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WORKING PAPER

International Institutional Reform

Slipping into Obscurity? Crisis and Reform at the IMF

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Bessma Momani is Senior Fellow at CIGI and Assistant Professor of Political Science and History at the University of Waterloo. Holding a Ph.D. from the University of Western Ontario, her areas of specialization include: Middle East economic liberalization; and International Monetary Fund decision-making, reform, and conditionality. Among Dr. Momani's publications include; *IMF-Egyptian Negotiations* (American University of Cairo Press, 2006); and, *Twentieth Century World History* (Thomson-Nelson, 2006). On the IMF, Dr. Momani has published journal articles in *Global Society*, *Asian Affairs*, *Review of International Political Economy*, *New Political Economy*, *Canadian Journal of Political Science*, and *Journal of International Relations and Development*. Her current research on the IMF examines the history of IMF Executive Board seat and quota allocations. In addition to examining the IMF, Dr. Momani has published journal articles on Middle East economic liberalization and integration in *World Economy*, *World Economics*, and *Middle East Review of International Affairs*.

Abstract

Top policymakers worry today that the International Monetary Fund (IMF) risks 'slipping into obscurity'. What explains the IMF's declining influence? Two significant developments have been the declining demand for IMF loans from middle-income borrowers, and the emergence of a more critical view towards the institution from US policymakers in recent years. In this new political context, a range of reform proposals has been put forward by Fund management, key shareholders, and the concerned policy community with the goal of restoring and preserving the IMF's significance. Advocates of change have focused particular attention on the need for process-oriented reforms that would change the nature of IMF governance as a means of restoring its legitimacy among many member governments. Also prominent have been more outcome-oriented reforms that propose various changes in IMF activities and performance. A re-invigorated IMF is unlikely to emerge from the current situation without the implementation of governance-related reforms.

1. Introduction

What a difference a decade can make. Ten years ago, the International Monetary Fund (IMF) was seen as one of the most influential international organizations. Today, top policymakers warn that the IMF might "slip into obscurity".¹ A far-reaching debate about the IMF's future role and purpose is now underway. What has caused this decline in IMF influence? What are the most prominent IMF reform proposals today? How would the Fund be changed by these proposed reforms?

This paper attempts to provide some tentative answers to these questions. The first section argues that two developments are particularly important in explaining the Fund's recent eroding influence: the declining demand for IMF loans from middle-income borrowers, and the emergence of a more critical view towards the institution from US policymakers in recent years. In the second section, we seek to make sense of the numerous reform proposals and suggest that the most politically prominent proposals can be divided into process-oriented reforms that focus on governance issues and outcome-oriented reforms that address the Fund's performance. Finally, the paper concludes by briefly exploring future scenarios of reform implementation and the implications of the current crisis for scholarly debates about the IMF's role in global governance.

2. What Explains the IMF's Diminishing Influence?

The IMF has frequently waned in and out of a position of influence in the international financial system, has faced historical moments when its role and purpose has been seriously questioned,

¹ Mervyn King, "Reform of the International Monetary Fund," Speech at the Indian Council for Research on International Economic Relations," New Delhi, India, 20 February 2006, 3.

and has adapted to new international economic circumstances. When the IMF was created at the 1944 Bretton Woods conference, it was meant to be at the centre of global financial governance and yet it was almost immediately sidelined by US officials. After the late 1950s, the IMF began to assume a more important position in international financial affairs, but this was short-lived as the Bretton Woods exchange rate regime system broke down in the early 1970s and the IMF's rationale became less clear. After the outbreak of the international debt crisis in the early 1980s, the IMF re-emerged once again with a renewed mandate that placed it back at the centre of international financial crisis management vis-à-vis developing countries. The IMF held its influential role in the international financial system throughout the 1990s, playing a lead role in advising post-communist states in their transition to capitalist economies. The IMF at the dawn of the new century, however, is facing yet another crisis of legitimacy and purpose.

3. Declining Demand for IMF Loans

Why today is the IMF once again facing questions about its future? One reason is that the use of Fund loans has been rapidly declining. While the IMF still has loans outstanding to dozens of low-income countries, three of its four largest borrowers - Argentina, Brazil, and Indonesia - recently announced that they will repay their loans early and will not renew their borrowing from the Fund. Many countries in East Asia have also indicated their disinterest in using Fund financial assistance and have been accumulating large reserves of foreign exchange to protect their countries from future currency crises. In total, the IMF's outstanding lending had declined from \$107 billion at the end of 2003 to \$35 billion by mid-2006.²

² John Snow, "Testimony of Treasury Secretary John W. Snow before the House Financial Services Committee on the International Financial System and the Global Economy," US Congress, 17 May 2006.

As the use of Fund loans declines, the IMF faces more than a loss of influence, utility, and legitimacy. The Fund's financial balance sheet is adversely affected because its organizational costs are financed by the interest and fees charged on its loans. The early loan repayments have already triggered budgetary shortfalls for the institution. The IMF's financial woes were highlighted in May 2006, when Managing Director Rogrigo de Rato appointed an expert group to advise him on how to develop alternative sources of income.

The declining use of IMF loans is partly explained by the absence of large-scale financial crises in the last few years as well as the increased availability of funding from private international financial markets for middle-income 'emerging market' countries. Private capital inflows to developing countries in 2005, for example, totalled \$491 billion, a figure that dwarfed IMF lending.³ In a sense we are returning to a situation similar to the 1970s, when the IMF's lending was increasingly being marginalized by developing countries that had access to abundant private international lending.

But the turn away from the IMF by many borrowing countries may not simply be a temporary, cyclical phenomenon that will be reversed when private funding dries up or balance of payments crises are experienced again. Instead, and more ominously for the Fund, it appears to be more of a long-term, secular trend that is linked to the declining legitimacy of IMF advice and governance. The institution's advice has never met universal approval, but opposition grew particularly intense after the 1997-1998 East Asian financial crisis. Many across the East Asian region and elsewhere blamed the Fund for worsening the financial crisis.

In the East Asian region, an important rationale for the accumulation of foreign exchange reserves is the desire to lessen

³ World Bank, *Global Development Finance* (Washington: World Bank, 2006).

any future dependence on the IMF. This sentiment has also led East Asian countries to explore the creation of regional mechanisms for balance of payments financing. The Japanese government at the height of the East Asian crisis famously put forward the first substantial proposal of this kind. Its proposed Asian Monetary Fund would have offered an alternative source of funding to East Asian governments that would not be accompanied by the same kinds of intrusive, heavy-handed loan conditionality that the IMF was imposing at the time. The proposed regional mechanism, however, was shot down by strong opposition from the United States and received wary reaction from some governments in the region, such as China, who worried about the Japanese government's intentions.⁴

Since the failed Asian Monetary Fund initiative, East Asian governments have been incrementally working in the same direction to create a set of regional swap arrangements among monetary authorities. This started under the Chiang Mai Initiative of 2000. As initially implemented, the swaps posed little challenge to the IMF's role in the region; governments requesting more than 10 per cent of the funds available had to have IMF programs in place. But as the figure was raised to 20 per cent in 2005 and if further changes of this kind were to be made, the Chiang Mai Initiative would indeed work towards diminishing the IMF's role in the region. Similarly, the Asian Development Bank is also beginning to take on new roles that the IMF traditionally performed such as surveillance functions.

Growing dissatisfaction with IMF advice also helps to explain declining use of IMF loans in Latin America. The IMF's intellectual standing in that region was undermined by the Argentine economic

⁴ Yong Wook Lee, "Japan and the Asian Monetary Fund," *International Studies Quarterly*, vol. 50, no. 2 (June 2006): 339-66.

collapse of late 2001. Argentina was widely seen as one of the IMF's 'star pupils' in the region throughout the 1990s. Its sudden economic crisis became seen by many - rightly or wrongly - as evidence of the failure of IMF's ideas and its ability to warn and predict of looming crises. Policymakers in many of the left-of-centre governments that have come to power across Latin America in the last few years have also been critical of the IMF's advocacy of the 'Washington Consensus.'

