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THE IMF’S PURSUIT OF CAPITAL ACCOUNT CONVERTIBILITY: A DEVELOPING COUNTRY PERSPECTIVE

Ramit Nagpal*

In the 1990s, the International Monetary Fund (IMF or Fund) aggressively encouraged and/or stipulated the opening up of the economies of the developing countries to unhindered movement of capital from the developed world. It did this (1) through surveillance consultations conducted annually with its member countries (Article IV Consultations), and (2) by stipulating policy and structural conditions in its financial program arrangements with the member countries (Conditionalities). Analysis of the IMF’s Articles of Agreement and its program arrangements with Korea, Thailand and Indonesia during the Asian Financial Crisis of 1997-98 reveals that the IMF’s insistence on capital account convertibility was untenable and beyond its mandate. Furthermore, proliferation in the Conditionalities after the Washington Consensus, 1989, and its rollback after the Monterrey Consensus, 2002, testifies to the IMF’s political subjugation and the economic philosophies of its major stockholders. To gain acceptability in the developing world, the IMF needs to realign itself to the growing role of the emerging markets in the world economy, restructure its governance by having a decision-making process independent of its ownership, and then look at de jure expansion of its oversight from international current to capital account transactions.

I. INTRODUCTION

THE IMF actively engages with almost all of its 184 member countries on matters of macro-economic policy and financial sector development, but yet remains extremely unpopular in the developing world. A string of financial crises since the 1990s, in Mexico, Korea, Indonesia, Thailand, Russia, Brazil, Argentina et al, attributable in varying degrees to the structural reforms insisted upon by the IMF in these countries, has severely battered its neutral credentials. The governments of the developing countries may find it convenient to shift the blame for their economic mismanagement onto the IMF, but it does merit a review if the IMF has stretched its mandate by imposing structural conditions extraneous to its financing. This paper explores, in the context of the Asian Financial Crisis of 1997-98, one such structural condition: the capi-

tal account convertibility. It seeks to ascertain the validity of the IMF's actions under its Articles of Agreement and also the influence of the 1989 Washington Consensus 1, and the 2002 Monterrey Consensus 2 on the conditions it stipulates for its assistance.

The remainder of this article proceeds as follows. Part II discusses the scope of the IMF's Articles of Agreement and the basis of the Conditionalities; Part III analyzes the IMF's commitment to the cause of capital account convertibility during the Asian Financial Crisis as experienced in Korea, Thailand, and Indonesia; Part IV reviews the linkage of the Conditionalities to the Washington Consensus and to its rollback after the Monterrey Consensus; and Part V concludes.

II. ARTICLES OF AGREEMENT; CONDITIONALITIES

A. Scope

The IMF's primary mission since its inception in 1945 has been to maintain international stability in foreign exchange rates, avoid competitive currency devaluations, and eliminate foreign exchange restrictions and barriers to current account transactions in order to foster international trade and economic growth. Article I of its charter, the Articles of Agreement, lays down the parameters that the IMF is required to operate under:

- To promote international monetary cooperation through a permanent institution which provides the machinery for consultation and collaboration on international monetary problems.
- To facilitate the expansion and balanced growth of international trade, and to contribute thereby to the promotion and maintenance of high levels of employment and real income and to the development of the productive resources of all members as primary objectives of economic policy.
- To promote exchange stability, to maintain orderly exchange arrangements among members, and to avoid competitive exchange depreciation.
- To assist in the establishment of a multilateral system of payments in respect of current transactions between members and in the elimina-

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tion of foreign exchange restrictions which hamper the growth of world trade.

- To give confidence to members by making the general resources of the Fund temporarily available to them under adequate safeguards, thus providing them with opportunity to correct maladjustments in their balance of payments without resorting to measures destructive of national or international prosperity.

- In accordance with the above, to shorten the duration and lessen the degree of disequilibrium in the international balances of payments of members.

In order to meet its objectives, the IMF provides (1) financial assistance to correct balance of payment problems; (2) surveillance consultations to monitor macro-economic and financial sector developments and policies at a global, regional, and country level; and (3) technical assistance to the governments and central banks of the member countries.

