumably 2003. (The last figure is higher than that shown in table 7 and possibly because we included trade in both goods and services.) Kelkar et al. (2005, three coauthors) compare the size of the Fund (total IMF quotas) in 1978 at the time of the 7th quota review and in 1998 at the time of the 11th review. He finds that the size of the Fund declined from 8.7 to 3.7 percent relative to current payments, from 1.4 to 0.9 percent relative to GDP, 33 to 18.4 percent relative to international reserves, and 9 to 6 percent in terms of imports. It is reasonable that quotas declined more relative to current payments than relative to imports, because non-trade current account items have increased in importance over this period, but I cannot explain the large decline in the Kelkar estimates of the size of the Fund relative to imports or relative to GDP compared with the data in table 7.

conclusion, “Limiting official resources is a key tool for increasing discipline over lending decisions.” (To date, O’Neill’s successor has not distanced US policy from this position.) In fact, over the past five years, the amount of IMF credit outstanding to emerging market members of the IMF has increased by more than 20 percent. Regardless of this record and the reasons for it, using an obscure budget constraint to enforce selectivity in IMF lending is questionable international public policy compared with a need-based approach in which selectivity is based on circumstances, policy conditions, and protections.

Augmenting the IMF’s Resources

Over the IMF’s 60 years increases in IMF quotas have occurred on average every 6.6 years—5.6 years since 1959.¹²⁰ On the other hand, the gap between the last two quota increases was 8 years and the previous gap was 7 years. Formal agreement on the last quota increase was reached in January 1998. Any way one looks at the historical data, they point to pressure for another increase in the next two or three years, at least by the end of the 13th quota review period in January 2008. However, don’t bet on an agreement to increase IMF quotas unless policies of the major IMF members or economic and financial circumstances change dramatically from what they are today.

A more reasonable bet is that strong pressures will build for a further increase in IMF quotas by 10 years from now. One reason for action sooner rather than later is that it difficult to imagine the IMF successfully addressing the issue of the distribution of IMF quotas in any other context than an overall increase in quotas because each country has an individual veto over any reduction in the absolute size of its quotas. In this context, the US position favoring a redistribution of quota shares but not favoring an increase in the total of IMF quotas at this time, and implicitly at any future time, is at best naïve and at worst cynical. Nevertheless, it may be a strategic calculation.

Augmentation of standing borrowing arrangements has been even more difficult to negotiate than quota increases. There have only been two such augmentations since 1962 when the GAB was first established—the augmentation of the GAB in 1983 and the grafting onto the GAB of the NAB in 1998. If the IMF wants to increase its resources, it could explore two other options: borrowing from the market and gold sales.

The advantage of IMF market borrowing is that doing so requires only a simple (weighted) majority of the IMF executive board rather than an 85 percent majority in connection with a generalized increase in quotas following a quota review. As increase in IMF quotas, in turn, must be approved by governments, starting with the US Congress. Adam Lerrick (1999) estimated that the IMF might be able to borrow in the market as much \$100 billion over time. The total that could be borrowed would be constrained by the liquid resources of the IMF and the value of its gold stock.

¹²⁰ The total of IMF quotas may increase slowly over time with the admission of new members and ad hoc adjustments in quotas, which have been rare. The text refers to increases in IMF quotas associated with general reviews of the size of the Fund.

Bird (2003) sees IMF borrowing in the private market as a temporary counter-cyclical source of additional financing for the IMF. When markets are holding back in lending to developing countries, the IMF could borrow and use the resources to increase lending to those countries. He also sees such an activity as having the benefit of making the IMF more market sensitive. For Bird it is an advantage that a program of market borrowing would loosen political influences over the scale of IMF lending. Kelkar et al (2005, three coauthors) makes many of the same arguments. From another perspective, one disadvantage of this mechanism for augmenting IMF financial resources, other than the fact that it cannot be expanded without limit, is that it would for a substantial period *remove* a political constraint on IMF lending activities. Both perspectives fail to recognize that the IMF is inherently a political institution because governments own and direct it.