Argentina's subsequent negotiations with the IMF under the Kirchner administration also undermined the Fund's powerful image. Using the Fund's large financial exposure to the country as a source of leverage, the Argentine government succeeded in extracting further funding with loose conditions and in segmenting its private creditors to its advantage.⁵ The near simultaneous announcements by Argentina and Brazil of early repayments of all IMF loans in early 2006 was also widely portrayed across the region as a kind of boycott of, or declaration of independence from, the Fund.

Some Latin American governments, like those in East Asia, have been proposing regional financial facilities that could replace the IMF's role. The most enthusiastic advocates of these regional proposals are usually the most critical of the IMF, its advice, and the Washington consensus. Unsurprisingly, Venezuelan President Hugo Chavez has suggested the most ambitious of proposals: the creation of a Banco Del Sur that could exclusively serve Southern countries and bypass the IMF entirely.

⁵ Eric Helleiner, "The Strange Story of Bush and the Argentine Debt Crisis," *Third World Quarterly*, vol. 26, no. 6 (September 2005): 951-69; and, Andrew F. Cooper and Bessma Momani, "Negotiating Out of Argentina's Financial Crisis: Segmenting the International Creditors," *New Political Economy*, vol. 10, no. 3 (September 2005): 304-20.

Discontent with the IMF in borrowing countries has not been restricted to Latin America and East Asia. It has also been strong in other regions, particularly in sub-Saharan Africa where the IMF's intrusive conditionality and the 'neo-liberal' nature of IMF policy advice have attracted many critics. But facing large debts and without the access to capital markets available to their Latin American and East Asian counterparts, most sub-Saharan African governments have found it more difficult to cut their financial dependence on the IMF. Without the tool of 'exit', sub-Saharan African governments have been restricted to using 'voice'. And their voice has attracted much less attention in debates about the future of the IMF, not least because of the nature of the IMF governance structures, as discussed below, which restricts the influence of these smallest quota holders.

In short, the decline of Fund legitimacy in the eyes of potential IMF borrowers has been a precipitating factor behind the declining demand for IMF loans. One of the key reasons why IMF reforms are being demanded today is that potential borrowers have demonstrated or voiced their dissatisfaction with the IMF. Reforming the IMF to restore its legitimacy, some believe, is a way of returning Fund borrowers and reasserting the Fund's place in global financial governance.

4. Criticism from the United States

The IMF faces calls to reform today not just because many potential borrowers are turning away from it. The Fund also faces prominent criticism from within many of the countries that act as creditors to the institution. Criticism has come from Northern 'civil society' groups who, often in alliance with their Southern counterparts, have focused much of their attention on the social, political and environmental costs of IMF lending programs in debtor countries. The fact that the Fund in recent years has felt

compelled to engage more systematically with Northern and Southern NGOs is clear evidence of these groups' growing influence. While these critical voices have contributed to the legitimacy crisis facing the Fund today, their actual impact in changing IMF policies and behavior is the subject of considerable scholarly debate.

What is clearer to judge is the impact of recent criticism from the IMF's chief creditor: the United States. Throughout the 1990s, the Clinton administration supported IMF efforts to address financial crises with large-scale rescue packages, beginning with the 1994 Mexican crisis through to the 1997-98 East Asian crisis. In contrast, the Bush administration has taken a different view and course, as many of its leading officials have sought to constrain the Fund's role.

Some of the increasing American scepticism towards the IMF has come from US policymakers of a free-market persuasion. During the second half of the 1990s, many such policymakers became very critical of IMF bailout lending, arguing that these large-scale rescue packages were distorting proper market signals and encouraging reckless lending by international investors. To address this 'moral hazard' problem, Fund critics felt it was necessary to scale back - or even end altogether - the practice of international bailouts. This shift in dealing with financial crises, Fund critics argued, would not only change market expectations but also 'bail in' foreign private creditors by forcing them to accept sovereign defaults and debt restructuring at the outset of crises.

Even before the Bush administration assumed office, these arguments for a new approach to sovereign debt crises had prompted the IMF to push more actively for 'private sector involvement' during South Korea's financial crisis in 1998 and subsequent crises in Ecuador, Pakistan, and Ukraine through 1999-

2000.⁶ Nevertheless, it was the election of George W. Bush that substantially boosted the new 'bail-in' approach. Key officials in the Bush administration were convinced of the "moral hazard" critique of IMF bailouts, including then Treasury Secretary Paul O'Neill and his undersecretary for international affairs John Taylor.⁷

Opposition to large-scale IMF bailouts was similarly coming from US Congress. This opposition had been apparent as far back as the 1994-5 Mexican crisis and it grew during the 1997-98 East Asian crisis when the Clinton administration asked Congress to approve an \$18 billion increase in IMF funding. At the time, the IMF's resources had been severely depleted by a number of large-scale bailouts. The Clinton proposal to increase US funding passed the Senate, but it was much less popular with many House Republicans. Some Republicans were influenced by the moral hazard critique of IMF bailout packages, while others were driven by a more general distrust of multilateral institutions and a desire to save US taxpayers' money. In the end, the US funding proposal passed, but subject to certain provisions that notably included the establishment of a Congressional commission to review US policy towards the IMF and other international financial institutions. The resulting 'Meltzer Commission' published its report in March 2000 and recommended a dramatic scaling back of the activities of the IMF.⁸ Many of the Meltzer Commission's recommendations have continued to be supported by a number of Congressional Republicans since then.

⁶ Paul Blustein, *The Chastening: Inside the Crisis that Rocked the Global Financial System and Humbled the IMF* (New York: PublicAffairs, 2001), chs.7, 9.

⁷ Ron Suskind, *The Price of Loyalty: George W. Bush, the White House, and the Education of Paul O'Neill* (New York: Simon and Schuster, 2004), 173, 175, 243-44.

⁸ International Financial Institutions Advisory Committee (IFIAC), *Report of the International Financial Institutions Advisory Committee*, Submitted to the US Congress and US Department of Treasury, 8 March 2000.

The views of Bush administration officials and members of US Congress have contributed to the recent diminution of the IMF's global role and influence. In their first months in office, Bush administration officials publicly signalled their intention not to bail investors out of future sovereign debt crises. In late 2001, they found an opportunity - in the context of Argentina's dramatic financial crisis - to translate their words into action (or more accurately, inaction). After initially backing an IMF loan to Argentina in August 2001, the US administration was much less supportive of further IMF assistance when Argentina failed to meet IMF targets. When Argentina then defaulted on its loans - marking the largest sovereign default in world history - the United States also did not press for further IMF intervention, and they defended their approach on the grounds of stopping moral hazard. During the subsequent lengthy negotiations to restructure Argentina's massive debts in 2002-05, Bush administration officials also appeared to undermine the IMF's bargaining power at some key moments - much to the consternation of some other creditor governments.⁹

Throughout the Bush administration's tenure, political support for new IMF funding has also been less forthcoming.¹⁰ American policymakers have also opposed the expansion of the IMF's mandate at some critical instances. Perhaps the most important such moment was the debate about the creation of a Sovereign Debt Restructuring Mechanism (SDRM) between 2001 and 2003. The Argentine crisis highlighted that there would be more defaults by sovereign debtors if the IMF was to refrain from large-scale bailout lending. To make debt restructuring more orderly, the IMF's Deputy Managing Director Anne Krueger suggested in

⁹ Helleiner, "The Strange Story of Bush."

