

Reforms in the IMF and World Bank

August 28th, 2018
Instructor Lauren Ferry

Class Learning Objectives

- Describe the governance and lending reforms that took place in the Bretton Woods institutions between 2008 and 2010
- Explain the causes and consequences of reform
- Evaluate the effectiveness of reform efforts and their role in alleviating political tensions within the Bretton Woods institutions. Will they help restore trust?

The IMF and a crisis of legitimacy

IMF Confidence Crisis

The International Monetary Fund is increasingly irrelevant and even its own assessment found major flaws in its track record in the poorest countries.

April 12, 2007 | Emily Schwartz Greco, Soren Ambrose



As International Monetary Fund (IMF) and World Bank officials engage in their joint semi-annual meetings in Washington, the Fund has a nettlesome new task: convincing its shareholders (most of the world's governments, represented at the meeting by Finance Ministers and Central Bank Governors) that the institution should continue to exist.

What is the biggest threat to confidence in the IMF?



When poll is active, respond at PollEv.com/laurenlee835

Top

Grievances against the IMF

The effectiveness of the IMF depends on whether members see it as competent and impartial.

The perceived competence of the Fund is hindered by:

- Surveillance: expanded to everything and anything
- Conditionality: disagreement over conditionality and sovereignty
- Management of crises: what does debt sustainability mean?
- Governance problems: is the IMF impartial?

Output legitimacy

Output legitimacy: the quality of the institution's performance

In an Independent Evaluation Office report (2007) on IMF aid to SS-Africa:

- There is little difference, in either process or product, resulting from the transition away from structural adjustment
- IMF has done little to address poverty reduction and income distributional issues, despite institutional rhetoric to the contrary
- IMF has failed to be “proactive in mobilizing aid flows”
- It has done little “to analyze additional policy and aid scenarios and to share the findings with the authorities and donors.”

Input legitimacy

Input legitimacy: the process through which decisions and power is exercised

In 2005: LDC have 50% in extreme poverty (\$1.25/day)

- China 60% (1990) → 15% (2005)
- Brazil 15% → 8%
- India 54% → 42%

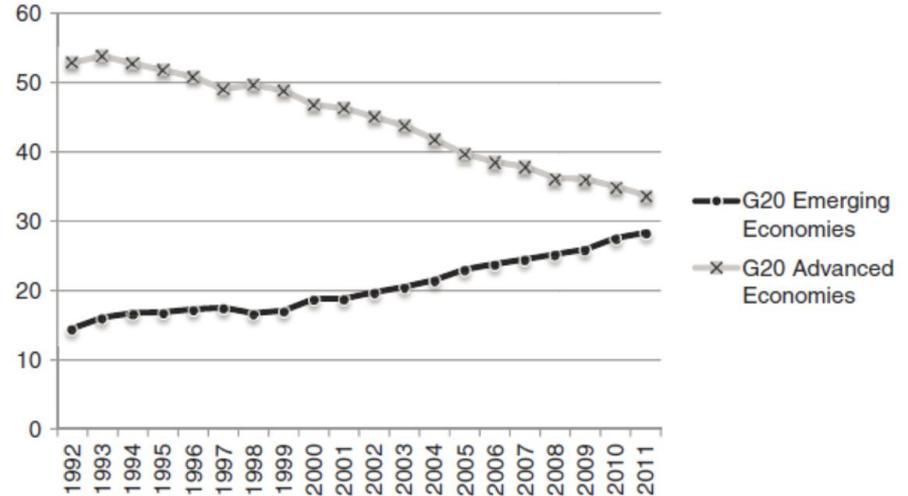


Figure 5.1 Share of world exports (%), G20 emerging and advanced economies. *Source:* Author's own calculations from WDI.

Input Legitimacy

Table 5.1 *Real GDP growth (%) in key economies*

	2009	2010	2011	2012	2013	2014	2015
World	-2.3	4.1	2.8	2.3	2.2	3.0	3.3
Euro Area	-4.2	1.7	1.5	-0.5	-0.6	0.9	1.5
Japan	-5.5	4.5	-0.5	2.0	1.4	1.4	1.3
United States	-3.5	3.0	1.8	2.2	2.0	2.8	3.0
China	9.2	10.4	9.3	7.8	7.7	8.0	7.9
Indonesia	4.6	6.1	6.5	6.2	6.2	6.5	6.2
Russia	-7.8	4.0	4.3	3.4	2.3	3.5	3.9
Turkey	-4.8	9.0	8.8	2.2	3.6	4.5	4.7
Brazil	-0.2	7.5	2.7	0.9	2.9	4.0	3.8
Mexico	-6.1	5.5	3.9	3.9	3.3	3.9	3.8
Argentina	0.9	9.2	8.9	1.9	3.1	3.0	3.0
India	9.1	8.7	6.2	5.0	5.7	6.5	6.7
South Africa	-1.8	2.8	3.1	2.5	2.5	3.2	3.3

Symptoms of a legitimacy crisis

States have two options:

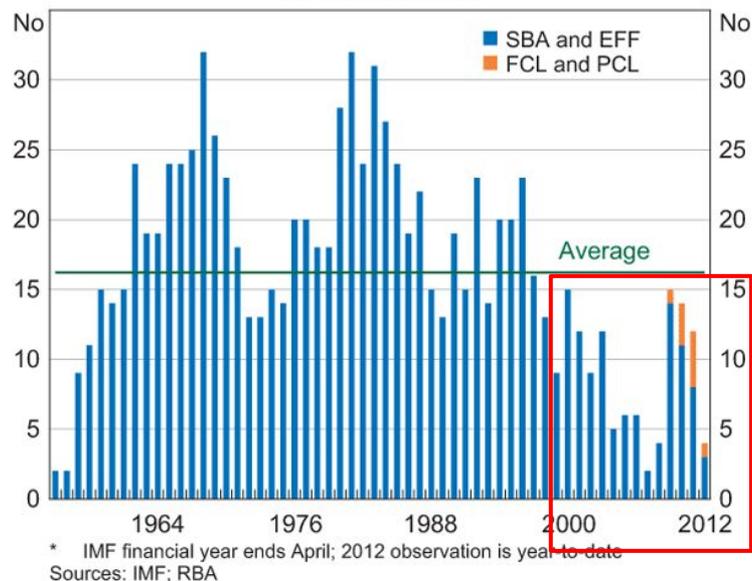
- Vote with their feet → find alternatives to the IMF
 - Less loans, more foreign reserves
 - Other multilateral banks (9/4)
 - Currency swaps (9/6)
- Reform from the inside
 - Governance and conditionality reforms

Fewer loans

After the early 00s, the IMF/WB gave fewer loans (by number and size)

- WB loans \$19 billion (1998) → \$10 billion (2004)
- IMF loans 25 billion SDR (2002) → 4 billion SDR (2004) → 3.5 billion SDR (2007)
 - In 2007, loans dropped to 10% of the 2003 level
 - Had to cut 15% of staff

Number of New IMF Lending Arrangements*
Non-concessional



Emerging markets even paid back their loans early

In 2005, Brazil and Argentina both unexpectedly announced an early repayment of IMF loans

- Argentina was clear that this was an emancipation from IMF conditions
- Serbia, Indonesia, Uruguay, and the Philippines soon followed

'Goodbye and good riddance'

The economics may be questionable but the decision by Argentina's president to pay off the IMF has broad public support, writes Oliver Balch



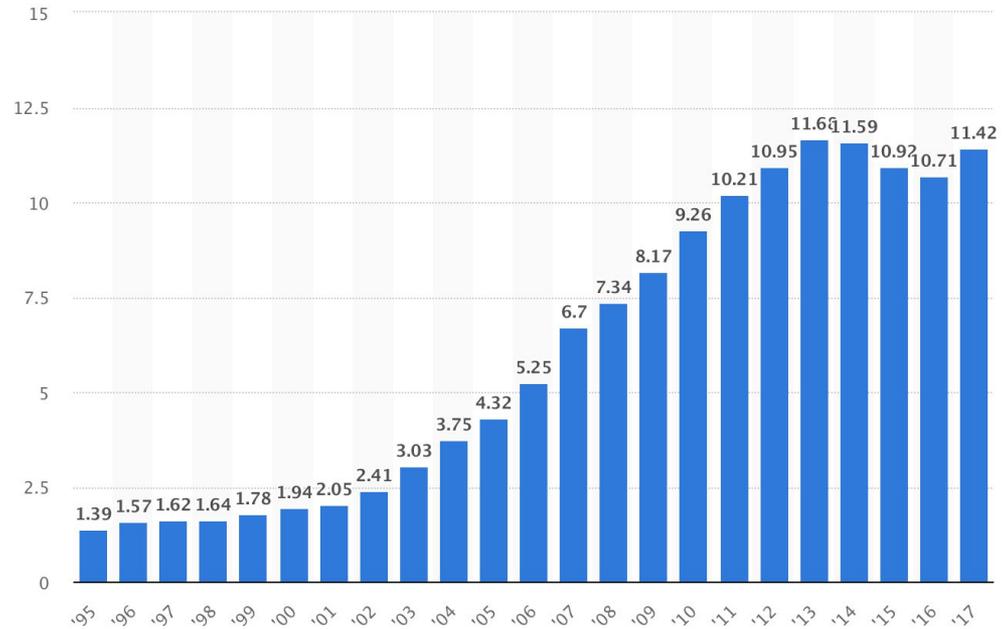
▲ The Argentinian president, Néstor Kirchner, announces that his country will pay off its IMF debt in full by the end of the year. Photograph: Leo La Valle/EPA

Four years ago, crisis-hit Argentinians took to the streets shouting "out with them all". Now they have seen part of their wish come true. In a surprise

More foreign reserves

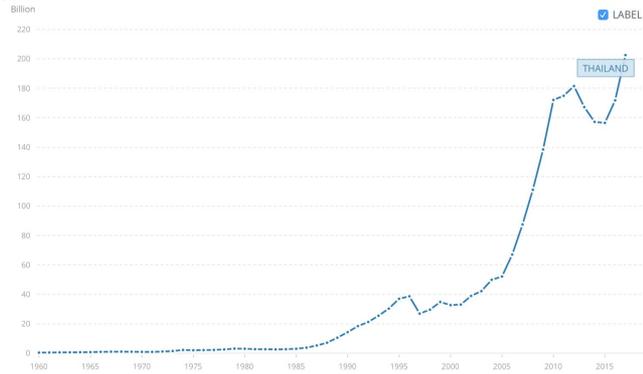
After the East Asian financial crisis countries began to build up foreign reserves

- Emerging economy reserves increased from \$0.4 trillion (1995) → \$1.5 trillion (1999) → \$7 trillion (2012)
- Con: inefficient use of resources