The approach of using the proceeds of IMF gold sales to augment IMF resources looks more attractive to some observers. IMF gold holdings are worth about \$45 billion at current market prices. The IMF carries its existing gold holdings of 103.4 million ounces at about \$9 billion.¹²¹ Therefore, if the IMF could sell its gold stock at about the current market price of \$430 per ounce, it would realize about \$36 billion in extra resources.¹²²

In addition to providing financial resources to the IMF, sales of IMF gold holdings would help to further phase gold out of the international monetary system. It would provide the IMF with a significant amount of assets that could earn returns and help to finance the nonlending activities of the IMF.¹²³ For this reason, representatives of developing countries, for example the G-24 (2005) and Indonesian Central Bank Governor Abdullah (2005) have expressed some interest in the idea along with the creation of an IMF investment account that would also generate financial returns to help support the IMF's activities.¹²⁴ On the other hand, the amount

¹²¹ Before 1999, the entire IMF gold stock was valued at SDR 35 per ounce, or about \$5.2 billion at the end-July 2005 dollar price of the SDR. In 1999 and 2000, the IMF increased the average value of its gold stock via transactions with Brazil and Mexico that had the effect of raising the valuation of a portion of the stock to the prevailing market price. The interest earnings on the realized capital gains from the gold transactions are being used to finance the first round of HIPC debt relief in the IMF.

¹²² Some argue that the IMF sales of as much as 100 million ounces of gold on the market would severely depress the market price and cause economic damage to gold holders and producers. Dale Henderson, John Irons, Steven Salant, and Sebastian Thomas (2005) provide a theoretical argument and empirical estimates that demonstrate this need not be the case. Their analysis is based on the assumption and revealed evidence that there is a service use of gold (for example jewelry) as well as depletion uses (tooth fillings). They also argue that the net welfare gain associated with government gold sales now compared with delaying those sales indefinitely is substantial, about \$340 billion. The net loss if the sales were delayed 20 years is estimated at \$105 billion. Philipp Hildebrand (2005) offers practical evidence about how an announced program of gold sales by the Swiss National Bank over a multi-year period appear to have had little effect on the market price of gold.

¹²³ The administrative cost of running the IMF in 2005 is more than \$800 million. Some worry that if the amount of IMF lending declines permanently, the IMF will either have to cut back on its activities or increase the interest rates on its loans further.

¹²⁴ Some argue that IMF borrowing countries pay a disproportionate share of IMF administrative expenses. Wood and Lombardi (2005) use a figure of 98 percent estimated on the basis of the difference between the interest earnings of the IMF and the return that IMF creditors receive relative to the SDR interest rate on their lending to the IMF. The G-24 (2005) complains, moreover, that two-thirds of the IMF's budget is not directly related to lending activities. See the brief discussion in the introduction of the IMF's technical assistance activities that absorb about a quarter of the Fund's internal resources. A relevant consideration as well is the fact that the IMF has been operating with a freeze on positions for several years. The Woods and Lombardi estimates are clearly too high because they ignore the underlying cost to creditor countries of lending to and through the IMF. Adam Lerrick (2003) places that

of additional resources that the IMF could raise through gold sales is not large. Moreover, some argue that IMF gold sales would weaken the IMF financially especially if the proceeds were used to expand IMF lending. Of more practical relevance, the United States has a double veto over IMF gold sales; they require an 85 percent majority vote and before the US Treasury Secretary can authorize a positive vote he must obtain the consent of the US Congress.¹²⁵

A final proposal for financing the IMF would involve the creation of an International Financial Stability Facility (IFSF) (Truman 2001) that would be financed by annual fees on stocks of cross-border investments and could be tapped by the IMF under certain circumstances to finance in whole or in part large programs of IMF financial support to systemically important countries. The IFSF is certainly not the most attractive alternative financing mechanism for the IMF, but it has the advantage of prepositioning financing from the private sector that can be disbursed, in part, for the benefit of the private sector, in other words, prepaid private sector involvement.