IMF member countries are obligated under article IV, section 1 of the Articles of Agreement to direct their economic and financial policies to achieve orderly economic growth without erratic disruptions. More specifically, each member commits under article VIII of the Articles of Agreement, subject to certain exceptions provided therein and in article XIV, not to “impose restrictions on the making of payments and transfers for current international transactions,” nor to “engage in, any discriminatory currency arrangements or multiple currency practices, . . . except as authorized under this Agreement or approved by the Fund.” Article VI, section 3, clarifies that members countries “may exercise such controls as are necessary to regulate international capital movements,” but not in a manner that “will restrict payments for current transactions” except to tide over temporary scarcity in currency as provided in article VII, section 3(b) and for the transition phase as provided in article XIV, section 2.

To ensure compliance with the above, the IMF has the right under article IV, section 3, of the Articles of Agreement, to “exercise firm surveillance over the exchange rate policies of members.” Each member country is obligated to provide the IMF with the information necessary for such surveillance and to consult with it on its exchange rate policies. The IMF is duty bound to “respect the domestic social and political poli-
cies of members, and... the circumstances of members."¹¹ Under article IV of the Articles of Agreement, the IMF holds bilateral discussions with member countries every year to collect economic and financial information and discuss the country's economic development and policies.¹² In other words, the appraisal of a member country's exchange rate policies is made within the framework of the general economic situation and economic policies of the member country. These are commonly known as Article IV Consultations¹³ and play a significant role in shaping the economic policies of the member countries.

B. Financial Assistance Program

The IMF's core responsibility is to provide short-term financial assistance to countries experiencing balance of payment problems. This enables countries to rebuild their international reserves, continue paying for imports, and restore conditions for economic growth.¹⁴ Over the years, the IMF has developed a number of financial assistance facilities. Low-income countries can borrow at a concessional interest rate of 0.5 percent through the Poverty Reduction and Growth Facility, which is required to be repaid over a period of five and a half to ten years.¹⁵ The IMF provides non-concessional loans through the following main facilities: (1) Stand-by Arrangements, (2) the Extended Fund Facility, (3) the Supplemental Reserve Facility, (4) the Compensation Financing Facility, and (5) Emergency Assistance.¹⁶ Stand-By Arrangements "help countries address short-term balance-of-payments problems."¹⁷ These arrangements are typically for a length of twelve to eighteen months and are to be repaid within two-and-a-half to four years.¹⁸ The Extended Fund Facility "help[s] countries address more protracted balance-of-payments problems."¹⁹ These arrangements are usually for three years, with repayment expected within four-and-a-half to seven years.²⁰ The Supplemental Reserve Facility was introduced in 1997 to bail out crisis-hit countries experiencing large and sudden outflows of capital.²¹ These arrangements are expected to be repaid within two to two-and-a-half years.²² The Compensatory Financing Facility "was established in

¹¹. Id.
¹². Id.
¹⁴. See What is the International Monetary Fund?, supra note 4.
¹⁷. Id.
¹⁸. See id.
¹⁹. Id.
²⁰. See id.
²¹. Id.
²². Id.
1963 to assist countries experiencing either a sudden shortfall in export earnings or an increase in the cost of cereal imports caused by fluctuating world commodity prices." Finally, Emergency Assistance was established to support recovery from natural disasters and conflicts, and is expected to be repaid within three-and-a-quarter to five years.

The IMF usually provides its financial assistance under an arrangement that sets out "the specific policies and measures a country has agreed to implement in order to resolve its balance of payments problem." This arrangement, formulated by the member country and the IMF together, is manifest in a Letter of Intent and may be accompanied by other documents such as Memoranda of Economic and Financial Policies or other policy framework papers.

C. Conditionalities

Since the IMF does not finance specific projects or activities, its lending is conditional on policies that the borrowing country must adopt in order to correct its balance of payments problem. Conditionality is a central feature in the IMF's involvement with its member countries. This is to ensure that the borrowing country repays the loan by strengthening its economy and removing the root causes for its balance of payment problems. The IMF's "financing and policy adjustments by the [member] country are intended to be two sides of a common response to external imbalances." Thus, it provides safeguards to the IMF "to ensure that successive tranches of financing are delivered only if key policies are on track." It also provides assurances to the borrowing "country that it will continue to receive the Fund's financing . . . [if] it continues to implement the policies envisaged." The funds are, therefore, disbursed in a phased manner linked to the borrowing country meeting its scheduled policy commitments.