¹⁰ Eric Helleiner and Geoffrey Cameron, "Another World Order? The Bush Administration and HIPC Debt Cancellation," *New Political Economy*, vol. 11, no. 1 (March 2006): 125-40.

November 2001 a IMF-linked SDRM to legitimize sovereign debt defaults and prompt private foreign creditors to join debt-restructuring negotiations. Krueger felt that the post-bailout world left a "gaping hole" in the international financial architecture that the IMF should fill.¹¹

Krueger's proposal generated enormous attention and it had the tentative support of Paul O'Neill, as well as that of officials in Canada, Britain and a number of other European countries. The SDRM proposal, however, also encountered powerful critics from within the international investor community (who preferred a more market-oriented approach) as well as from some emerging market countries (most notably Mexico and Brazil). Important criticism also came from US officials such as Taylor and prominent Republican members of Congress. One source of opposition within some US policymaking circles was the belief that the SDRM would reinforce the power of the IMF. As Congressman Jim Saxton put it, Krueger's proposal represented another example of IMF 'mission creep' and it "would have the effect of compensating the IMF for the reduction in its influence arising from a more restricted policy towards international bailouts."¹²

When O'Neill left as Treasury Secretary in December 2002, Krueger lost a key supporter and the SDRM proposal was taken off the table at the IMF's April 2003 steering group meeting of the International Monetary and Financial Committee. If the SDRM had succeeded, it would have left more at the centre of the governance of sovereign debt crises in the post-bailout age. However,

¹¹ See Anne Krueger, *International financial architecture for 2002: A new approach to sovereign debt restructuring* (Washington, DC: International Monetary Fund, 2001), 1.

¹² James Saxton, "IMF Sovereign bankruptcy supervision is unnecessary: New analysis rejects more IMF mission creep," Press Release, Joint Economic Committee, US Congress, 19 April 2002.

as discussed below, the failure of the initiative represented an important turning point for the Fund: the Fund was being assigned a more marginal role in the governance of international financial crises.

5. What Kind of Reforms?

With critics in many parts of the world and a shrinking set of borrowers, what is the IMF's future in global governance? A few opponents of the Fund - on both the left and right of the political spectrum - would like to see it abolished, and they see its current vulnerability as a political opportunity to push for this outcome. But international organizations rarely die. Reform is the more common fate, and the IMF has certainly experienced its share of transformations during its 60-year history. What are the most politically prominent proposals for reform today? In what direction could these proposed reforms take the Fund?

Governance Reforms: The Quest to Re-establish Legitimacy

Among those advocating IMF reform today, there is near universal agreement that an overhaul of Fund governance must be a top priority. This focus reflects the widespread sentiment that the Fund is facing a serious crisis of legitimacy that can only be addressed by creating governance structures that are more open to the voices of those disaffected with the institution and more reflective of changing political and economic realities.

Chairs and Shares. Perhaps the highest issue found on the agenda of those advocating IMF governance reform is the realllocation of quotas (and thus votes) as well as the composition of chairs at the IMF Executive Board. There have been a number of moments in the IMF's history when such a change in the allocation of quotas and chairs has taken place to reflect changing

political and economic realities. At the founding of the IMF, for example, the US quota share was more than 30 per cent of the total votes; today, it is 17 per cent after numerous adjustments over time. Similarly, the Executive Board started with only 12 Executive Directors (EDs), with the five largest contributors being assigned a single seat and other members being represented by constituency groups. Today, the number of EDs has risen to 24 and, in addition to the five largest contributors, single-country constituencies have been created for Saudi Arabia, China, and Russia.

It is worth highlighting that these changes can reflect political bargains and not just technical economic arguments. In the current debate, considerable attention has been devoted to various economic calculations when making arguments for changes to specific countries' relative positions. This attention is understandable, but its importance should not be overstated. Historically at the Fund, economic calculations were sometimes used only after the fact to *justify* decisions already made on political grounds for countries' relative quota positioning and for ED seat allocation.¹³

Given the legitimacy crisis facing the Fund, the political circumstances would seem ripe for a major reallocation of 'chairs and shares' to take place. Indeed, de Rato has effectively highlighted the importance of seat reallocations by backing a two-stage process to address governance reform. First, at the September 2006 annual meeting in Singapore, Fund members endorsed ad hoc quota increases of at least four countries whose existing shares were particularly out of line with their growing economic significance: China, South Korea, Mexico, and Turkey. The agenda and timeline for the second stage has been left more open-ended and to be decided throughout 2007.

¹³ Bessma Momani, "Another Seat at the IMF Table: Russia's IMF Executive Director," Paper presented at the Canadian Political Science Association Meeting, York University, Toronto, 3 June 2006.

There are loud calls from Asian governments for a more systematic redistribution of quotas and Executive Board seats in order to boost their region's share. The economic case for this reform is clear: under-representation of Asian economies in the IMF has been well documented.¹⁴ The political case is equally compelling since it is the Asian countries whose drift away from the institution poses one of the most serious threats for the Fund at the moment. Importantly, US policymakers have backed the call for an increase in Asian voting weight, although they have also called for a rationalization of overall Executive Board representation.¹⁵

Supporters of developing countries have also argued for enhancing low-income country votes and voice at the Executive Board. Peter Evans and Martha Finnemore note that the combined vote of all of the 80 low-income countries that qualify for the Fund's Poverty and Growth Reduction Facility is roughly 10 per cent, while G10 industrialized countries have 52 per cent.¹⁶ Democratizing the IMF, some argue, requires the board to better reflect the Fund's main clients and frequent users: borrowing, low-income countries.¹⁷ Former Executive Director Cyrus Rustomjee,

¹⁴ See David Rapkin and Jonathan Strand, "Is East Asia under-represented in the International Monetary Fund?" *International Relations of the Asia-Pacific*, vol. 3, no. 1 (February 2003): 1-28.

¹⁵ Snow, "Testimony of Treasury Secretary."

¹⁶ Peter Evans and Martha Finnemore, "Organizational Reform and the Expansion of the South's Voice at the Fund," *G-24 Discussion Paper*, no.15 (Geneva: UNCTAD, 2001).

¹⁷ Kelkar et al. argue that restoring basic votes will help enhance developing countries' perceived legitimacy of the Fund. Vijay Kelkar et al., "Time for a change at the IMF," *Finance and Development*, Washington, DC: International Monetary Fund, March 2005; For a cautionary note on the limits of this democratization argument, Birdsall who argues that many LICs are not developed democracies and their presence at the Executive Board may not be representative of the many disenfranchised citizens in those countries. Nancy Birdsall, "Why it matters Who Runs the IMF and the World Bank," *Working Paper Number*, no. 22, (Centre for Global Development, January 2003); Similarly, Kahler adds that the IMF should not be compared to national parliaments, but treated as a 'delegated authority' and compared to judiciaries or central banks. Miles Kahler, *Leadership Selection in the Major Multilaterals* (Washington, DC: Institute for International Economics, 2002), 266.

who represented the Sub-Saharan constituency, also suggests that enhancing developing members' voice in IMF decision-making will translate into better suited IMF loan conditionality that emphasizes long term economic growth.¹⁸ Critics of the Washington Consensus add that more developing countries on the board will allow countries to better resist 'pressure to liberalize' and to press for more staff recruitment from developing countries.¹⁹

In formulating ways to enhance developing countries' influence at the Executive Board, former Executive Director and head of the Group of 24 Ariel Buiira suggests developing a new quota formula that uses purchasing power parity (instead of market exchange rates) and population as factors adjusting GDP (Michel Camdessus also thinks population deserves more weight).²⁰ This would not, however, change representation of less populous and relatively poor countries in Sub-Saharan Africa. To give them more votes, it will be necessary to restore the importance of 'basic votes'. As an equalizing measure, all members of the IMF were allocated 250 votes at the time of the founding of the institution. But these votes have not been changed since and their significance has diminished over the years from their original level of 11 per cent of total votes to approximately 2 per cent today because of the entrance of new members and quota increases.²¹ Managing Director de Rato has responded positively to the idea of increasing basic votes. African policymakers are also pressing for the creation

¹⁸ Cyrus Rustomjee, "Why Developing Countries Need a Stronger Voice," *Finance and Development*, vol. 41, no. 3 (September 2004): 21-3.