The Future of the SDR

Where does the SDR fit into the future financing of the IMF? The IMF issues SDRs to members in proportion to their quotas. SDR holdings are an alternative to foreign exchange holdings. Governments can use SDRs to deal with temporary payments imbalances, just as they use foreign exchange reserves. If countries have large foreign exchange or SDR holdings they are less likely to need to borrow from the International Monetary Fund.

The IMF has issued a total of SDR 21.4 billion (about \$30 billion at the dollar price of SDR at the end of July 2005) in 1970-72 and 1979-81. Under the fourth amendment of the IMF Articles of Agreement an additional SDR 21.9 billion would be issued principally to those countries that joined the IMF before one or both of the issues of SDR. The IMF's Board of Governors approved the amendment in 1997. Enough members have ratified the amendment that it will go into force as soon as the US Congress does so. IMFC communiqués (2005) routinely call for completing the ratification of the amendment.¹²⁶

Bird (2003, chapter 14) argues that the SDR as an alternative reserve asset in the international monetary system is destined to return to obscurity. His is an argument based on politics as well as economics. He makes this argument in a paper that was first published in 1998 following a debacle at the IMF Annual Meeting in Madrid on the SDR issue. At that meeting, there was a strong initial presumption promoted by Managing Director Camdessus that a positive

figure at about \$600 million for the United States alone, about seven times the figure of about \$80 million Woods and Lombardi estimate for all creditor countries. Many would argue that Lerrick's figure is too high because he uses long-term interest rates to estimate the costs of US borrowing and US "loans" to the IMF are liquid claims that should be compared with short-term government borrowing rates, but the Woods and Lombardi figure is too low. Lerrick also triples his estimate to account for his assessment of the risk associated with IMF loans despite the fact that actual defaults on IMF loans have been minimal and losses can be covered by accumulated reserves.

¹²⁵ Neither veto is relevant to the potential "use" of gold to help "finance" the G8 proposal for 100 percent debt relief for certain HIPC borrowers. However, the IMF self-financing of that proposal has raised a number of other issues for the IMF.

¹²⁶ Managing Director de Rato (IMF 2005g) reported in April 2005 that 131 members of the Fund (71 percent) with 77 percent of the votes had ratified the amendment. US ratification would raise the second figure to 94 percent.

decision would be taken to resume SDR allocations, but the proposal was killed by the G-7 who had failed to communicate clearly to Camdessus and to the rest of the IMF membership their position or, alternatively, Camdessus and the rest of non-G-7 members of the executive board failed to understand the G-7 position before they broke for the meeting in Madrid.

The basic argument against a resumption of regular SDR allocations is that the international monetary and financial systems have undergone profound changes since the mechanism was established in 1969, as indeed they have. The argument made is that with floating exchange rates countries do not need international reserves or if they need reserves they can borrow them on international capital markets. The problem is that the facts do not fit the argument. Most countries do not borrow their foreign exchange reserves; they accumulate them by running current account surpluses that distort current account positions while forcing poor countries to lend to rich countries. Between 1994 and 2004 the foreign exchange reserves of emerging market and other developing countries more than quadrupled from SDR 293 million to SDR 1,247 million.¹²⁷ Recall that the data presented in table 7 demonstrate a secular decline in the ratio of IMF quotas to foreign exchange reserves.

At the analytical level, Michael Mussa (1996) made the case for the allocation of SDR under the current IMF Articles of Agreement, which require a finding of “long-term global need, as and when it arises, to supplement existing reserve assets in such a manner as to promote the attainment of its [the Fund’s] purposes and will avoid economic stagnation and deflation as well as excess demand and inflation in the world.” (Article XVIII, 1(a).) The counter-argument is that in today’s international monetary system, one can never find such a “long-term global need.”