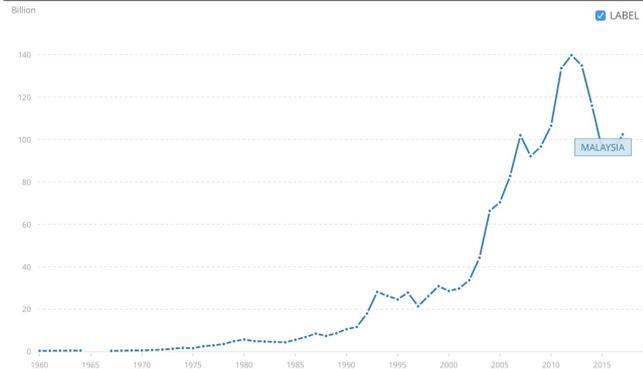


Especially in developing countries

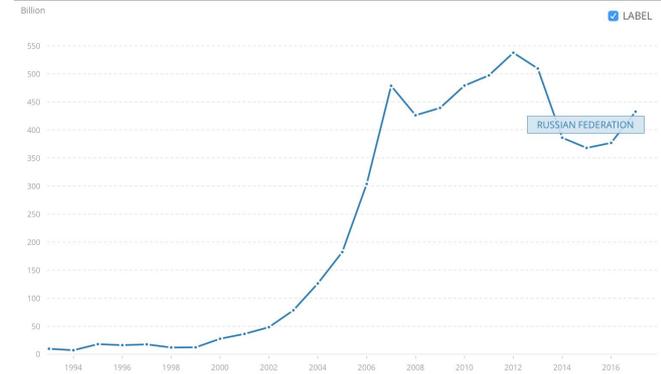
Thailand



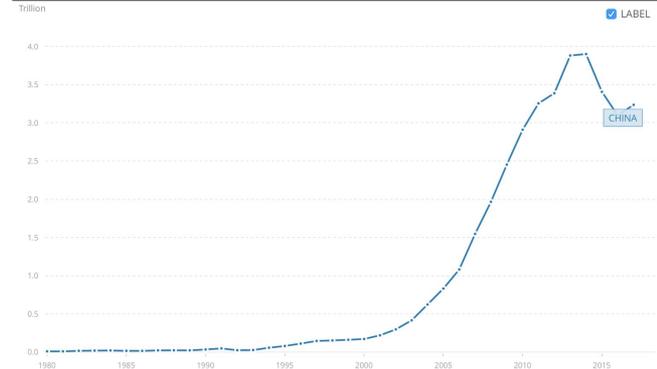
Malaysia



Russia



China



A call for reforms in the IMF

On September 18, 2006 the Board of Governors agreed to the “Singapore Resolution”

- The IMF would reform its governance system to increase the voice of quickly growing emerging markets and low income countries
- Negotiations and implementations would be carried out over two years
- 4 Ad-hoc adjustments would be implemented immediately
 - Increased voting power of China, Korea, Mexico and Turkey

A call for reform in the World Bank

— — —

- Monterrey Consensus (2002): Early call to enhance the participation of all developing countries
- 2008: The World Bank launched a “voice reform” to increase developing country representation
 - Without a general capital increase, the WB would have to cut back lending by 2014
 - After the call for reform in the IMF
 - Called for two phases of reform

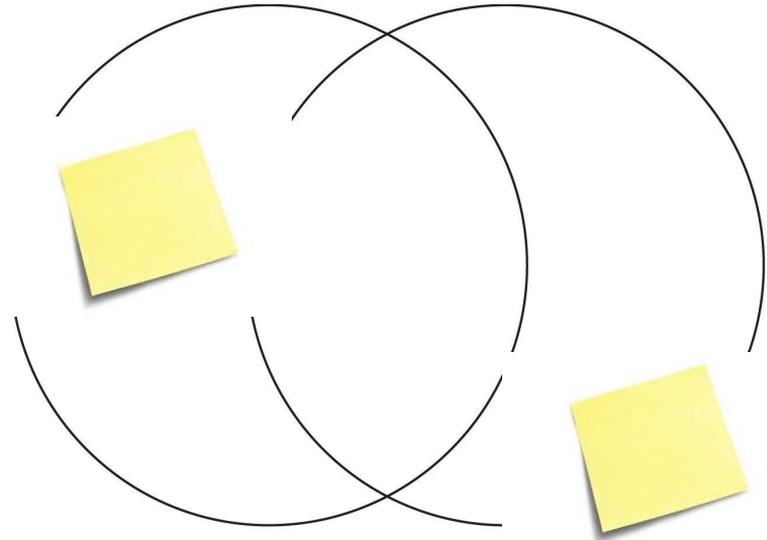
What happened?

1. With your group, identify the key points of reform for the IMF and World Bank
 - a. Right each separate reform on a different post-it-note
2. Identify three explanations for these reforms (according to Kaya)
 - a. Right each separate explanation on a different post-it-note



IMF vs. World Bank Reforms

1. Half your group will take the key points of reform post-it-notes. The other half will take the key explanations post-it-notes.
2. Pair up with the matching group from the other organization.
3. What do the IMF and World Bank reforms have in common? Where are they different?
 - a. Place your post-it-notes on the appropriate part of the venn diagram



IMF Reforms

- Triple Basic Votes to 5% (2008)
- Double quotas (2010) to \$733.90 billion (roll back NAB)
- All elected executive board (2010)
 - Europeans agree to give up two seats
- Multi-country constituencies appoint an Alternative Executive Director
- Vote formula reform and redistribution: 60% formula, 40% ad hoc
 - 6% to under-represented economies
 - Inclusion of International Reserves (5%)