¹⁹ See Birdsall, "Why it Matters," 12.

²⁰ Michel Camdessus, "International Financial Institutions: Dealing with New Global Challenges," Speech to The Per Jacobsson Foundation, Washington, DC, 25 September 2005.

²¹ Ariel Buiira, "A New Voting Structure for the IMF" (Washington, DC: Group of 24, 2002); Ariel Buiira, "The Governance of the International Monetary Fund" (Washington, DC: Group of 24, 2003).

of an additional third seat on the Board because of the heavy workload for the existing two Executive Directors.²²

Any effort to assign emerging market countries and LICs more votes and Executive Board seats will involve a reduced relative share for other countries. Past history suggests that this kind of reform will be politically very difficult. Throughout the 1970s and 1980s, the efforts of Japanese policymakers to increase substantially their quota share met with considerable resistance from the existing powers who would lose relative voting shares.²³ The prospect of a major shift today would seem on the surface to be even dimmer because an overall increase in IMF quotas seems unlikely. In the past, the reallocation of voting shares usually took place in the context of quota increases; that is, countries have not seen their absolute quota reduced but rather simply their relative share.

Still, many argue that the push for closer European integration provides a unique window of opportunity to push for substantial change. Those who are calling for a reform of the 'chairs and shares' tend to agree that the IMF board is overrepresented by European chairs. Indeed, members of the European Union appoint or play a major role in selecting 10 of the 24 executive directors. This distribution of seats in favour of Europe may have reflected relative economic and political weight in the early years of the Fund's history, but today there is a clear economic shift away from Europe to emerging market economies that puts Europe's pre-eminence at the board into doubt. The merging and consolidation of the European Union and the European adoption of a common

²² Rodrigo de Rato, "The Managing Director's Report on Implementing the Fund's Medium-Term Strategy" (Washington, DC: International Monetary Fund, 5 April 2006), 196.

²³ Yoshiko Kojima, "Burden-sharing Under US Leadership: The Case of Quota Increases of the IMF since the 1970s," in H. Bienen, ed., *Power, Economics and Security* (Boulder, CO: Westview, 1992).

currency both further support calls for a more consolidated European representation. A relatively straightforward method of consolidation has been proposed by Edwin Truman who suggests that countries that are not members of the European Union should not be members of EU-led constituencies while Ireland, Spain and Poland should join EU-led constituencies.²⁴ This change would reduce the number of EU or potential EU executive directors by three or four. A more radical proposal would be to consolidate the members of the European Union or perhaps just the euro zone into one seat.²⁵

Some US policymakers have openly highlighted how this latter option would provide a means of increasing the numbers of seats to other regions.²⁶ There is also support in Europe for the idea. Lorenzo Bini Smaghi, of the European Central Bank, argues that consolidating the chairs of euro area countries into one effective seat would actually enhance EU voting, power, and voice at the Executive Board.²⁷ Former German Executive Director Fritz Fischer added that a consolidated EU seat would even help in efforts to harmonize European foreign policy and should be actively pursued.²⁸ Moreover, consolidating EU seats has been endorsed by the European Parliament which has most recently called on members to "work towards a single voting constituency".²⁹

²⁴ Edwin Truman, ed., *A Strategy for IMF Reform*, Policy Analyses in International Economics, no. 77 (Washington, DC: Institute for International Economics, February 2006).

²⁵ Camdessus, "International Financial Institutions"; Lorenzo Bini Smaghi, "IMF Governance and the Political Economy of a Consolidated EU Seat," in Edwin M. Truman, *Reforming the IMF for the 21st Century*, Special Report (Washington, DC: Institute for International Economics, April 2006).

²⁶ See Tim Adams comments in *IMF Survey* 2006, 105.

²⁷ Bini Smaghi, "IMF Governance and the Political Economy."

²⁸ Fritz Fischer, "Why Europe Should Spearhead IMF and World Bank Reform," *Europe's World* (Spring), 42-9; for a critique see Marek Dabrowski, "Consolidating EU votes would be more symbolic than real," *Europe's World* (Spring): 43-47.

²⁹ European Parliament, Resolution on the Strategic Review of the International Monetary Fund, European Parliament, Strasbourg, 14 March 2006, 4.

There is of course some European resistance to these proposals. Some outside Europe have also been worried that a reduction in European influence might undermine the region's commitment to the institution. But it is worth highlighting that the opposite could also be a result. If the European Union consolidated its vote under the existing quota distribution, its quota would be the largest in the Fund, a fact that might give it new influence and interest in the institution.

To ease European resistance, it may be worth considering changes to the IMF decision-making rules. The Executive Board, using a simple majority, decides most day-to-day issues, but special majorities are required for a number of important changes to governing issues. During the mid-1970s, when the US was being pressed to reduce its share below 20 per cent in favour of allocating more votes to Japan and Germany, raising the threshold required for qualified majority votes from 80 to 85 per cent helped soften US resistance. Today, a similar change - or an alteration of the kinds of issues required for qualified majority voting - might help to address European concerns. It might also help increase the voice of poorer countries.³⁰

Beyond Chairs and Shares. Despite the attention given to 'chairs and shares', their importance should not be overstated. The Board, after all, rarely takes votes and usually operates on a 'consensus' basis. Insiders also report that the Board's chair, the Managing Director, often plays a dominant role in Executive Board discussions. The kinds of changes to chairs and shares that are likely to find enough support are also likely to be rather limited.³¹

³⁰ See Ngaire Woods, *The Globalizers* (Ithaca: Cornell University Press, 2006), 210.

³¹ As Mervyn King has put it, a comprehensive deal rearranging chairs and shares "will be extremely difficult to reach". King, "Reform of the International Monetary Fund," 14.

In this context, some analysts suggest that other governance reforms may in fact be more significant in enhancing the legitimacy of the Fund.³² A number of these alternatives also have the benefit of being easier to implement politically.

One of the most important ways to enhance the Fund's legitimacy would be to modernize its procedure of selecting the Managing Director. This procedure remains trapped in a time warp of the 1940s; since the creation of the Fund, the European members and the United States have conspired to allow Europe to nominate the head of the IMF while the United States nominates the president of the World Bank. This process has remained unchanged, even as other international institutions have developed more transparent, merit-based and inclusive mechanisms for selecting their heads. Fund reformers call for changing the selection process to include candidates selected on merit and elections, without citizenship restrictions.³³ Former Managing Director Michel Camdessus in a recent lecture also called on the United States and Europe to forgo their 'privileges' in choosing Fund leadership; instead, Camdessus suggested opening the leadership selection process to allow a competitive process. He argued this would help enhance organizational and external legitimacy.³⁴

Kahler cautions against an overly transparent and competitive process that could lead to a deadlock as the case of selecting the head of the World Trade Organization demonstrated. Instead, Kahler recommends 'a process of restrained competition' where 1) minimum qualifications are agreed upon, 2) search committees

³² Peter Kenen, "Comments on the Address of the Managing Director of the IMF," Remarks made at the book release meeting, *Reforming the IMF for the 21st Century*, Institute for International Economics, Washington, DC, 20 April 2006.

³³ Jonathan Ostry and Jeromin Zettelmeyer, "Strengthening IMF Crisis Prevention," *IMF Working Paper* (Washington, DC: International Monetary Fund, 2005), 17.