Peter Clark and Jacques Polak (2004) provided a fresh examination of this issue. They argued that a resumption of regular SDR allocations would benefit the functioning of the international monetary system by lowering the interest cost of holding reserves and enhancing the strength of the system as a whole through greater reliance on owned versus borrowed reserves. Boyer and Truman (2005) reach a similar conclusion and stress, as well, the contribution of a resumption of SDR allocations to global cooperation and the resolution of global imbalances by lowering incentives for some countries to have essentially fixed, undervalued exchange rates. At the policy level, the Zedillo Report (UN 2002b) called for the resumption of regular SDR allocations. Buira (2005) and Stephany Griffith-Jones and Jose Antonio Ocampo (2004) do as well.

It is noteworthy that despite the opposition to the resumption of SDR allocations based on the specious argument that doing so would damage the international financial system, for example, by weakening balance of payments discipline (what discipline?) or contributing to inflation, no one, to my knowledge, has called for cancellation of the existing outstanding stock of SDR. Nevertheless, betting people are unlikely to place much money on the resumption of SDR allocations in connection with the original purpose of augmenting countries’ holdings of international reserves.

¹²⁷ These figures exclude the reserves of industrial countries and PRGF-eligible countries. The categories of countries are the same as those underlying tables 1-6. The increase for other developing countries as a group, 284 percent, was almost as large as the increase for emerging market countries as a group, 334 percent.

On the other hand, a number of people advocate the modification of the purpose of SDR allocations. For example, a proposal broadly consistent with the original purpose has been made by a Council on Foreign Relations task force (1999) that advocated special allocations of SDR to fund on a one-time basis a “contingency facility” in the IMF. Richard Cooper (2002) goes further and would allow the IMF to make temporary issues of SDR to deal with financial crises and forestall creditor panics. Camdessus (Camdessus et al. 2004) also favors selective emergency, self-liquidating SDR allocations, as do Kelkar et al. (2005, both sets of coauthors).

Departing further from the original purposes of the SDR, the G-24 (2004) continues to advocate the creation of SDR and the voluntary redistribution of them to developing countries to increase aid flows. Soros (2002) argues for the creation of SDR to fund grants for specific global public goods and poverty reduction programs. The Soros proposal is essentially a device to fund additional aid flows by avoiding national appropriation processes, as was the SDR-aid link that was widely discussed in the 1960s and 1970s.

The best guess is that nothing will happen with respect to the SDR in the next decade or so. The fourth amendment will not be ratified, which is untidy, SDR will not be allocated or cancelled, and none of the proposals for stretching or transforming the SDR’s role will come to fruition. The SDR is not as central to the reform of the IMF as some of the other issues that have been reviewed in this paper.

Concluding Remarks

The IMF is in eclipse as the preeminent institution of international financial cooperation. Consequently, the world is worse off. Despite the considerable reforms over the past decade, more should be done.

This paper has reviewed the case for further IMF reform and considered some of the major reform proposals. The necessary steps cover all aspects of IMF responsibilities and operations. A major priority is IMF governance. An equally important priority is to upgrade the IMF’s role in the international monetary system. In addition, improvements should be made in IMF lending operations, and the IMF must be pulled back from becoming just another development financing institution. The IMF’s financial resources will soon need to be augmented.