The legal basis for the Conditionalities stipulated by the IMF on a borrower country flows from the following provisions in the Articles of Agreement:

- Article I: The IMF is mandated to make "the general resources of the Fund temporarily available to them under adequate safeguards."
Article V, section 3: The IMF is authorized to adopt general policies on the use of its general resources and to adopt special policies that will assist members to solve their balance of payments problems in a manner consistent with the IMF’s articles;\(^{34}\) and

Article XXX (b): All the conditions for access to the IMF’s resources are spelled out in the self-contained arrangements. A decision of the IMF that a member is assured that it will be able to access the financing “in accordance with the terms of the decision during a specified period and up to a specified amount.”\(^{35}\)

Conditionality may be in the form of (1) Prior Action: i.e., a prior measure that the member country agrees to take before the loan is approved.\(^{36}\) “Prior actions could include . . . adjustment of the exchange rate . . . [and] elimination of price controls.”\(^{37}\) (2) Performance Criteria: these are specific conditions that have to be met for the agreed amount of credit to be disbursed.\(^{38}\) These could be both quantitative (“macroeconomic policy variables such as international reserves . . . [and] fiscal balances”\(^{39}\)) and structural (“specific measures to improve financial sector operations . . . or restructure key sectors such as energy” or pensions);\(^{40}\) (3) Structural Benchmarks: these “are used for measures that cannot be monitored objectively enough to be [performance criteria]”;\(^{41}\) and (4) Program Review: this is a monitoring tool for a broad-based assessment by the IMF of the “progress toward the program’s objectives.”\(^{42}\)

The scope of Conditionality was defined by the Guidelines on Conditionality issued by the IMF on March 2, 1979,\(^ {43}\) which provide, inter alia, that

The number and content of performance criteria may vary because of the diversity of problems and institutional arrangements of members. Performance criteria will be limited to those that are necessary to evaluate implementation of the program with a view to ensuring the achievement of its objectives. Performance criteria will normally be confined to (i) macroeconomic variables, and (ii) those necessary to implement specific provisions of the Articles or policies adopted under them. Performance criteria may relate to other variables only in exceptional cases when they are essential for the effectiveness of the member’s program because of their macroeconomic impact.\(^ {44}\)

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34. Id. art. V.
35. Id., art. XXX.
37. Id.
38. Id.
39. Id.
40. Id.
41. Id.
42. Id.
44. Id. at 6.
Therefore, while designing its Conditionality, the IMF was to be guided by two considerations: (1) the conditions must help the member "to solve their balance of payments problems in a manner consistent with" the purposes of the IMF while safeguarding the IMF's resources, and (2) the conditions are only those necessary to achieve those purposes (to prevent intrusion in a member's exercise of its sovereign powers).

Interestingly, "[s]ome element of policy conditionality has been attached to Fund financing since the mid-1950s, but the scope of conditionality has expanded, particularly since the early 1980s," and, more specifically, in the 1990s. Another notable development is the expansion of Conditionalities in the structural area, as demonstrated in the figure below, which was not common in IMF-supported programs earlier.

Average Number of Structural Conditions per Program Year

![Graph showing the average number of structural conditions per program year from 1987 to 1999.](source: International Monetary Fund)

The proliferation in structural Conditionalities extended from macro-critical to other areas as well. The exchange and trade-related Conditionalities saw a steady decline from 1987-90 to 1997-99 and capital account related Conditionalities started to increase from 1991-93. The fiscal sector and financial sector saw the bulk of structural conditions and privatization and systemic reform-related Conditionalities continued to grow steadily from 1991 to 1999 (see figure below).

45. Id. at 8.
46. Id.
47. Conditionality in Fund-Supported Programs—Overview, supra note 27.
48. Id. Fig. 1.
49. Id.
Distribution of Structural Conditions by Economic Sector (as percentage of total Structural Conditions)\textsuperscript{50}.