³⁴ Camdessus, "International Financial Institutions," 11.

establish a qualified long-list of possible candidates, and 3) national governments narrow down the long-list to a veto-proof nomination short-list.³⁵ There are strong normative arguments made in favour of democratizing the process, but clearly the hesitation of US and European political capitals to forgo their 'privileges' remains. To initiate this change, Kahler suggests that members who want to change the status quo "withhold their support" for a candidate selected by the Western Europeans and the Americans in the next search for a Managing Director unless the process of competition and meritocracy is used.³⁶

Another set of important reform proposals concern the functioning of the Executive Board. Woods and Lombardi argue that reallocating Executive Board chairs may not be necessary if improvements could be made to the constituency system which pools votes and shares into one elected Executive Director. They observe that constituency members who do not hold a chair at the Executive Board are underrepresented with less voice and voting power in the organization, because chairs do not cast split votes and often reflect the wills of the EDs' own capitals.³⁷ This leaves the majority of IMF members represented within constituencies with ineffective means of getting heard on the board. Woods and Lombardi recommend enhancing the capabilities of chairs and improving chair accountability to its constituency members.

A number of proposals have also been made to enhance the ability of the Executive Board to provide the kind of strategic, political direction to the Fund that might enhance the institution's

³⁵ Kahler, *Leadership Selection*, 92-98.

³⁶ Miles Kahler, "Internal Governance and IMF Performance," in Truman, *Reforming the IMF*, 265.

³⁷ Ngaire Woods and Domenico Lombardi, "Uneven Patterns of Governance: How Developing Countries are Represented in the IMF," *Review of International Political Economy*, vol. 13, no. 3 (August 2006): 480-515.

legitimacy among its member country governments. As Mervyn King has highlighted, executive directors are currently engaged primarily in very time-consuming micro-management of the Fund's activities.³⁸ The Board meets several times a week and the directors are left swimming in a mass of detailed paperwork; in 2004 alone, they were given 70,000 pages of material to absorb and they generated another 10,000 pages themselves. The directors also do not always have the kind of political weight within their respective countries that allows them to go much beyond repeating their official government positions on various issues. Indeed, they are not even fully accountable to national governments in the way that an Ambassador is and it is the Fund that pays their salaries.³⁹

In King's view (as well as that of David Dodge), the Fund would be better served by a non-resident Board (as Keynes had initially suggested) that would meet infrequently - perhaps 6-8 times per year - and which could be made up of more senior officials from member governments.⁴⁰ This reform would enable the Board to assert its authority more decisively on big picture issues in ways that ensured that the Fund's strategic direction better reflected the preferences of its member governments.

A non-resident board would of course provide the Fund's Managing Director and staff with greater independence in their day-to-day operations. This enhanced staff independence could affect perceived IMF's legitimacy in a couple of ways. On one hand, freed of direct political oversight of day-to-day affairs, the IMF staff's ability to offer more dispassionate advice on key issues facing member governments, and the world economy as

³⁸ King, "Reform of the International Monetary Fund."

³⁹ Woods, *The Globalizers*, 192; Bessma Momani, "American Politicization of the International Monetary Fund" *Review of International Political Economy*, vol. 11, no. 5 (December 2004): 880-904.

⁴⁰ See also Kelkar et al., "Time for a change at the IMF."

a whole, could be improved. This might bolster the credibility and authority of its 'surveillance' role (Fund staff would be less apt to 'clientism') and of its role in prescribing conditionality (Fund staff could resist the kind of micro-managing of conditionality by the United States that appeared to take place during the Asian crisis). On the other hand, without the day-to-day watchful eye of the Executive Board, Fund staff might prescribe more intrusive conditionality, taking less political-economy considerations into account when devising loan programs. In this vein, the Executive Board ensures that IMF staff do not prescribe conditionality that is deemed politically damaging to member states.⁴¹ A more technocratic-based IMF might decrease perceived IMF legitimacy if borrowing member states are pressured to accept more intrusive and politically impractical conditionality.⁴²

A more ambitious proposal with the similar goal of devising a more independent Executive Board has come from Michel Camdessus. Instead of altering the mandate of the Executive Board in King's way, Camdessus calls for the creation of a new IMF 'Council' that could assume the responsibility for strategic decision-making and meet perhaps four times per year. As he notes, the creation of such a council was in fact endorsed at the time of the 1976 Jamaica amendment of the IMF Articles of Agreement. Camdessus suggests that the Council - whose membership he left unspecified - could replace the International Monetary and Financial Committee which is presently only advisory and has become more of a communiqué-writing body than a creative decision-making forum. Under Camdessus' proposal, the existing Executive Board would remain in place but would focus on

⁴¹ See Momani, "American Politicization of the International Monetary Fund."

⁴² King acknowledges that this reform would have to be accompanied by mechanisms to keep the Managing Director and staff accountable, and he suggests that Independent Evaluation Office could help in this task.

more technical issues in ways that helped to keep the management accountable. Peter Kenen has gone even further to suggest that the Executive Board could be transformed into a 16 member Managing Board of experts not representing governments but rather nominated by the Managing Director (with consideration given to the differing interests of the members) and working without weighted voting.⁴³

One further proposal to increase the legitimacy of the Fund among developing countries is to reform the recruitment, training and deployment of its staff. Evans and Finnemore argue that reforms in this area could play a major role in enhancing the voice of developing countries within the Fund as well as enhancing their sense of ownership of the institution. They suggest a range of reforms including allocating more support staff to developing country executive directors and drawing more on people with 'hands-on' knowledge of concrete circumstances in developing countries.⁴⁴ Others have also been particularly critical of the IMF's narrow base of recruitment.⁴⁵ Michel Camdessus has discussed the staff's "cloning syndrome" and argued that the Fund would "benefit greatly in selecting for their dialogues with officials facing the complexities of political life, staff members with national experience, or a broader culture in social studies than the one that is generally required for their recruitment".⁴⁶

One noteworthy feature of the debate on reforming IMF governance within the last year or two has been the relative absence of proposals seeking to involve 'civil society' groups more formally in IMF decision-making. Proposals of this kind were

⁴³ Kenen, "Comments on the Address of the Managing Director of the IMF."

⁴⁴ Evans and Finnemore, "Organizational Reform and Expansion."

⁴⁵ See Bessma Momani, "Recruiting and Diversifying IMF Technocrats," *Global Society*, vol. 19, no. 2 (April 2005): 167-87.

⁴⁶ Camdessus, "International Financial Institutions," 9.

popular in the wake of massive societal protests against the IMF and other international economic institutions during the late 1990s and early 2000s.⁴⁷ To enhance its relations with civil society and the NGO community, the IMF has become more transparent in its publications. This has included releasing more staff reports and Executive Board documents after a 5 and 10 year embargo. Many have argued that this is not enough. For the IMF to be credible and accountable, many suggest that the IMF release Executive Board votes and minutes immediately after conclusion of board meetings. There have also been proposals to establish more formal linkages between the IMF and 'civil society' groups (i.e. the creation of an IMF ombudsman and an IMF-NGO Liaison Committee⁴⁸). At the current political conjuncture, however, the IMF reform debate has shifted to one that is more traditionally state-centric. This shift no doubt reflects the fact that the nature of the challenges to the IMF have shifted: today, attention is being devoted more to the goal of re-establishing the credibility and legitimacy of the Fund in the eyes of those national governments which have been drifting away from the institution.

The IMF's Performance: Refocusing Its Activities

While governance reforms are clearly fundamental to restoring the IMF's global standing, many also argue that reforms to the Fund's performance are important to its future. Particularly prominent have been calls for the IMF to strengthen its surveillance role and to redefine its lending and crisis-management roles.

⁴⁷ See Ben Thirkell-White, "The International Monetary Fund and Civil Society," *New Political Economy*, vol. 9, no. 2 (June 2004): 251-70.; and, Jan Aart Scholte, *Civil Society Voices and the International Monetary Fund* (Ottawa: North South Institute, 2002).