Changes in IMF voting power

Table 5.3 *States' voting power (%) before and after the reforms*

Group/state	Pre-2006	Post-2008	Post-2010	Rate of change
G20 Advanced	46.62	44.35	42.54	-8.76
<i>USA</i>	<i>17.02</i>	<i>16.73</i>	<i>16.48</i>	<i>-3.20</i>
G20 European	19.07	17.53	16.37	-14.14
<i>Japan</i>	<i>6.11</i>	<i>6.23</i>	<i>6.14</i>	<i>0.49</i>
G20 Emerging	17.41	18.97	22.24	27.74
<i>China</i>	<i>2.93</i>	<i>3.81</i>	<i>6.07</i>	<i>107.34</i>
Sub-Saharan Africa	4.08	4.48	4.25	4.14
LDCs	3.03	3.58	3.63	20.04
LICs	2.44	2.78	2.79	14.45

World Bank Reforms

— — —

- Increase Basic Votes to 5.5% (2008)
- General Capital increase of \$86.2 billion
- Creation of elected executive board seat for Sub-Saharan Africa
- New formula for shareholders
 - Economic weight (70%), cumulative past and future contributions to IDA (20%), and development contributions (5%)
 - 3-4% to under-represented economies
- Commitment to revisit every 5 years

Changes in World Bank voting power

Table 6.2 *States' voting power (%) before and after the reforms*

Group/state	Pre-2008	Post-2008	Post-2010	Rate of change
G20 Advanced	44.37	43.07	40.59	-8.52
<i>USA</i>	16.36	15.85	15.85	-3.12
G20 European	15.86	15.4	14.14	-10.84
<i>Japan</i>	7.85	7.62	6.84	-12.87
G20 Emerging	18.8	18.73	22.3	18.62
<i>China</i>	2.78	2.77	4.42	58.99
Sub-Saharan Africa	4.72	5.29	5.07	7.42
LDCs	3.78	4.37	4.3	13.76
LICs	3	3.44	3.35	11.67

Explanations for IMF reforms

Table 5.4 *GDP of G20 emerging economies*

Country	GDP (2007–2009 average) at ME	GDP (2007–2009 average) at PPP
Argentina	300.19	560.25
Brazil	1544.71	1951.92
China	4334.91	8205.99
India	1223.01	3377.39
Indonesia	493.97	904.53
South Korea	938.24	1333.33
Mexico	1002.79	1503.81
Russia	1394.18	2170.86
Saudi Arabia	413.11	575.03
South Africa	281.79	498.24
Turkey	664.62	893.68

GDP at market exchange vs. GDP at PPP

GDP at market exchange: Conversion of GDP using the rate prevailing in the foreign exchange market

- How many USD do I need to convert to buy a £2 hamburger in London?

GDP at purchasing power parity: capture the differences between the cost of a given bundle of goods and services in different countries.

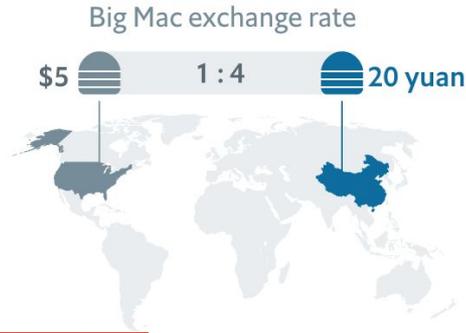
- If a hamburger is selling in London for £2 and in New York for \$4, this would imply a PPP exchange rate of 1 pound to 2 U.S. dollars
- Goods are usually cheaper in emerging markets
- More relevant for goods that are not internationally traded

How it works

Purchasing-power parity implies that exchange rates are determined by the value of goods that currencies can buy



Differences in local prices – in our case, for Big Macs – can suggest what the exchange rate should be



Raw index / GDP-adjusted

Using burgeronomics, we can estimate how much one currency is under- or over-valued relative to another



The Big Mac index

Local currency under(-)/over(+) valuation against the dollar, %



Sources: McDonald's; The Economist

* At market exchange rates (Jan 17th 2018)

† Average of four cities ‡ Weighted average of member countries § Average of five cities

Compares the cost of a Big Mac anywhere in the world

- Tells us whether currency is over or undervalued
- <http://www.imf.org/external/pubs/ft/fandd/2007/03/basics.htm>

Explanations for IMF reform

- Disputes over the role of emerging markets
 - Advanced economies want to increase accountability and discipline
- Disputes over financing
 - Advanced economies want to burden share
 - IMF requires upfront commitment and cannot raise its own funds -- large impetus
- Rules and convention
 - Followed general procedure for quota increase
 - Quota calculation with political adjustment

