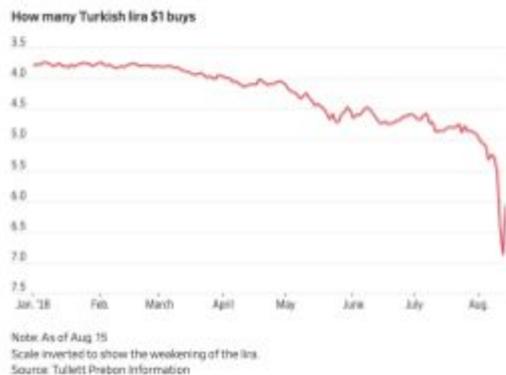


Evaluating the IMF (Part II)

August 21st, 2018
Instructor Lauren Ferry

What happened to Turkey's currency? Why did this happen?



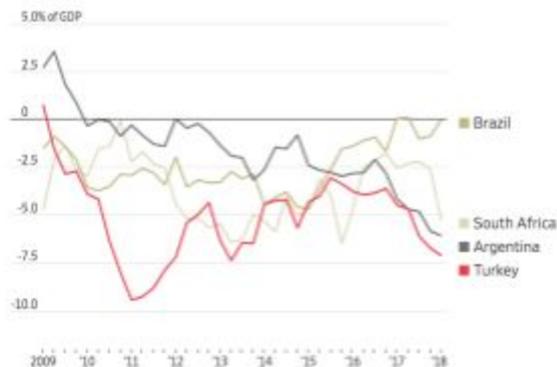
1) Central bank should have raised interest rates to fight inflation, but they didn't

2) Over reliance on hard currency loans

Are they doing anything to fix it? Not really

Is this likely to affect other countries? Maybe, but probably not

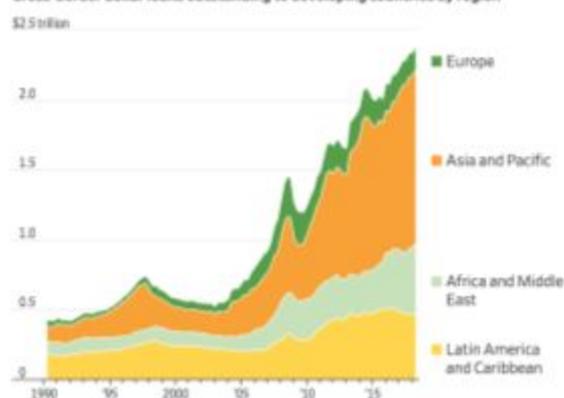
Current account balance, quarterly



Dollar Binge

Emerging markets' reliance on hard-currency funding has soared.

Cross-border dollar loans outstanding to developing countries by region



Source: Bank for International Settlements

Class learning objectives

- Evaluate evidence in favor of the effectiveness of IMF/World Bank lending based on social, economic and political outcomes.
- Evaluate the IMF's role in the Greek debt crisis
- Synthesize competing arguments on the impact of lending and formulate a persuasive argument in favor of one position.

The IMF and Tanzania

What was the relationship between the IMF and Tanzania? Is Tanzania an IMF success story?

Review Sharer's account of Tanzanian financial history

- Make a timeline of key events in Tanzania's history and its relationship with the IMF
- Economic trends? Political events? IMF policies?

1961: Tanzanian
independence



2007-2008 End of Sharer
article

Tanzania's key events

- 1961: Independence
- 1967-1980s: Ujamaa socialism
- 1985: Nyerere steps down
 - Recall Vreeland (2003) in Lecture 3 on refusing IMF assistance in 1983
- 1987: Camdessus becomes IMF President, implements reforms for the poorest countries (increases concessional lending)
- 1992: Amended constitution
- 1996: Multiparty elections

IMF success?

Sharer calls IMF intervention in Tanzania a success based on:

IMF success?

Sharer calls IMF intervention in Tanzania a success based on:

- Lower inflation
- Increased government revenues
- Privatization of banks and state owned enterprises (SOEs)
- Increase in per capita growth

On a post it note: What other information do you need to evaluate the role of the IMF?

- What other questions do you have? What statistics or facts could you look at?

Evaluating the IMF

- 3 activities of the IMF
 - Monitor economic developments (ind. countries and world trends)
 - Technical assistance (Advise in monetary and fiscal policy)
 - Conditional lending (smooth shocks and a catalyst to other lending)
- Also a goal of the World Bank
 - “We offer support to developing countries through policy advice, research and analysis, and technical assistance.”

Technical assistance

Capacity development accounts for 28% of the IMF's budget



Sharing knowledge and best practices leads to strong institutions and effective policies.