Table 1: IMF Members 2005—Total 184

	Industrial (24)	Emerging (22)	Other Developing (61)	PRGF (77)
Africa (53)		South Africa (1)	Algeria, Bahrain, Botswana, Equatorial Guinea, Gabon, Mauritius, Morocco, Namibia, Seychelles, Swaziland, Tunisia (11)	Angola, Benin, Burkina Faso, Burundi, Cameroon, Cape Verde, Central African Republic, Chad, Comoros, Democratic Republic of Congo, Republic of Congo, Côte d'Ivoire, Djibouti, Eritrea, Ethiopia, Gambia, Ghana, Guinea, Guinea-Bissau, Kenya, Kiribati, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritania, Mozambique, Niger, Nigeria, Rwanda, São Tomé and Príncipe, Senegal, Sierra Leone, Somalia, Sudan, Tanzania, Togo, Uganda, Zambia, Zimbabwe (41)
Asia (34)	Australia, Japan, New Zealand (3)	China, India, Indonesia, Korea, Malaysia, Philippines, Singapore, Thailand (8)	Brunei Darussalam, Fiji, Marshall Islands, Micronesia, Palau (5)	Afghanistan, Bangladesh, Bhutan, Cambodia, Lao, P.D.R., Maldives, Mongolia, Myanmar, Nepal, Pakistan, Papua New Guinea, Samoa, Solomon Islands, Sri Lanka, Timor-Leste, Tonga, Vanuatu, Vietnam (18)
Europe (49)	Austria, Belgium, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Luxembourg, Netherlands, Norway, Portugal, San Marino, Spain, Sweden, Switzerland, United Kingdom (19)	Turkey, Russia, Hungary, Czech Republic, Poland (5)	Belarus, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Estonia, Kazakhstan, Latvia, Lithuania, Macedonia, Malta, Romania, Serbia & Montenegro, Slovak Republic, Slovenia, Turkmenistan, Ukraine (17)	Albania, Azerbaijan, Armenia, Georgia, Kyrgyz Republic, Moldova, Tajikistan, Uzbekistan (8)
Middle East (14)		Egypt (1)	Iran, Iraq, Israel, Jordan, Kuwait, Lebanon, Libyan Arab Jamahiriya, Oman, Qatar, Saudi Arabia, Syrian Arab Republic, United Arabs Emirates (12)	Republic of Yemen (1)
Western Hemisphere (34)	Canada, United States (2)	Argentina, Brazil, Chile, Colombia, Ecuador, Mexico, Venezuela (7)	Antigua and Barbuda, Bahamas, Barbados, Belize, Costa Rica, Dominican Republic, El Salvador, Guatemala, Jamaica, Panama, Paraguay, Peru, St. Kitts and Nevis, Suriname, Trinidad and Tobago, Uruguay (16)	Bolivia, Dominica, Grenada, Guyana, Haiti, Honduras, Nicaragua, St. Lucia, St. Vincent and the Grenadines (9)

Table 2: The Composition of IMF Membership—1975 and 2005

2005	Africa	Asia	Europe	Middle East	Western Hemisphere	Total
Industrial	0	3	19	0	2	24
Emerging Market ^a	1	8	5	1	7	22
Other Developing	11	5	17	12	16	61
PRGF-Eligible ^b	41	18	8	1	9	77
Total	53	34	49	14	34	184

1975	Africa	Asia	Europe	Middle East	Western Hemisphere	Total
Industrial	0	3	17	0	2	22
Emerging Market ^a	1	8	1	1	7	18
Other Developing	9	1	4	12	12	38
PRGF-Eligible ^b	31	10	0	2	6	49
Total	41	22	22	15	27	127

a. Even though India is PRGF-eligible, we classify it as an emerging market economy as it is often treated as such by market participants.

b. Based on IMF categorization as of March 2005.

Table 3: Distribution of Members with IMF Credit Outstanding—1975 -2005 (Percent)^a

Category of Country	1975	1980	1985	1990	1995	2000	2005 ^b
Industrial	11	10	2	0	0	0	0
Emerging Market^c	13	9	18	16	11	11	7
Western Hemisphere	4	1	6	7	5	4	4
Asia	6	5	8	6	2	4	2
Other	4	3	4	3	4	2	1
Other Developing	17	20	20	22	30	22	20
PRGF-Eligible^d	58	61	60	62	59	67	73
Africa	34	39	37	41	37	40	44
Other	25	23	23	21	22	28	29
Total	100	100	100	100	100	100	100
Memo:							
Total number of countries with credit outstanding	53	80	87	86	98	91	85
Countries with credit outstanding as a percent of total members	42	57	58	56	55	50	46

- a. The data capture all member countries that borrowed from the IMF over the 1975-2005 period, with the exception of Czechoslovakia/The Czech Republic. This country was briefly indebted to IMF between 1991 and 1994. Consequently it was not picked up as having had credit outstanding to IMF in either 1990 or 1995. See footnote 16 in the text for more details.
- b. Data as of May 31, 2005.
- c. Even though India is PRGF-eligible, we classify it as an emerging market economy as it is often treated as such by market participants.
- d. Based on IMF categorization as of March 2005.