Explanations for World Bank Reforms

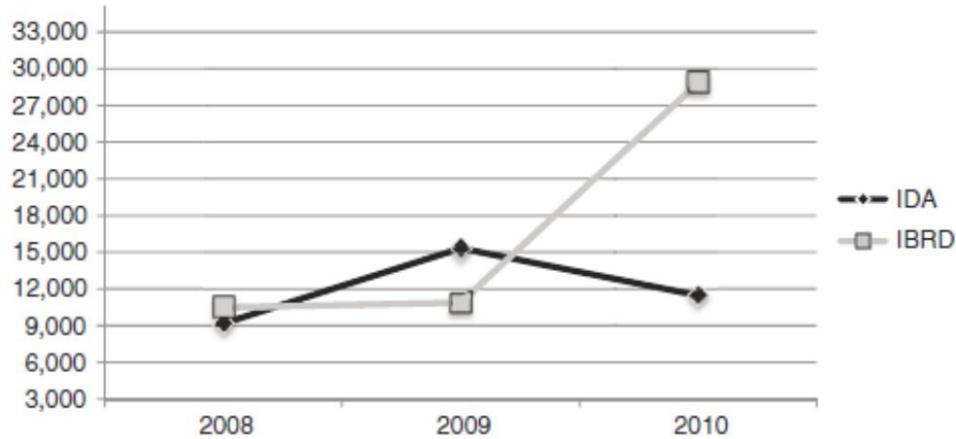
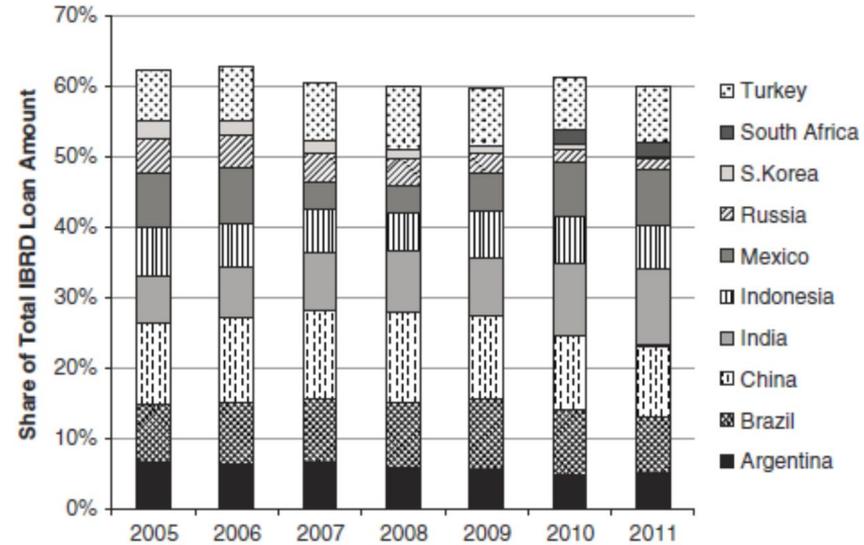


Figure 6.2 IBRD and IDA disbursements (in million USD). *Source:* Author's calculations from World Bank Annual Reports.



Explanations for World Bank Reform

— — —

- Disputes over the role of emerging markets
 - Emerging markets use the IBRD as a “bank”
 - Advanced economies want it to lend to the poorest members
- Disputes over financing
 - Emerging markets want to keep funds in the IBRD and limit their donations to the IDA
 - Advanced economies want to increase burden sharing in the IDA
 - WB has callable rather than paid in resources -- lower impetus
- Rules and convention
 - WB larger follows the IMF: Ex. GDP blend and basic votes

Which reforms were bigger?

Table 6.4 *States' post-reform voting power (%) in the World Bank and the IMF*

World Bank				
Group/state	Pre-2008	Post-2008	Post-2010	Rate of change
G20 advanced	44.37	43.07	40.59	-8.52
<i>USA</i>	16.36	15.85	15.85	-3.12
G20 European	15.86	15.4	14.14	-10.84
<i>Japan</i>	7.85	7.62	6.84	-12.87
G20 emerging	18.8	18.73	22.3	18.62
<i>China</i>	2.78	2.77	4.42	58.99
Sub-Saharan Africa	4.72	5.29	5.07	7.42
LDCs	3.78	4.37	4.3	13.76
LICs	3	3.44	3.35	11.67
IMF				
Group/state	Pre-2006	Post-2008	Post-2010	Rate of change
G20 advanced	46.621	44.347	42.535	-8.76
<i>USA</i>	17.023	16.727	16.479	-3.20
G20 European	19.068	17.529	16.372	-14.14
<i>Japan</i>	6.108	6.225	6.138	0.49
G20 emerging	17.411	18.973	22.241	27.74
<i>China</i>	2.928	3.806	6.071	107.34
Sub-Saharan Africa	4.083	4.477	4.252	4.14
LDCs	3.025	3.5787	3.6312	20.04
LICs	2.435	2.7759	2.7869	14.45

Do the governance reforms improve legitimacy?

Political success

Negotiations in the Fund and Bank were over the third decimal point

- “The package we have arrived at is a balanced one. The negotiations have not been easy, but our members have [shown a willingness to compromise and to demonstrate the flexibility needed to reach an agreement for the greater common good](#). For that I thank each and every member country—all the various national authorities that have made great efforts in advancing these discussions, including Korea which played an important role in bringing together the G-20 two weeks ago. I look forward to the Board of Governors’ approval of these reforms.”
- Had to be ratified by 85% of domestic legislatures -- almost didn’t pass the US!