![Graph showing distribution of structural conditions by economic sector](image)

Source: International Monetary Fund

The IMF attributed the proliferation in the structural conditions to (1) its realization that the monetary and fiscal policy objectives key to macroeconomic adjustments for sustainable economic growth are themselves dependent on structural conditions, and (2) its involvement in alleviation of structural imbalances in low-income countries, crisis-hit countries in Asia, and the transition economies of Eastern Europe.\textsuperscript{51}

In a nutshell, the IMF, by its Articles of Agreement, has jurisdiction over current account transactions of its member countries. It is not empowered to require opening up of the capital account by its member countries. The only exception is article VI, section 3, which cautions that a member country may not regulate its international capital movements in a manner that restricts payments for current transactions, such as those that may lead to distortion in exchange rates. But capital account Conditionality came into play from 1991 to 1999. Albeit small in its dispersion relative to other structural conditions, its potency was acutely felt during the Asian Financial Crisis in 1997-98. While the proliferation in structural Conditionalities by the IMF was justified in response to changing market conditions, it remains a moot point if these were minimum conditions necessary for provision of financing by the IMF as required by the 1979 Guidelines, or if they contained policy prescriptions for the member countries that went beyond the IMF’s mandate.

\textsuperscript{50} Id. Fig. 3.

\textsuperscript{51} Id.
III. CAPITAL ACCOUNT CONVERTIBILITY IN THE ASIAN FINANCIAL CRISIS

Through the medium of Article IV Consultations and the Conditionalties, the IMF requires a member country to take action on issues that impact macro-economic performance (interest rates, money, credit, inflation, exchange rates, and balance of payments etc.) and financial sector development (including regulation and supervision of financial institutions). While doing this, the IMF is required to take into account the domestic social policies, political policies, and the circumstances of member countries. This makes for an interesting review in the context of the Asian Financial Crisis of 1997-98. It is by now well-documented that liberalization of the capital account in the affected Asian countries was premature, i.e. neither "well sequenced nor accompanied by . . . [a] strong prudential supervision of the financial system,"52 thereby leaving these economies vulnerable. In fact, "[t]he vulnerabilities of the economy to external events stemming from weaknesses in the corporate and financial sectors were not fully recognized."53 In other words, ill-timed capital account liberalization, irrespective of the readiness of the economy, resulted in deceptively large inflows of foreign capital—both short-term and reversible. This shielded the fundamental underlying problems, which eventually caused a shift in the foreign investor sentiment, triggering massive capital outflows and resulting in tragic economic and social losses across Asia.54 Yet, the IMF's Conditionality for assistance was, inter alia, a further and unrestricted opening of the capital account in the hardest hit Asian Crisis countries—Korea, Thailand, and Indonesia.55

A. KOREA

Until the financial crisis in 1997, Korea had experienced a long period of rapid growth, which transformed it into an advanced industrial economy. But the Korean government had begun an economic reform program, which gained momentum in 1993-96, to gradually liberalize financial markets and the capital account. In its 1997 Annual Report, the IMF summarized its Article IV Consultations with Korea by stating that: "The fiscal situation in Korea remained sound as the result of a long tra-

53. Id.
54. I am not suggesting that other factors such as political issues, bad governance, and lack of transparency in financial and economic data were not also responsible. See generally IMF, The IMF's Response to the Asian Crisis (Jan. 1999), available at http://www.imf.org/external/np/exr/facts/asia.htm.
55. This paper does not seek to ascertain the causes of the Asian Financial Crisis nor the adequacy of the IMF response. Much has already been said and written about it. The focus is on the IMF's handling of its Conditionality of capital account convertibility.
dition of fiscal conservatism." The report also stated that directors of the fund welcomed the recent acceleration of capital account liberalization; although some Directors agreed with the authorities' gradual approach to capital account liberalization, a number of Directors considered that rapid and complete liberalization offered many benefits at Korea's stage of economic development. Directors agreed with the authorities' intention of not rigidly linking capital account liberalization to the narrowing of interest differentials with partner countries and noted that liberalization itself would be important in reducing Korean interest rates from the current high levels.