Table 4: Distribution of IMF Credit Outstanding—1975-2005 (Percent) ^a**A. By Category of Country**

	1975	1980	1985	1990	1995	2000	2005 ^b
Industrial	48	12	2	0	0	0	0
Emerging Markets ^c	27	35	60	60	63	70	76
Others Developing	7	16	13	11	15	9	10
PRGF-Eligible ^d	19	37	24	29	22	18	14
Total	100	100	100	100	100	100	100

B. By Region of the World

	1975	1980	1985	1990	1995	2000	2005 ^b
Africa	8	26	22	25	17	13	9
Asia	28	38	30	15	12	38	15
Europe	49	20	10	4	27	34	28
Middle East	4	5	1	1	1	1	1
Western Hemisphere	11	11	37	55	43	14	47
Total	100	100	100	100	100	100	100
Memo:							
Total credit outstanding (in billions of SDR)	7.4	11.1	37.7	23.3	41.6	49.3	55.6
Percent of total quotas	25.1	17.6	40.0	25.6	28.6	23.4	26.0

a. The data capture all member countries that borrowed from the IMF over the 1975-2005 period, with the exception of Czechoslovakia/the Czech Republic. This country was briefly indebted to IMF between 1991 and 1994. Consequently it was not picked up as having had credit outstanding to IMF in either 1990 or 1995. See footnote 16 in the text for more details.

b. Data as of May 31, 2005.

c. Even though India is PRGF-eligible, we classify it as an emerging market economy as it is often treated as such by market participants.

d. Based on IMF categorization as of March 2005.

Table 5. Share of Groups of IMF Members with Credit Outstanding—1975-2005 (Percent) ^a

A. By Category of Country

	1975	1980	1985	1990	1995	2000	2005 ^b
Industrial	27	36	9	0	0	0	0
Emerging Market ^c	39	39	84	67	50	45	27
Other Developing	24	40	40	42	51	33	28
PRGF-Eligible ^d	63	82	80	80	76	80	81
Total	42	57	58	56	55	50	46

B. By Region of the World

	1975	1980	1985	1990	1995	2000	2005 ^b
Africa	44	77	74	79	77	75	74
Asia	55	64	70	57	35	39	32
Europe	36	41	22	12	50	44	35
Middle East	20	13	13	21	21	14	21
Western Hemisphere	44	55	71	68	58	44	44
Total	42	57	58	56	55	50	46

a. The data capture all member countries that borrowed from the IMF over the 1975-2005 period, with the exception of Czechoslovakia/the Czech Republic. This country was briefly indebted to IMF between 1991 and 1994. Consequently it was not picked up as having had credit outstanding to IMF in either 1990 or 1995. See footnote 16 in the text for more details.

b. Data as of May 31, 2005.

c. Even though India is PRGF-eligible, we classify it as an emerging market economy as it is often treated as such by market participants.

d. Based on IMF categorization as of March 2005.