It's a baby step

— — —

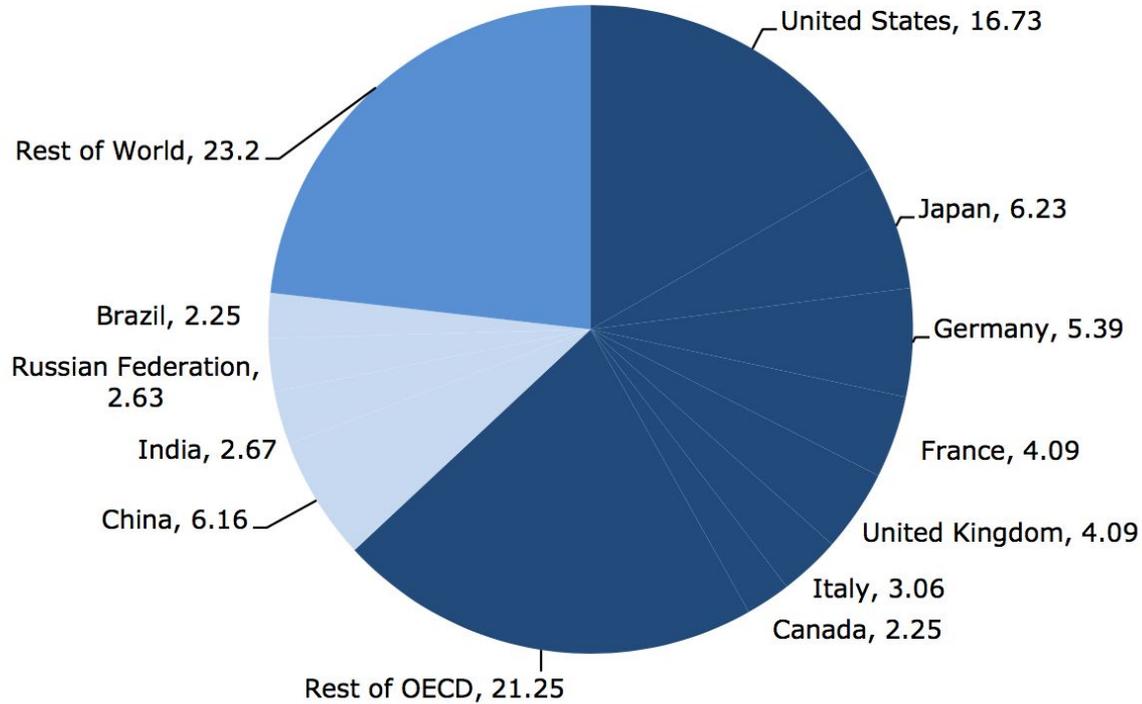
"These governance reforms are tremendously important for the future of our institution. They will enhance our effectiveness and add legitimacy to all of the other reforms that we are implementing. Their passage is a tribute to the hard work of the staff and the Board, and to your vision in recognizing that preparing the Fund for the future is in every country's interests. We will implement the agreed package over the next two years. There is much work to do, but this vote is a great start. It shows that the spirit of international cooperation is alive and well at the Fund."

-Christine Lagarde

Reforms are lacking...in the IMF

- Increased developing country shares by 6% BUT
 - Most of the increases went to emerging economies
 - China, India and Brazil and Russia = 4.5% change
 - Still based on market exchange rates
- Maintains US veto
- Some poor countries lost voting power
 - Nigeria, Venezuela, Libya
- Undemocratic election of IMF Managing Director
 - Also still a European

Voting power still biased



Reforms are lacking...in the World Bank

— — —

- General capital increase was actually very small
 - Probably only allows the WB to sustain lending similar to the 1980s
- Increased developing country shares by 3-4% BUT...
 - Some countries that are actually advanced economies were classified as developing
 - South Korea, Singapore, Saudi Arabia, etc.
 - Most of the shift went to middle income countries including China, Brazil, Turkey
- Lowest income countries still have <5% of the vote
- Shareholder “framework” still subject to political considerations

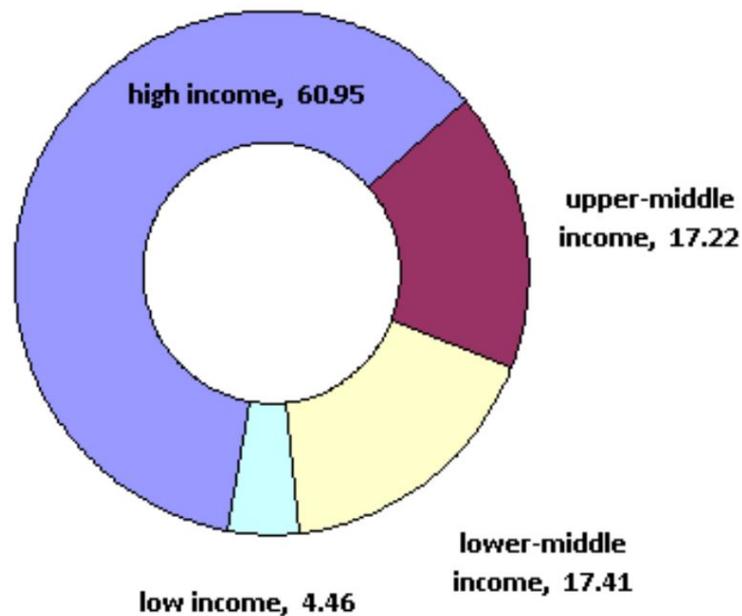
Politics > Shareholder formula

“Under the formula relating the capital increase to the change in shares, Russia and Saudi Arabia were destined to lose shares. Russian Prime Minister Vladimir Putin and his Saudi counterpart informed the president in imperative tones that **they would block the whole voice reform if they lost shares. So the architects of the voice reform changed the formula in such a way as to enable these states to gain back what they would have lost**—by pledging an additional amount for the *next* International Development Association (IDA) subscription (IDA16), and weighing these future contributions much more heavily than countries’ past contributions.”