⁴⁸ See Daniel Bradlow, "The Changing Role of the IMF in the Governance of the Global Economy and Its Consequences" (*Mimeo*, 2006).

Refocusing on Surveillance. When the Fund was created in 1944, the IMF's architects hoped the institution could draw attention to the financial needs of the world economy as a whole and discourage countries from returning to the 'beggar-thy-neighbour' economic policies of the 1930s. In the 1970s, the IMF was given a formal mandate to engage in 'surveillance' of member countries' policies.⁴⁹ In the current context, IMF surveillance of financial sector policies, exchange rates, and capital accounts of both systemically important countries and emerging market economies is seen by many as a key Fund function. Indeed, many argue that the surveillance role should now be seen as the central *raison d'être* of the institution.

Fund officials have supplied a number of reform proposals to expand and enhance IMF surveillance. The current Managing Director Rodrigo de Rato has argued for increasing Fund surveillance by targeting the monitoring of systematically important countries and global capital markets' vulnerabilities. To accomplish this, de Rato has merged the International Capital Market Department and the Monetary and Financial Systems Department to create what he calls a "single centre of excellence".⁵⁰ The Fund has recently argued that surveillance is its organization's comparative advantage over financial institutions and domestic governments because it can provide impartial analysis.⁵¹

To improve Fund surveillance, IMF research department's Jonathan Ostry and Jeromin Zettelmeyer have suggested that the IMF remove ambiguous evaluation of member states by openly rating all of its members on their overall performance in

⁴⁹ Louis Pauly, *Who Elected the Bankers?* (Ithaca: Cornell University Press, 1997).

⁵⁰ See *IMF Survey* 2006, 51.

⁵¹ Raghuram Ragan, "The Role of the International Monetary Fund in a Changing World," Speech to the Kiel Institute for World Economics, Kiel, Germany, 10 April 2006.

a publicized 'report card'. This report card would also determine the level of financing a country could receive, as an added measure to preventing crises.⁵² This is further supported by Truman who calls on the IMF to start 'naming and shaming' its members, including systemically powerful countries like the United States.⁵³ To date, Truman argues, the IMF has been soft on member states that did not follow IMF advice in Article IV consultations. This soft approach harms the international economic system while systemically important countries remain insulated from crisis. The Fund, Truman argues, needs to act more like an 'umpire' rather than just an 'adviser' or 'lender'. This would require the Fund to get specific about country wrongs and detail how to correct country errors.⁵⁴ In a March 2006 speech, the Bank of Canada Governor David Dodge reiterated this suggestion, calling for the IMF to become an "independent, impartial umpire, ready to call out countries that break the rules". He recalled Keynes' hope that the Fund would engage in "ruthless truth-telling".⁵⁵

Some have expressed concerns about this kind of umpire role, arguing that it might compromise the Fund's ability to act as trusted advisor to governments. One difficulty is organizational according to Michael Mussa, former head of IMF Research. He notes that the IMF staff act one day as 'social worker', sympathetically prescribing conditionality, and then 'tough cop', enforcing rules of conduct perceived to be for the benefit of the economic community.⁵⁶ Mussa suggests that staff members are

⁵² Jonathan Ostry and Jeromin Zettelmeyer, "Strengthening IMF Crisis Prevention," *IMF Working Paper* (Washington, DC: International Monetary Fund, 2005), 8-9.

⁵³ Truman, *A Strategy for IMF Reform*, 13.

⁵⁴ *Ibid.*, 45.

⁵⁵ David Dodge, "The evolving international monetary order and the need for an evolving IMF," Lecture to the Woodrow Wilson School of Public and International Affairs, Princeton University, Princeton, NJ, 30 March 2006.

⁵⁶ Michael Mussa, *Argentina and the Fund: From Triumph to Tragedy* (Washington, DC: Institute for International Economics, 2002), 67.

under pressure to appease country officials, with whom staff work closely, producing watered-down bilateral surveillance reports. Releasing bilateral Article IV surveillance reports immediately after consultations end provides one way to insulate staff from such pressure.⁵⁷ Both Mussa and Kahler go as far as to suggest some bureaucratic reorganization to separate surveillance work from area departments and thereby remove this tendency for watered-down assessments and chummy IMF-authority relations. Ideally, an independent IMF Surveillance Department would remove IMF staff involved in bilateral surveillance from area departments where loan programs are designed and conditionality prescribed.⁵⁸

Many analysts have devoted particular focus to reinvigorating the Fund's surveillance of exchange rates. Goldstein argues that the IMF needs to return to its traditional role of monitoring exchange rates, and that it has simply not been successful in pressuring countries, particularly China in recent years, to change their policies. He recommends the Fund issue reports on exchange rate policies and shame countries that use manipulative practices.⁵⁹ But the idea of pressing the Fund to focus on monitoring exchange rates has been challenged by Chinese officials who maintain the need for country sovereignty in determining exchange rate policies.⁶⁰

Others point out that apart from macro-level surveillance of world economic trends, like those found in the *World Economic Outlook*, Fund staff concentrate their surveillance on a country by country basis. This has prevented the staff from appreciating countries' policy linkages and their spill-over effects, and perhaps

⁵⁷ Kahler, "Internal Governance and IMF Performance," 267.

⁵⁸ Mussa, *Argentina and the Fund*, 69-70.

⁵⁹ Morris Goldstein, "Currency Manipulation and Enforcing the Rules of the International Monetary System," in Truman, *Reforming the IMF*.

⁶⁰ Zhou Xiaochuan, "IMFC Statement by Zhou Xiaochuan, Governor, People's Bank of China" (Washington, DC: International Monetary Fund, 22 April 2006), 4.

explains why the staff's toolkit in warning of financial contagion remains weak. In response to this criticism, Managing Director de Rato has announced expanding surveillance to include 'multilateral consultations' where systematically important countries will have a forum to discuss and debate specific issues of global economic significance in an effort to thwart unravelling of the world economy.

In June 2006, he announced a first multilateral consultation to focus global imbalances that will involve China, the Euro area, Japan, Saudi Arabia and the United States.⁶¹ Some see this as a way of appeasing the United States in raising the issue of an overvalued Chinese currency, but de Rato has stated that the forum will also be used to tackle many global issues including 'US current account deficits' affect on external indebtedness.⁶² More ambitiously, Camdessus recently argued that the IMF should take an active role to reinvigorate efforts to create a new Plaza or Louvre Accord. The IMF, he argues, is best suited to do this "because there is no other... legitimate, global forum to tackle such a systemic problem".⁶³

Devoting more attention to this kind of multilateral surveillance activity would be a shift in focus for the IMF. Lombardi and Woods note that relatively little of the Executive Board's time has been devoted to multilateral surveillance. But this is a shift that should serve the IMF well.⁶⁴ Since the IMF's birth, many other organizations have been created that engage in surveillance activities - from the OECD to the BIS and the various G-groupings. But the Fund is uniquely well positioned to assume a lead role in this area at the multilateral level because of its more universal membership.

⁶¹ See, *IMF Survey* 2006, 179.

⁶² See de Rato, "How the IMF Can Help Promote."

⁶³ Camdessus, *International Financial Institutions*, 4.

⁶⁴ Domenico Lombardi and Ngaire Woods, "The Political Economy of IMF Surveillance," *CIGI Working Paper*, no. 17 (February 2007).

It is important, however, not to overstate the influence of IMF surveillance activities. Even in the bilateral context, the Fund's advice has often had significant impact only when backed up by the promise of loans. Without the financial carrot, and in an era when the quality of its advice is being questioned, an IMF focused more on surveillance activities may be an IMF with an increasingly marginal position in the world economy. To avoid this fate, the IMF must ensure that its advice is credible and useful to policymakers. This, in turn, may depend heavily on a successful implementation of some of the kinds of governance reforms outlined above.