Through technical assistance (strengthening institutions) and training, the IMF helps countries grow their economies and create jobs.

 imf.org/capacitydevelopment
fb.com/IMFCapacityDevelopment
[@IMFCapDev](https://twitter.com/IMFCapDev)

Technical assistance

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- Provided through staff missions, long-term country placements, regional CD centers, and online learning
- Advice is centered on fiscal and monetary policy, legal frameworks and statistical training
- Additional trainings in person and online
 - 12,600 government officials have successfully completed online training
- Demand driven
 - All 189 members have used capacity development services at some point

Technical assistance

“ This partnership has been of substantial value to Nepal. We have arrived at a stage of sound AML/CFT legal, regulatory and enforcement frameworks as well as have come out of the FATF monitoring process. The credit of this achievement primarily goes to our international team, IMF and development partners.

I would like to extend our warm appreciation and sincere thanks to the members of IMF mission and development partners. It is indeed a cornerstone in our capacity building process. We look forward to strengthening such cooperation in the days to come.

DR. CHIRANJIBI
GOVERNOR, NEPAL RASTRA BANK

Public Finances

- Global – Helping Countries Manage Fiscal Risks from PPPs
- Liberia – Establishing a Modern Tax Administration
- Mali – Helping Manage Public Finances
- Mongolia – Improving Tax Collection
- Myanmar – A Holistic Approach to Strengthen Macroeconomic Capacity
- Peru – Improving Tax Compliance and Management of Public Funds
- Senegal – Mobilizing Domestic Revenue to Rebuild Fiscal Space
- South Sudan – Developing Capacity in Tax and Customs Administration

Monitoring and Data Collection

IMF

- World Economic Outlook
 - <http://www.imf.org/en/Publications/WEO/Issues/2018/07/02/world-economic-outlook-update-july-2018>
- Global Financial Stability Report
 - <http://www.imf.org/en/Publications/GFSR/Issues/2018/04/02/Global-Financial-Stability-Report-April-2018>
 - They even publish podcasts on the report:
<https://soundcloud.com/imf-podcasts/global-financial-stability>
- Regional Economic Reports
 - <http://www.imf.org/en/Publications/REO>

GROWTH PROJECTIONS

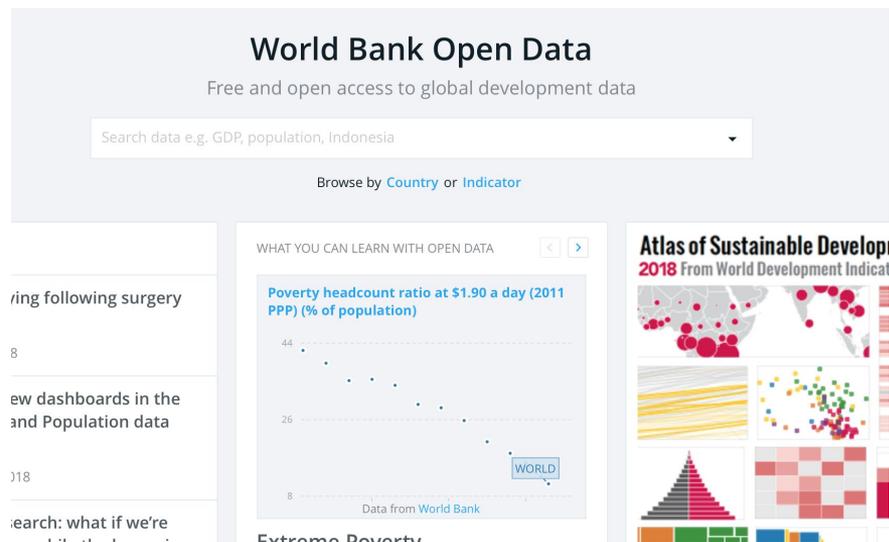
Less Even Growth, Rising Trade Tensions



Monitoring and Data Collection

World Bank Open Data

- Quarterly external debt statistics
- World development indicators
- Sustainable development goals
- Doing business



IMF data mapping

Go to <http://www.imf.org/external/datamapper/datasets>

What other information do you need to evaluate the role of the IMF in Tanzania?

- Financial statistics? History with the IMF? Social development issues?
- Choose one indicator that matches your questions, then screenshot a graph or image. Add the image to our class google slides:
https://docs.google.com/presentation/d/1JiZ76basD2Tl1NiSlkcStcuyeZLCtoW6LzSLHAeYR_4/edit?usp=sharing
- What does the graph tell us about Tanzania and the IMF?