Table 6: Countries Borrowing from the Fund—1970 to Present ^a

Category of Countries	Borrowers (139) ^b	Nonborrowers (45)	Percent of Borrowers (76)
Industrial (24)	Australia, Finland, Greece, Iceland, Italy, New Zealand, Portugal, Spain, United Kingdom (9)	Austria, Belgium, Canada, Denmark, France, Germany, Ireland, Japan, Luxembourg, Netherlands, Norway, San Marino, Sweden, Switzerland, United States (15)	38
Emerging (22)	Argentina, Brazil, Chile, China, Colombia, Czech Republic, Ecuador, Egypt, Hungary, India, Indonesia, Korea, Malaysia, Mexico, Philippines, Poland, Russian Federation, South Africa, Thailand, Turkey, Venezuela (21)	Singapore (1)	95
Other Developing (61)	Algeria, Barbados, Belarus, Belize, Bosnia and Herzegovina, Bulgaria, Costa Rica, Croatia, Cyprus, Dominican Republic, El Salvador, Equatorial Guinea, Estonia, Fiji, Gabon, Guatemala, Iraq, Israel, Jamaica, Jordan, Kazakhstan, Latvia, Lithuania, Macedonia, Mauritius, Morocco, Panama, Paraguay, Peru, Romania, Serbia and Montenegro, Slovak Republic, Slovenia, St. Kitts and Nevis, Swaziland, Trinidad and Tobago, Tunisia, Ukraine, Uruguay (39)	Antigua and Barbuda, Bahamas, Kingdom of Bahrain, Brunei Darussalam, Botswana, Iran, Kuwait, Lebanon, Libya, Malta, Marshall Islands, Micronesia, Namibia, Oman, Palau, Qatar, Saudi Arabia, Seychelles, Suriname, Syrian Arab Republic, Turkmenistan, United Arab Emirates (22)	64
PRGF-Eligible (77)	Afghanistan, Albania, Armenia, Azerbaijan, Bangladesh, Benin, Bolivia, Burkina Faso, Burundi, Cambodia, Cameroon, Cape Verde, Central African Republic, Chad, Comoros, Democratic Republic of Congo, Republic of Congo, Côte d'Ivoire, Djibouti, Dominica, Ethiopia, The Gambia, Georgia, Ghana, Grenada, Guinea, Guinea-Bissau, Guyana, Haiti, Honduras, Kenya, Kyrgyz Republic, Lao People's Dem. Rep., Lesotho, Liberia, Madagascar, Malawi, Maldives, Mali, Mauritania, Moldova, Mongolia, Mozambique, Myanmar, Nepal, Nicaragua, Niger, Nigeria, Pakistan, Papua New Guinea, Rwanda, Samoa, Sao Tome & Principe, Senegal, Sierra Leone, Solomon Islands, Somalia, Sri Lanka, St. Lucia, St. Vincent & the Grenadines., Sudan, Tajikistan, Tanzania, Togo, Uganda, Uzbekistan, Vietnam, Yemen, Zambia, Zimbabwe (70)	Angola, Bhutan, Eritrea, Kiribati, Timor-Leste, Tonga, Vanuatu (7)	91

a. The countries borrowing during 1970-1975 are approximated on the basis of countries that had credit outstanding in 1975.

b. Colombia, Nigeria, and Paraguay have had IMF program(s), but have not borrowed.

Table 7: IMF Quotas Relative to Reserves, GDP, and Trade (Percent)

Year	Foreign Exchange Reserves	Gross Domestic Product	International Trade ^a
1970	62.2	0.83	7.1
1975	21.3	0.54	3.2
1980	20.3	0.65	3.2
1985	25.6	0.76	4.2
1990	14.8	0.57	3.0
1995	15.6	0.74	3.5
2000	14.1	0.87	3.5
2004	8.9	0.81	3.0
2005 ^{e/b}	7.0	0.71	2.6
2015 ^{p/c}	2.9	0.57	1.6

e = estimate
p = projection

- a. Average of world exports and imports of goods and services.
b. Data from 2005 are estimated using the compound growth rates for 2000-2004.
c. Projections for 2015 use the average of the compound growth rates for the period of 1990-1995, 1995-2000, and 2000-2004: foreign exchange reserves (11.5 percent); gross domestic product (4.5 percent); and trade (7.2 percent). IMF quotas are projected for 2005 at their end-2004 level adjusted to the dollar/SDR rate on July 25, 2005. The 2015 projection assumes a 25 percent increase in the dollar price of SDR by 2015.

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