The IMF's Lending and Crisis-Management Role. And what of the IMF's lending role? Many have suggested that crisis lending is unlikely to be the main focus of the IMF's activities in the coming years because countries are finding alternate ways to insulate themselves from crises.⁶⁵ It is worth remembering, however, that some of the declining demand for IMF crisis-lending has been linked to the broader question of the IMF's legitimacy. Once again, if the kinds of governance reforms outlined above succeeded in restoring confidence in the institution, then this trend could be reversed.

Even if there was new demand for IMF financing, other analysts question whether IMF support could have much of an impact in stemming crises because of the size of international capital flows today. To be effective in this task, IMF loans would need either to be very large or to act in a catalytic role vis-à-vis enormous private capital flows. But, larger loans have become increasingly unlikely in the wake of the political backlash in creditor countries against the large-scale bailouts of the 1990s.

⁶⁵ See King, "Reform of the International Monetary Fund."; and, Dodge, "The evolving international monetary order."

Moreover, evidence suggests that the IMF's lending does not generally play a positive catalytic role in generating private capital inflows.⁶⁶

This need not imply, however, that IMF lending has no role to play in future financial crises. Tom Willett argues that an international lender of last resort (ILLR) is needed because financial markets can be inefficient, but an ILLR should not be used to protect pegged currencies under intense speculative attack. To make this work, however, Willett suggests the Fund add facilities that offer front-loaded financing on a short-term basis while demanding members meet loan preconditions.⁶⁷ De Rato has also clearly endorsed the IMF's role of providing crisis-lending, and has called for a new type of arrangement to be developed to provide contingent financing for crisis prevention. He has also suggested that the IMF devote more attention to its policy on lending into arrears during debt restructuring episodes.⁶⁸

In addition, de Rato has made the important suggestion that the IMF should be more open to supporting member governments' reserve pooling arrangements at the regional level, while signalling out the need for the IMF to support *existing* arrangements such as the Chiang Mai Initiative. This support for pooling arrangements, he suggests, could come primarily through the Fund's surveillance

⁶⁶ Graham Bird and Dane Rowlands, "The catalytic effect of lending on the international financial institutions," *World Economy*, vol. 20, no. 7 (November 1997): 967-91; Martin Edwards, "Signaling Credibility? The IMF and Catalytic Finance," *Journal of International Relations and Development*, vol. 9, no. 1 (March 2006): 27-52.

⁶⁷ Thomas Willett, "A Likely Political Unrealistic Proposal to Make the IMF and Effective ILOLR and Increase the Effectiveness of Conditionality," Discussion points presented to a workshop on *Reform of Global Financial Governance: Whither the IMF?*, The Centre for International Governance Innovation, Waterloo, 10 June 2006.

⁶⁸ Rodrigo de Rato, "The Managing Director's Report on Implementing the Fund's Medium-Term Strategy" (Washington, DC: International Monetary Fund, 5 April 2006).

role: "While it would be up to these groups to determine terms for access, the scope for expanding such [regional] safety nets would rise with a group's confidence in the economic policies of its members. The Fund can play a role, focusing on regular and intensive surveillance. It should explore modalities for further engagement in this area."⁶⁹

De Rato's suggestion for pooling arrangements marks an important openness on the part of the Fund to working with, rather than resisting, recent calls for a more decentralized international monetary and financial system - a system where regional monetary funds would be first invoked and used in times of crisis. Regional organizations, it has been argued by some, can better represent their clients than the likes of the IMF which tend to reflect the interests of its key shareholders. Regional institutions could provide needed funds with less conditionality and more peer pressure, while fostering greater policy ownership that could be further used to achieve long-term development goals.⁷⁰ Proponents of the idea argue that regional funds would produce a competitive environment for both economic policy ideas and funds that could benefit emerging market economies, but others caution that regional funds would be more susceptible to political considerations and therefore moral hazards.⁷¹

More generally, Tony Porter also points out that the decentralization of global monetary and financial institutions is in keeping with similar devolution of global governance. Porter suggests that this contemporary devolution of global governance

⁶⁹ Ibid., 7.

⁷⁰ Roy Culpeper, "Reforming the Global Financial Architecture: The Potential of Regional Institutions," Presented at a workshop on *The Reform of Global Financial Governance: Whither the IMF?*, The Centre for International Governance and Innovation, Waterloo, 10 June 2006.

⁷¹ See Jose De Gregorio et al., *An Independent and Accountable IMF* (Geneva: Centre for Economic Policy Research, 1999), 103-104.

has advantages over the centralized, bureaucratic IMF which the Fund should use to reflect and assess in determining its own comparative advantage.⁷² There has been a proliferation of the number of public and private institutions that overlap with IMF function and scope not just vis-à-vis its lending role but also with respect to its surveillance and other activities. Many of them are less prone to legitimacy and accountability problems, and the IMF's capacity to develop formal and informal, creative collaborative relationships with them - becoming more of a "node in a network" than a top down bureaucracy - is crucial to its future.

Developing a more active relationship with regional initiatives thus represents an important initiative, but some also question the effect of regional agreements on the IMF. Louis Pauly cautions about the "erosion of normative solidarity" resulting from emerging regional competitor organizations.⁷³ In similar vein, Henning argues the IMF needs to recognize regional initiatives while also assessing them by labelling some organizations as 'acceptable' and others as 'unacceptable' based on a set of agreed criteria.⁷⁴ This approach is, of course, unlikely to evoke much sympathy from those who see regional arrangements as a way to insulate their countries from IMF dictates and advice.

What about the IMF's existing lending to low income countries (LICs)? Many have suggested that the IMF should get out of the business of development lending by reducing IMF involvement in low-income countries. Critics of the Fund have

⁷² Tony Porter, "Beyond the International Monetary Fund: The broader institutional arrangements in global financial governance," *CIGI Working Paper*, no. 19 (February 2007).

⁷³ Louis Pauly, "IMF Surveillance and the Legacy of Bretton Woods," in D. Andrews, ed., *Orderly Change* (Ithaca: Cornell University Press, forthcoming 2007).

⁷⁴ Randall Henning, "Regional Arrangements and the International Monetary Fund," in Truman, *Reforming the IMF*.

argued that the IMF does not have the expertise to advise developing countries on development and trade policy. Debtor countries have long complained that the number and scope of loan conditionality were excessive and intrusive. Referred to as 'mission creep', critics of Fund conditionality have noted that the IMF has moved beyond its historical role of exchange rate monitoring to prescribing policies mirroring other development agencies. The Fund's 1999 Poverty Reduction and Growth Facility (PRGF) designed for heavily indebted poor countries (HIPC), in particular, has been highlighted for its intrusive and extensive conditionality that has involved the IMF staff in development issues beyond their expertise.

Former Managing Director Horst Köhler (2000-2004) had called for a "more focused IMF", one that would "streamline conditionality" especially structural conditionality that developing countries found particularly intrusive.⁷⁵ Fund staff were told that in design of loan conditionality they were to return to their core areas of expertise: exchange rate policies, macroeconomic stabilization, and financial sector policies.⁷⁶ Moreover, in response to criticism that IMF programs, especially PRGF programs, tended to fail because member states lacked commitments to reforms, the IMF introduced the concept of 'country ownership': member states would 'own' their programs by making greater commitments to their implementation. A new set of Guidelines on Conditionality was created in 2002, committing to increase member state 'ownership' of loan conditionality and implicitly reduce IMF structural conditionality that was deemed intrusive.

⁷⁵ Horst Köhler, "Toward a More Focussed IMF," Luncheon Address at the International Monetary Conference, Paris, 30 May 2000.