Even if we focus just on lending:

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- It is difficult to evaluate the IMF's success
 - No counterfactual
 - Other interventions
 - Tradeoff between preventing financial crises and moral hazard
 - Represents the hardest cases
 - What is success?
 - What about the IMF? (lending, conditions, size, etc)

Moral hazard vs. Adverse selection

Moral hazard:

Adverse selection:

Moral hazard vs. Adverse selection

Moral hazard: “if agents do not pay for the consequences of their actions because they are insured, they have weak incentives to mitigate risk”

- If governments can rely on the IMF for foreign reserves, the government has fewer incentives to enact good policies

Adverse selection: “one partner...has private information that affects the other partner’s payoff if the transaction occurs.”

- Borrowing countries have informational advantages over the IMF. The IMF can’t screen out bad borrowers

How can we tell the difference

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If it's a moral hazard problem:

- Risk taking should be based on the likelihood that the IMF will bail them out
- Recidivism is bad. It incentivizes long term risk taking and countries that get multiple loans will be less likely to experience growth

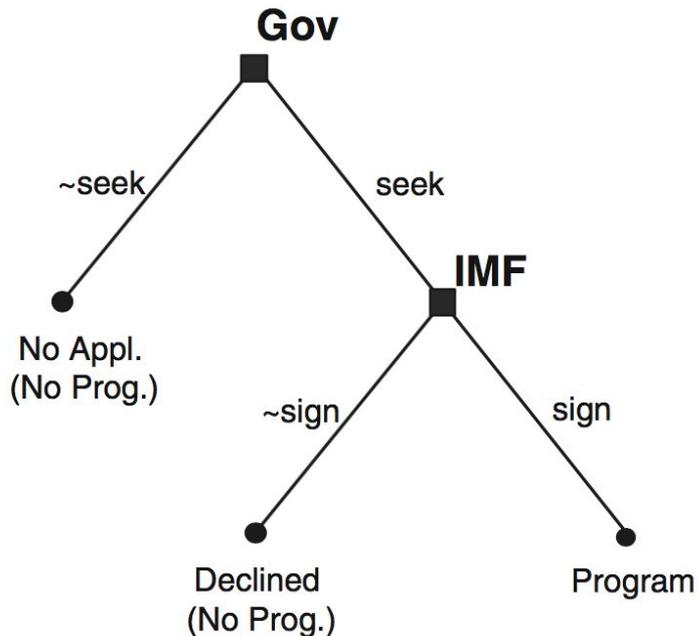
If it's an adverse selection problem:

- Countries that are most interested in participating in IMF programs are the worst candidates for growth
- If we control for selection, the effect of the IMF on growth should be positive
- Recidivism is positive. The IMF can gather information, and countries that get multiple loans should experience more growth.

Method Part I

How do we tease out moral hazard vs. adverse selection empirically?

- Selection equation
 - Governments that want IMF loans should be the worst candidates for growth
 - But if we don't observe a loan is it because...
 - The government didn't seek a loan
 - The IMF didn't sign a loan
 - Use economic data to assign non-loan countries to the most likely cases



The worst candidates are the most interested

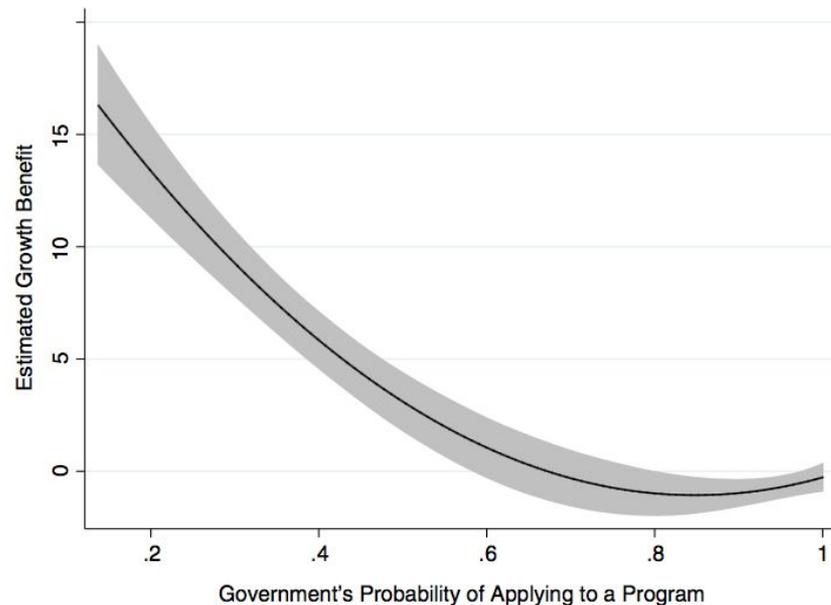
Governments are more likely to enter an IMF program when they have low levels of central bank reserves, high fiscal deficits, large debt service burdens