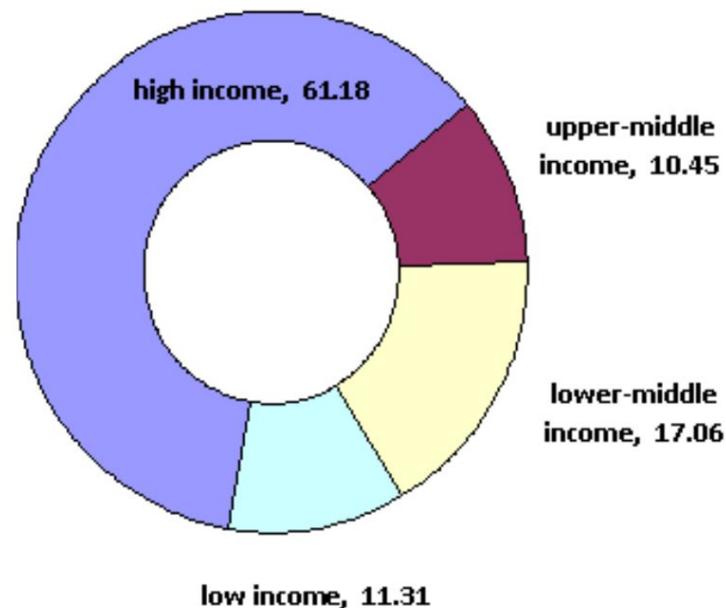
- The US suffered the fewest losses, most likely due to its veto power

Adjusting for mis-classified countries...

IBRD Voting Shares (%)



IDA Voting Shares (%)



Where do you stand?

act:onaid



CAFOD
just one world

RESULTS
the power to end poverty

tearfund

World Vision



Rt Hon Douglas Alexander MP
1 Palace Street
London
SW1E 5HE

16th April 2010

cc: Nemat Shafik
Michael Anderson
Rachel Turner

Dear Secretary of State

We are writing as civil society organisations in the UK as part of a European-wide alliance of NGOs, to urge you to push for progressive reform of the World Bank's governance. As the current round of reform reaches its conclusion, we believe it is crucially important to both secure as many gains as possible now, and also ensure that future reform will set an ambitious agenda. We believe there will be three key tests for the current round of reform.

Would you sign the petition?

Yes

No

15th General Review of quotas

The 15th Review provides an opportunity to assess the appropriate size and composition of the IMF's resources and to continue the process of governance reforms to realign quota shares with members' relative positions in the world economy, while protecting the poorest members. On December 5, 2016, the Board of Governors adopted a Resolution calling on the Executive Board to work expeditiously on the 15th Review in line with existing Executive Board understandings and the guidance provided by the IMFC, with the aim of completing the 15th Review by the 2019 Spring Meetings and no later than the 2019 Annual Meetings.

The fifteen general quota review

- 15th review should have taken place in 2015
 - But the 14th review wasn't ratified until 2016
- On October 3, 2016 the EB submitted a report that confirmed:
 - The importance for the Fund's legitimacy of continuing the process of governance reform
 - The need to move the timetable to 2019
 - March 2018, G20 reaffirmed this goal
- In 2018, the goals were to work on the quota size, formula, and distribution

The fifteen general quota review

- 15th review should have taken place in 2015

The biggest question: Will the US be on board?

- March 2018, G20 reaffirmed this goal
- In 2018, the goals were to work on the quota size, formula, and distribution

US position is uncertain

President Trump has not taken an official position on the 15th general quota review.

US Treasury Under Secretary David Malpass in 2017:

- “The IMF currently has ample resources to fulfill its mission...[and] in the upcoming review, [the United States will maintain] its veto on key issues within the IMF.”
- “The Administration has not yet made a decision regarding the 15th review”

Issues at stake

- Bilateral borrowing arrangements are expected to expire 2020
 - US participation in New Arrangements to Borrow (NAB) will expire in 2022 without Congressional approval (which is unlikely)
- The only way the US can maintain the IMF's capacity is to support a general quota increase
- The GDP shares of the advanced economies have fallen since 2010
 - The GDP shares of the emerging economies have risen since 2010
 - What does this mean for voting power?

According to quota calculations...

— — —

COUNTRY	ACTUAL QUOTA SHARE	GDP BLEND WORLD SHARE	CALCULATED QUOTA SHARE
<i>United States</i>	17.398	20.137	14.478
<i>Japan</i>	6.461	5.533	5.100
<i>China</i>	6.390	15.441	12.581
<i>Germany</i>	5.583	4.255	4.951
<i>France</i>	4.225	3.077	3.168
<i>UK</i>	4.225	3.190	3.568
<i>Italy</i>	3.159	2.387	2.399
<i>India</i>	2.749	4.299	3.113
<i>Russia</i>	2.705	2.781	2.564
<i>Brazil</i>	2.315	2.862	2.250
OTHERS			
<i>Saudi A.</i>	2.095	1.158	1.663
<i>Mexico</i>	1.868	1.766	1.737
<i>S. Korea</i>	1.799	1.734	1.989
<i>Belgium</i>	1.344	0.574	1.113
<i>Turkey</i>	0.979	1.282	1.161
<i>Indonesia</i>	0.974	1.692	1.307

Importance to the BRICs

2017 BRICS summit:

- The leaders of the five member countries resolved to foster a global economic governance architecture that is more effective and reflective of current global economic landscape, increasing the voice and representation of emerging markets and developing economies.

India has been particularly vocal

- “There is an urgent case for revising quota shares in favour of dynamic emerging market countries in line with global economic realities to maintain fairness in the governance structure of the Fund”

What is the most important area of reform in 2019?