⁷⁶ Policy Development and Review Department (PDR), *Conditionality in Fund-Supported Programs: Policy Issues* (Washington, DC: International Monetary Fund, 16 February 2001), 34.

Critics argue that the PGRFs continue to be poorly conceived and implemented. Ramesh Kumar notes that the PRGFs have been marginal in terms of the size of developing countries' budgets which has explained why many eligible countries, particularly the poorest ones, do not use the facilities. Moreover, Kumar argues that there are continued difficulties in the IMF in actually internalizing the idea of conditionality ownership.⁷⁷ Momani attributes IMF staff organizational culture for staff failure to adopt political-economy tools needed to evaluate and measure members' country ownership. She argues that to achieve better policy implementation of conditionality, the Fund's organizational culture needs to promote debate and foster diverse internal thinking.⁷⁸

Others point out that development lending is taking the IMF away from providing countries with its comparative advantage: exchange rate advice. Truman suggests that the World Bank should absorb the role of development lending while the IMF continue its bilateral and multilateral surveillance of LICs.⁷⁹ This would make the LICs the main clients of the World Bank while keeping and applying IMF opinion and analysis. In defence of the Fund, James Boughton argues that the IMF still has a comparative advantage in offering LICs policy advice on how to improve governance, enhance revenue, and control spending. In his view, the IMF is the only universal institution with the expertise to provide LICs with policy advice and should therefore continue to service these members.⁸⁰

⁷⁷ Ramesh C. Kumar, "Poverty Reduction and the Poverty Reduction Facility at the IMF: Carving a New Path or Losing Its Way," *CIGI Working Paper*, no. 18 (February 2007).

⁷⁸ Bessma Momani, "Recruiting and Diversifying IMF Technocrats," *Global Society*, vol. 19, no. 2 (April 2005): 167-87; and, "IMF Staff: Missing Link in IMF Reform Debates," *Review of International Organizations*, forthcoming 2007.

⁷⁹ Truman, *A Strategy for IMF Reform*.

⁸⁰ James Boughton, "Does the World Need a Universal Financial Institution," *World Economics*, vol. 6, no. 2 (April-June 2005), 40.

The US government has generally endorsed the idea of lessening the Fund's role in development lending.⁸¹ De Rato has also stressed that the IMF's role in LICs "needs to be better defined and less thinly spread". In his view, IMF support and advice for these countries should focus only on issues relating to its core mandate of macroeconomic policies. In so doing, he notes that the Fund will have to develop "clear understandings" with other development agencies because the Fund's narrow macroeconomic focus will "not necessarily translate into growth and poverty reduction unless a more multi-disciplinary view of development is taken".⁸²

6. Conclusion

What kind of an IMF is likely to emerge from this patchwork of reform proposals? Beyond the marginal changes to four countries' quotas at the Singapore meeting, it is difficult to predict which of these proposals, if any, are most likely to be adopted. Still, there are some tentative lessons that can be learned from Singapore and beyond. To begin with, there is a remarkable degree of consensus that the IMF will become an increasingly marginal institution unless serious governance reforms are adopted. Most attention has been given to the need to reallocate 'chairs and shares', but this may also be where many political roadblocks will be erected, even with the opportunity created by European integration. The potential significance of this reform in re-establishing the Fund's legitimacy - even with a major reallocation - is also easily overstated. Equally if not more significant - and with less political roadblocks - may be other governance reforms such as changing the selection process for the Managing Director,

⁸¹ See Timothy D. Adams, "Statement by Under Secretary for International Affairs Timothy D. Adams in Advance of Meetings of the G-7, IMF, and World Bank" (Washington, DC: US Treasury Department, 19 April 2006).

⁸² de Rato, "The Managing Director's Report," 9.

the constituency system, the mandate of the Executive Board, and the staffing of the institution.

If a significant package of governance reforms was implemented, the result would likely be a re-invigorated IMF. It would also likely be an IMF whose activities were somewhat different than a decade ago when the IMF's reputation as a powerful international organization was based primarily on its lending capacity and associated conditionality. If the IMF emerges reborn from its current crisis in a strengthened form, its surveillance functions will likely be more prominent, particularly in their multilateral dimensions, and the content of its advice would be more flexible. The IMF would still be involved in lending and crisis-management, but its role in that respect will be both more collaborative with other private and public institutions and more focused on its core function of providing balance of payments support.

Of course, an alternative scenario is that there is no serious overhaul of the Fund's governance structure. In that event, the significance of reforms to the IMF's performance would diminish considerably. Without legitimacy, the Fund's ability to perform its surveillance role effectively - at both the bilateral and multilateral levels - will be severely constrained. And without trust in the institution, potential borrowers will only accelerate their drift away from the institution and increase their efforts to construct alternative crisis-management mechanisms.⁸³ In the words of Injoo Sohn, potential borrowers will move from 'rule takers' to 'rule makers' in global financial governance; the rules they make may assign little role to the IMF.⁸⁴

⁸³ See also Woods, *The Globalizers*, 188.

⁸⁴ Injoo Sohn, "Asian Financial Cooperation: The Problem of Legitimacy in Global Financial Governance," *Global Governance*, vol. 11, no. 4 (October 2005): 487-504.

What broader lessons can be learned from this crisis moment for scholars of the IMF and of global governance more generally? First, the crisis has highlighted the vulnerability of the IMF's power. Historically, its power has stemmed from three sources: its material resources (i.e. its lending), the authority derived from its technical expertise, and its delegated authority from states.⁸⁵ In the current moment, all three sources of power are being challenged seriously. Taken together, these challenges have generated a crisis for the institution.

Second, the crisis has highlighted some of the limitations of bureaucratic culture explanations for the IMF's changing global role. The most prominent explanation of this kind is advanced by Barnett and Finnemore, who attribute the expanding role of IMF conditionality into domestic affairs, particularly in the 1990s, partly to a bureaucratic logic; that is, in the face of persistent failure to stabilize balance of payments situations, IMF staff have pressed for an expansion of their mandate. They also add that the Fund staff have had expertise authority which states choose to listen to and learn from.⁸⁶ As borrower and non-borrower states have become more open to criticize Fund staff failures, it is less convincing that Fund member states have that much faith in Fund advice. As state preferences have changed, the Fund's ability to expand its mandate has also been constrained.

Also noteworthy has been the fact that the state preferences which have mattered have not just been those of dominant states. To be sure, the IMF's recent fate has been determined partly by the changing priorities of its dominant shareholder: the United States. But a number of lesser powers, particularly in East Asia

⁸⁵ For a discussion of these sources of power for international organizations, see Michael Barnett and Martha Finnemore, *Rules for the World: International Organizations in Global Politics* (Ithaca: Cornell University Press).

⁸⁶ *Ibid.*

and Latin America, have also had an important impact. Their new ability to influence the IMF predicament is a product not just of a broader shift in power in the world economy towards 'emerging markets' - a shift that is also currently influencing the governance of international trade in important ways. It is also a product of their new use of the political tool of 'exit' via their boycotting of IMF borrowing, the creation of regional financial alternatives, and the unilateral accumulation of large foreign exchange reserves.

Finally, even the role of the United States in this current crisis has been interesting. The shift in policy towards the IMF that was ushered in during the Bush years has surprised many who assumed the US sees the IMF positively as an institution that served its interests. It has revealed how the fate of international institutions can be strongly influenced by changing domestic politics within the US.⁸⁷ Our reading of the period also suggests the domestic political battles do not just reflect competing material interests of various private interests, but also important ideational variables.⁸⁸

⁸⁷ See also, J.Lawrence Broz and Michael Brewster Hawes, "Congressional Politics of Financing the International Monetary Fund," *International Organization*, vol. 60, no. 2 (April 2006): 367-99.

⁸⁸ See also, Woods, *The Globalizers*.

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