Predicted program participation is a good model of reality:

Pred. outcome	Actual outcome		
	No program	Program	Total
No Program	483	233	716
Program	256	524	780
Total	739	757	1496

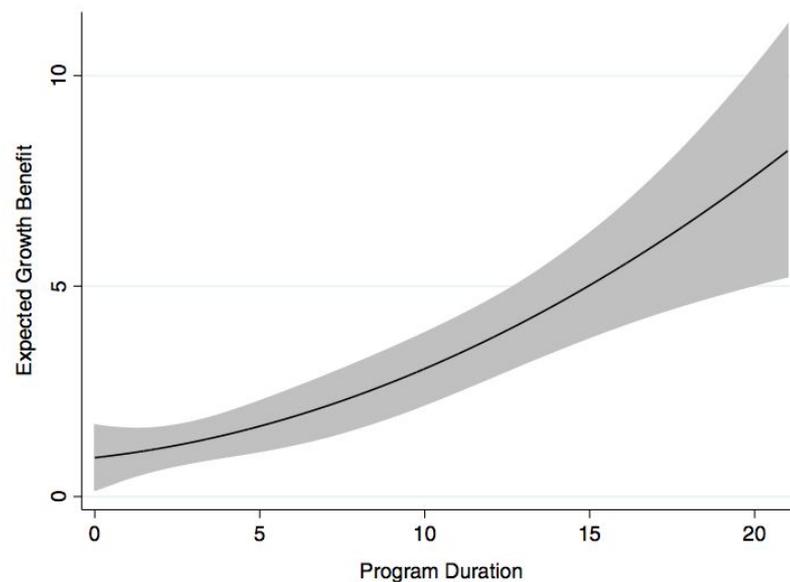
Method Part II

- Do countries that are more likely to use the IMF grow less?
 - Use the predicted probability of applying to an IMF program (from the selection equation)
- Countries most likely to use the IMF grow the least
 - Philippines
 - Gambia
 - Argentina



Method Part III

- Do multiple IMF programs provide the staff with more information to improve good programs and stop bad ones?
 - Use the estimated growth benefit (from the growth equation)
- IMF programs have more positive effects on growth after the country has already participated for a few years



Method Part III

- Do multiple IMF programs

The IMF has an adverse selection problem.
Correcting for this, IMF programs increase
recipient growth

participated for a few years

Program Duration

Other positive effects of IMF lending

- Catalyzing effects
 - Fund staff have highlighted that the IMF spurs additional aid inflows by signaling to donors policy credibility and commitment to reforms
 - Stubbs et al. (2016): IMF programs increase aid from other sources
 - IMF catalysis is stronger in sectors linked to its core competency areas, namely debt-related relief and general budget support
 - Stronger for large donors - US, Japan, etc.
- Prevention of other crises
 - The IMF can help lock in reforms that decrease the possibility of future crises
 - IMF involvement reduces the probability of a currency crisis (Dreher and Walter 2010) and banking crises (Papi et al. 2015)

Did the IMF “help” Greece and the Eurozone?

Origins of the Eurozone

- After WWII, the U.S. and political leaders in France and Germany sought to bind the former antagonists together economically
 - Minimize the Franco-German tensions that led to WWII
 - Bind together against Soviet expansion
- First focus was on coal and steel
 - Schuman plan to “make war not only unthinkable but materially impossible”
 - Economic integration increases the costs of war

European Coal and Steel Community

- The ECSC was founded in 1951 with 6 members: France, Germany, Italy, Belgium, Netherlands and Luxembourg
- It led to the formation of the European Economic Community
 - Established by the Treaty of Rome
 - Set common tariffs within Europe
- 1979: Set up the European Monetary System
 - Fixed exchange rates to the Deutsche Mark
- The Maastricht Treaty in 1991 formally established the EU with a common currency (Euro) and monetary authority (ECB)

Why a currency union matters

A common currency required countries to adjust their macroeconomic position prior to the use of the Euro