It is pertinent to note, however, that the acceleration of capital account liberalization hastened portfolio investments and short-term inter-bank debt over long term foreign direct investment. In fact, in the few years leading up to the crisis, movement of foreign direct investment vis-à-vis the inflow of "hot money" makes a very interesting comparison:

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<tr>
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<tbody>
<tr>
<td>Direct investment</td>
<td>-0.5</td>
<td>-1.3</td>
<td>-1.9</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Portfolio investment</td>
<td>10.7</td>
<td>6.8</td>
<td>8.5</td>
<td></td>
<td></td>
</tr>
<tr>
<td>External Debt (% of GDP)</td>
<td>13.3</td>
<td>14.7</td>
<td>17.2</td>
<td>32.5</td>
<td>34.9</td>
</tr>
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Source: The International Monetary Fund*  

High domestic interest rates (to maintain dollar-pegged exchange rates) attracted inflow of short-term foreign capital. Borrowings from the foreign markets, made possible by relaxation in capital account restrictions, financed the overzealous domestic credit expansion and led Korea to become highly leveraged. Loan defaults by the Korean conglomerates triggered a loss of confidence leading to large outflows, depleting foreign reserves, and raising the specter of sovereign bankruptcy.

The IMF stepped in with a package of economic reforms manifest in various Letters of Intent that provided for, inter alia, macro-economic, fiscal, and financial sector measures; for example: restructuring of finan-

57. Id. at 60.
58. See Press Release, IMF Concludes Article IV Consultation with Korea, supra note 52.
cial sector and large conglomerates, debt workouts, etc; accommodation of larger fiscal deficits to provide for financial restructuring, recession, and to allow for higher expenditure on the social safety program and unemployment benefits; and capital market development through privatization of government enterprises. Among others, the trade and capital account liberalizations required of Korea at the time of the crisis were:

- **Trade liberalization measures:** these included setting a timetable in line with WTO commitments to eliminate trade related subsidies and import diversification programs; and permitting foreigners to engage in securities dealings, insurance, leasing, property-related businesses and in deep sea foreign transport.

- **Capital account liberalization measures:** these included permitting foreign investment without restriction in domestic money, equity, and bond markets; removal of sectoral caps on foreign direct investment in various sectors such as newspapers, periodicals, and telecom; increasing the range and amounts of financial instruments available to foreign investors; permitting foreign financial institutions to participate in mergers and acquisitions of domestic financial institutions; permitting foreign banks to purchase equity in domestic banks without restriction; and abolishing restrictions on foreign ownership of land and real estate properties.61

In other words, while indeed providing macro-economic, fiscal, and financial relief, the IMF appeared to be leveraging its position to extract capital account concessions beyond its mandate enshrined in its Articles of Agreement. The argument that these concessions would make foreign investors return to Korea is plausible, but at the same time highly speculative and debatable under the circumstances.

### B. Thailand and Indonesia

Stepping back to Thailand in 1997, the Thai baht was coming under a series of speculative attacks with foreign investors who were losing confidence in the economy. In Thailand, the combination of a fixed exchange rate, an increasingly open capital account, and high domestic interest rates to combat inflation attracted short-term capital flows that left the economy vulnerable to sudden shifts in market sentiment and external shocks.62 The IMF’s program policies for Thailand kept evolving in response to the worsening crisis.63 At its core was the comprehensive restructuring of the financial sector, the strengthening of the fiscal position, and the strengthening of the legal and institutional framework for corporate debt restructuring. Other policies were supportive of external cur-

61. See id.
rent account adjustment, strengthening of the social safety net, and structural reforms—notably civil service—and further opening of Thailand’s economy to foreign investment through privatization and the conversion of the Alien Business Law into a new and more liberal foreign investment law.

The shift in market sentiment in Thailand also exposed structural weaknesses in Indonesia’s economy, notably the large amount of short-term foreign debt owed by the private corporate sector. Indonesia, unlike Korea, had already liberalized extensively on the capital account. Rapid expansion of the financial system since the late 1980s had left a number of banks with significant amounts of non-performing loans, straining their liquidity and undermining their financial viability. Also, the relative stability of the Indonesian rupiah during most of the 1990s, together with the high rates of return on domestic investment, both encouraged and facilitated high levels of unhedged overseas borrowing, a significant portion that was private short-term debt. “Consequently, by end-June 1997, Indonesia’s external debt had increased to $140 billion (about 60 percent of GDP), of which $33 billion was short term.”