Reconstruct board
membership

Greater balance
between GDP and vote
share

Greater representation for
the poorest countries

Separate IMF reform
from quota increases

Reforms aren't that
important

Output legitimacy

IMF modernizes lending practices

Press Release: IMF Overhauls Lending Framework

March 24, 2009

Press Release No. 09/85

March 24, 2009

The Executive Board of the International Monetary Fund (IMF) today approved a major overhaul of the IMF's lending framework, including the creation of a new Flexible Credit Line (FCL).

2009 reforms in the IMF

Direct response to the European financial crisis

Includes:

- Modernizing conditionality
- New, flexible, credit line
- Enhanced flexibility of regular stand by arrangement
- Double access limits

Modernizing conditionality

— — —

- IMF will rely more on ex-ante conditionality rather than ex-post conditionality
 - Pre-set qualifications to borrow
 - Rather than end targets to continue borrowing
- Structural performance criteria will no longer exist
 - Structural reforms are still important
 - Monitoring will be done through program reviews
 - No formal waivers required if countries don't meet structural reforms
 - "Reduce the stigma"

Flexible credit lines

— — —

- For countries with “strong fundamentals, policies and track records of policy implementation”
 - Aimed at crisis prevention
 - No phases of lending and no ex-post conditions
- Specifics
 - Longer repayment period
 - No hard cap on Fund resources
 - Flexibility to draw or treat it as a precautionary instrument

Questions?

Go to <https://www.imf.org/external/np/exr/faq/facfaqs.htm>

1. Choose one commonly asked question about lending reform
2. Read and analyze the answer
3. Describe the answer to your neighbor

Return to a focus on governance

April 2018: EB approves a new framework for promoting good governance

- Assess the nature and severity of governance vulnerabilities (corruption)
- Establish the negative impact of corruption on development
- Provide policy advice and capacity development support to members engaged with the Fund
- Focus on measures designed to prevent private actors from taking bribes

Recent waves of reforms in the World Bank

April 2018: Shareholders endorsed a \$13 billion paid-in-capital increase in World Bank

- \$7.5 billion to IBRD
- \$5.5 billion to IFC



Lending reforms

The world bank will charge higher rates for developing countries with higher incomes

- IBRD will channel 70% of its lending to low-income crises
 - Income based lending target
 - Not binding in crisis situations
- More aggressive approach to borrowing country “graduation”
 - No change in policy, but a more systematic application
- Cap annual salary growth
- China increases voting power from 4.68 to 6.01 (US 16.89 to 16.77)

Lending reforms

The world bank will charge higher rates for developing countries with higher incomes

According to the US Treasury, the US agreed to capital increase in exchange for reforms

- No change in policy, but a more systematic application
- Cap annual salary growth
- China increases voting power from 4.68 to 6.01 (US 16.89 to 16.77)

Infographic assignment

1. Sign up for the development bank of your choice
 - a. Two students per development bank
2. Requirements
 - a. Present information of interest to a general audience
 - b. Provide information on multiple aspects of the organization
 - c. Four graphics and two statistics
 - d. Clear, organized, and easy to follow
 - e. 1-2 paragraph of analysis
3. For guidance see: Prompt, examples, how-to-guide, rubric
 - a. All on TritonEd

Example

WORLD OCTOPUS DAY

ALL SPECIES ARE VENOMOUS, BUT THE BLUE-RINGED OCTOPUS IS THE ONLY ONE DANGEROUS TO HUMANS, RESPONSIBLE FOR AT LEAST TWO DEATHS.

one hundred thousand IS THE MAXIMUM NUMBER OF EGGS THAT A FEMALE OCTOPUS CAN LAY, BUT THE AVERAGE LITTER SIZE IS ONLY 80.

OCTOPUSES VS. OCTOPI THE PLURAL IN ENGLISH IS "OCTOPUSES," BUT THE GREEK PLURAL FORM "OCTOPODES" IS SOMETIMES USED. "OCTOPI," WHILE COMMONLY USED, IS CONSIDERED INCORRECT.

AN OCTOPUS HAS 3 HEARTS

THE GIANT PACIFIC OCTOPUS CAN WEIGH MORE THAN 600 POUNDS

OCTOPUSES ARE ABOUT **90%** MUSCLE

THE GIANT PACIFIC OCTOPUS CAN INHABIT DEPTHS OF UP TO 5,000 FEET

A mature female octopus can have up to 280 suckers on each arm! Each sucker contains thousands of chemical receptors, with sensitivities to both touch and taste.

OCTOPUSES CAN QUICKLY CHANGE THE **COLOR AND TEXTURE** OF THEIR SKIN

Octopuses inject their prey with venom using a beak similar to a bird's made from the same tough material as a lobster shell.

BECAUSE THEY DON'T HAVE BONES, EVEN LARGE OCTOPUSES CAN FIT THROUGH AN OPENING THE SIZE OF A QUARTER

300 RECOGNIZED SPECIES OF OCTOPUS

NATIONAL AQUARIUM | aqua.org

Example Graphic

Example Statistic

Reminders

NO CLASS THURSDAY 8/30

- Virtual Office Hours BY APPOINTMENT on Friday, August 31st from 1:30-3pm PST
 - Email me by Friday at 9am to sign up for a 15 minute block
 - I will email you a google hangout link a few minutes before your time slot
- No office hours on MONDAY 9/3 (Labor day)
 - Will be available for virtual office hours BY APPOINTMENT
 - Will be available via email