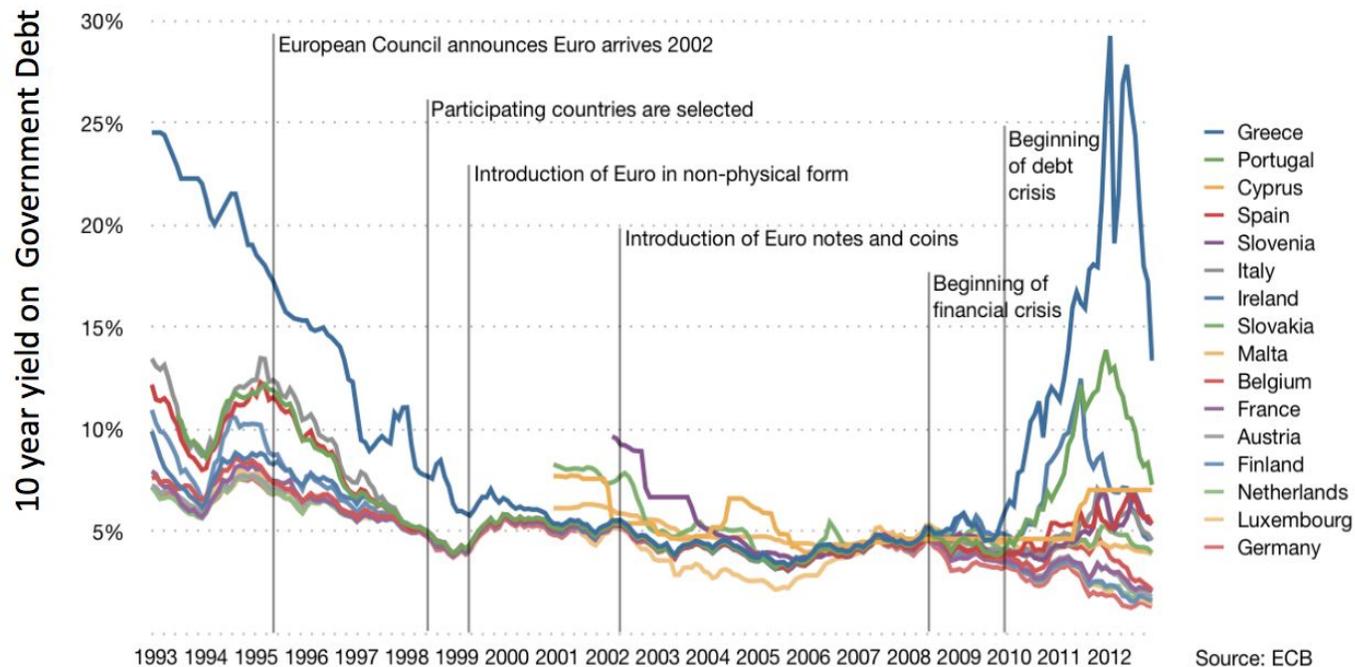
- Bring inflation down to the same level across countries
- Reduce national budget deficits to 3% of GDP, government debt to below 60% of GDP and inflation below 1.5%
- Enact common economic policies
- Lower all remaining barriers to the movement of goods, services, and people

Before the Euro was created, many countries (including Germany and France) had trouble meeting the requirements

Costs of a monetary union

- A currency union requires the government to give up key tools of macroeconomic adjustment
 - Can't use currency depreciation to attract trade
- Underlying weaknesses of the Eurozone
 - EU did not meet the requirements of an optimal currency area
 - Implicit bailout guarantee
 - ECB was not designed to be a lender of last resort in crisis
 - Not enough policy coordination
 - Large imbalances between surplus and deficit countries

Evidence of moral hazard



Source: ECB

Greece's history in the Eurozone

- 1981: Greece joins the European Economic Community
- 2001: Greece adopts the Euro currency
 - Later revealed that Greece misrepresented their finances (aided by Goldman Sachs)
 - Debt level is ~100% of GDP
- 2004: Greece hosts the Olympic games
 - Major loans to fund the games (loans are cheap because of Euro stability)
- 2007-8: Subprime crisis shook confidence in the European periphery
 - Foreign banks worried about loan repayment -- stopped lending to Greece
 - Greece can't get new loans to cover its current debt payments (sudden stop)

Causes of crisis

Greece built up massive external debts pre- 2009:

- Cheap borrowing because of Eurozone stability
- High government spending
- Current account deficit
- Tax evasion
- Cronyism/Labor market inefficiencies

The Greek Debt Crisis

October 2009, PM Papandreou announced that:

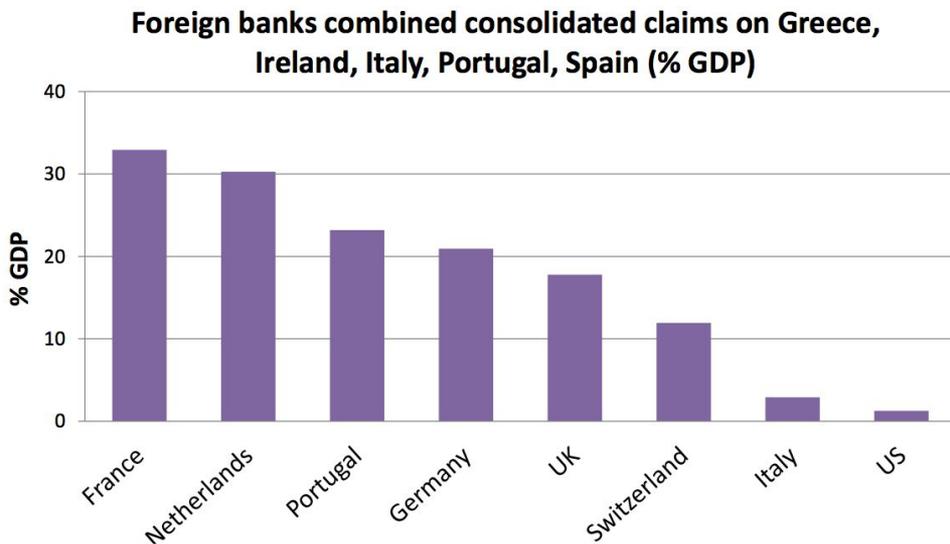
The Greek economy is in “intensive care. This is without doubt the worst economic crisis since the restoration of democracy.”

- Budget deficit > 12%
- Larger revised to 15%



Too big to fail?

- If one debtor defaults, it might trigger other defaults
- If a nation(s) default, the banking system in creditor countries may face large, perhaps fatal, losses



Options to deal with the Greek debt crisis

- Depreciation was not an option
- Austerity measures (reduce spending, reduce wages)
 - Opposed by Greek citizens
- Default on debt and leave the Eurozone
 - Opposed by elites and business interests
- More loans from the core Eurozone countries
 - Opposed by Germany and other core Eurozone countries
- Debt restructuring (write off private debt)
 - Opposed by bondholders

Options to deal with the Greek debt crisis

- Depreciation was **not** an option

Or...turn to the IMF and EU as lender of last resort

- Opposed by Germany and other core Eurozone countries
- Debt restructuring (write off private debt)
 - Opposed by bondholders

Greece and the IMF

In 2010 Greece experienced a sudden stop of private lending

- **May 2010:** the IMF and EU agreed to lend Greece \$146 billion
 - Austerity measures including 30 billion in spending cuts
- **February 2012:** the IMF and EU agree to a second bailout for \$130 billion
 - Banks agree to a 53% debt reduction
 - More austerity: increase taxes, reduce public salaries, pensions, etc.
- **June 2015:** Greek bailout expires and Greece becomes the first developed country to default on its IMF loans

Press Release: Statement by the IMF on Greece

June 30, 2015

Press Release No.15/310

June 30, 2015

Mr. Gerry Rice, Director of Communications at the International Monetary Fund (IMF), made the following statement today regarding Greece's financial obligations to the IMF due today:

"I confirm that the SDR 1.2 billion repayment (about EUR 1.5 billion) due by Greece to the IMF today has not been received. We have informed our Executive Board that Greece is now in arrears and can only receive IMF financing once the arrears are cleared.

"I can also confirm that the IMF received a request today from the Greek authorities for an extension of Greece's repayment obligation that fell due today, which will go to the IMF's Executive Board in due course."

A third bailout

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- **August 2015:** Greece receives a third rescue package
 - Funds and conditions come from the EU
 - **The IMF does not contribute**
 - Says it will not contribute until creditors provide significant debt relief
 - It will wait for the program's review to decide on its participation
- The government signed an “Articles of Agreement” with Greece in 2017
 - Makes the IMF a participant in the third bailout program
 - But does not commit the IMF to disbursing funds

EU says Greece can 'finally turn the page' as bailout ends

'The worst is over' after eight very difficult years for the country, commissioner says

Jennifer Rankin
in Brussels

Mon 20 Aug 2018
07:50 EDT



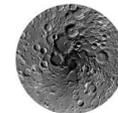
▲ The European commissioner for economic and financial affairs, Pierre Moscovici, announces the end of the Greek bailout. Photograph: Francois Lenoir/Reuters

Greece has turned the page to become “a normal” member of the single currency, European Union authorities in Brussels declared as the country finally exited its eight-year bailout programme.

most viewed in US



Francis Ford Coppola agrees Winona Ryder and Keanu Reeves might be married



Ice found on moon surface



The Eagles score biggest-selling album of all time in US, surpassing Thriller

August 20, 2018 officially exits the bailout program



Summer weather is getting 'stuck' due to Arctic warming

EU says Greece can 'finally turn the page' as bailout ends

most viewed in US



Francis Ford Coppola agrees Winona Ryder and Keanu Reeves might be married

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Donald Tusk 
@eucopresident



You did it! Congratulations to Greece and its people on ending the programme of financial assistance. With huge efforts and European solidarity you seized the day.

11:42 PM - Aug 19, 2018

 5,154  1,793 people are talking about this



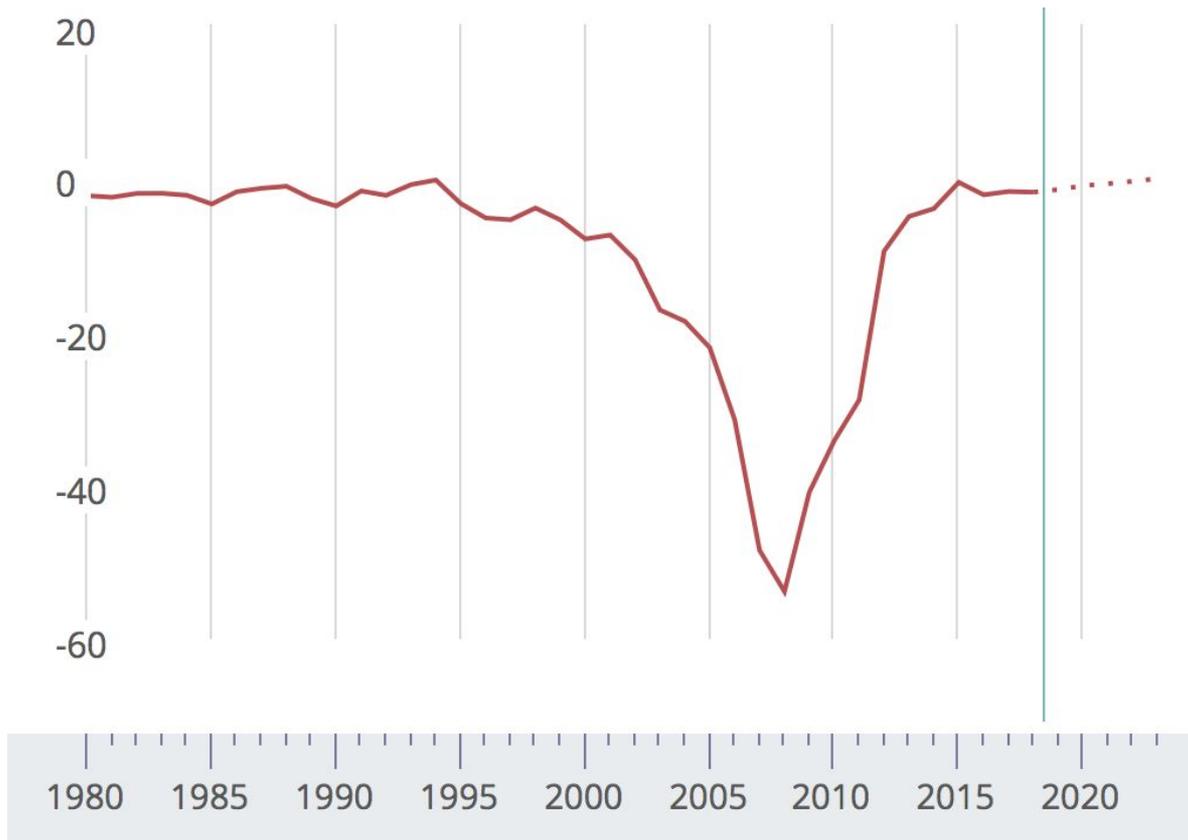
▲ The European commissioner for economic and financial affairs, Pierre Moscovici, announces the end of the Greek bailout. Photograph: Francois Lenoir/Reuters

Greece has turned the page to become “a normal” member of the single currency, European Union authorities in Brussels declared as the country finally exited its eight-year bailout programme.

Did the IMF (and the EU) help Greece?

— — —

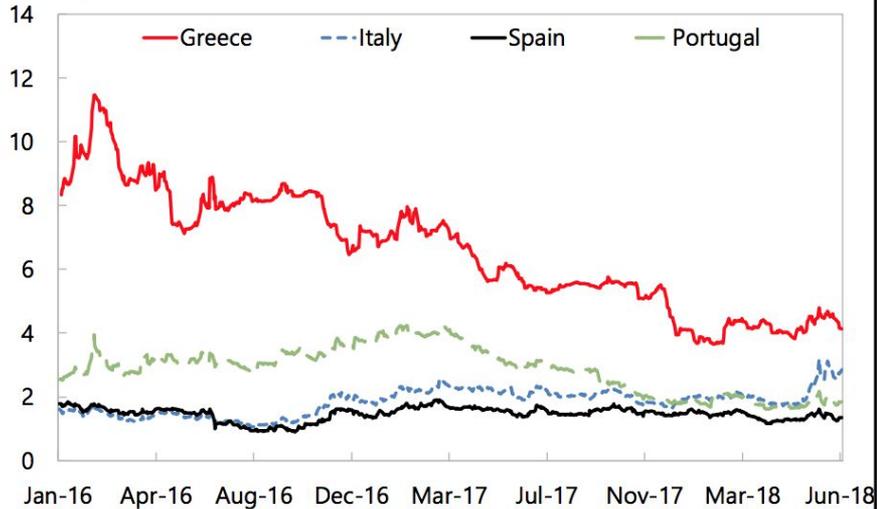




Greece had a (small) budget surplus in 2017

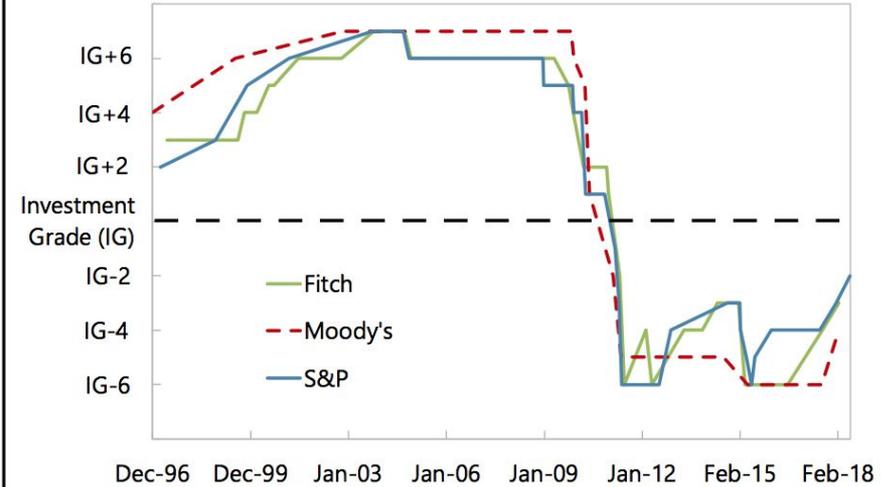
General Government 10-Year Bond Yields

(Percent)



Sources: Reuters; and Haver Analytics.

Greece: Sovereign Rating History



Sources: S&P; Moody's; and Fitch.

Notes: Investment grade corresponds to BBB-(S&P and Fitch), and Baa3 (Moody's).

Greece is viewed as more credit-worthy. Move towards borrowing on private international credit markets again soon.

What else can we attribute to the IMF?

Go to <https://data.worldbank.org>

What other information do you need to evaluate the role of the IMF in Greece?

- Financial statistics? Social development issues?
- Choose either an economic or social indicator, then screenshot a graph or image. Add the image to our class google slides:
<https://docs.google.com/presentation/d/1HwvmywsbBC4YWcYKz9ZKipw0fdRXyvR5MpXT79J2664/edit?usp=sharing>
- What does the graph tell us about Greece following IMF intervention?

What does the IMF say?

“Greece can point to many successes. It has [eliminated its extraordinarily high fiscal deficits](#) (from a deficit of 15 percent of GDP in 2009 to a surplus of just over one percent in 2017) and [brought its external transactions, its current account, into near balance](#). Doing this required some difficult decisions including pension and tax reforms, and improvements in public administration, such as a more independent revenue administration.

At the same time, Greece has put in place [better social safety nets](#), such as the Social Solidarity Income. Greece has also [made its labor markets more flexible](#) and wages more competitive.”

What does the IMF say?

But the IMF is leery about Greece's long run recovery if it doesn't get more debt relief

- Relief “can only be sustained over the long run under what appear to be very ambitious assumptions about G.D.P. growth and Greece's ability to run large primary fiscal surpluses, suggesting that it could be difficult to sustain market access over the longer run without further debt relief.”
- The IMF has criticized other creditors (Germany) for not forgiving more debt relief

Greece will most likely require further debt relief

Would you call the IMF (and EU)'s intervention in Greece a...

Success

Mixed

Failure

Which stack of evidence is more convincing?

Criticisms
of the
IMF

Triumphs
of the
IMF