The IMF’s program for economic reform in Indonesia provided for the macro-economic, fiscal, social, and financial sector measures to stabilize the economy. Some measures, however, merit additional scrutiny, such as cancellation of several infrastructure projects and controversial discontinuation of the airplane and national car projects. The IMF also sought the elimination of existing foreign ownership restrictions on banks, the further liberalization of foreign trade and investment, the dismantling of domestic monopolies, and the expansion of the privatization program. Trade measures included reduction in, or phasing out of, tariffs and quantitative import restrictions, and other non-tariff barriers that protect domestic production. For example, consistent with Indonesia’s commitment to the WTO, the local content program for motor vehicles, which gives preferential tariff rates to vehicle manufacturers using a high percentage of local parts, was to be phased out by 2000. The list of activities open to foreign investors was to be further expanded and the restrictions were to


66. Ostensibly to conserve government expenditure.
be removed in the wholesale and retail sector.67

The IMF’s relentless pursuit to extract capital account concessions at the time of the crisis does appear opportunistic. The virtually coercive requirement of large scale liberalization of trade and investment policies (which otherwise were part of the WTO framework) and the unrestricted opening of the capital account imposed by the IMF, irrespective of their local conditions in these countries, not only exceeded its mandate under its Articles of Agreement, but also made the developing world question the IMF’s agenda at the time of the crisis.

At the 1997 Annual Meeting of the Interim Committee (as it was then called) of the Board of Governors, the IMF toyed with the idea of an amendment to the Articles of Agreement to include liberalization of capital movements as one of the purposes of the IMF, or at least to have an express power to impose capital liberalization as an IMF Conditionality.68 A further emphatic pitch to attribute the Asian Financial Crisis to improper sequencing of capital account liberalization (and not capital account liberalization per se) was made by Michel Camdessus, Managing Director of the IMF in March 1998,69 but with Asian countries sinking further in a downward spiral the matter was put on a back burner.

The IMF was instrumental in restoration of investor confidence in the affected countries under the umbrella of its bailouts, which amounted to U.S. $36.3 billion for Korea, Thailand, and Indonesia. The IMF also spearheaded the mobilization of U.S. $81.6 billion of additional financing from multilateral and bilateral sources in support of these reform programs. But scars of its excesses ran deep—the IMF pushed too far beyond its mandate, ostensibly at the behest of its major stockholders, and its credibility as a guardian of the international monetary system was at an all time low in the developing world.

IV. WASHINGTON CONSENSUS; MONTERREY CONSENSUS

Admittedly he who pays the piper calls the tune, but a multilateral financial institution charged with maintaining stability in the international payment systems cannot sustain the cooperation of the changing world order if it continues to be perceived as owing allegiance to its major stockholders. Through the 1990s, the IMF’s economic medicine for the developing world was a standard prescription: remove barriers to foreign investment, remove capital account restrictions, liberalize financial sector, and privatize. The roots of this ran deep into the Washington Consensus in 1989. A series of crises followed, but it was not until the IMF’s poster

child, Argentina, collapsed in 2001 that the IMF sought to review its practice of Conditionalities against the backdrop of immense negativity surrounding its operations. The Monterrey Consensus in 2002 provided the IMF with an opportunity to regain its credibility. But clearly more needs to be done.

A. Washington Consensus

Briefly, the Washington Consensus was a set of policy prescriptions for fostering economic growth in Latin America, summarized as follows:

- Fiscal discipline;
- A redirection of public expenditure priorities toward fields offering both high economic returns and the potential to improve income distribution, such as primary health care, primary education, and infrastructure;
- Tax reform (to lower marginal rates and broaden the tax base);
- Interest rate liberalization;
- A competitive exchange rate;
- Trade liberalization;
- Liberalization of inflows of foreign direct investment;
- Privatization;
- Deregulation (to abolish barriers to entry and exit); and
- Secure property rights.70

John Williamson, from the International Institute of Economics, who is credited with coining the phrase “Washington Consensus,” meant the phrase to refer to the lowest common denominator of policy advice being addressed by the Washington-based institutions to Latin American countries as of 1989.71 But this later morphed into a neo-liberal movement and became the IMF’s mantra for the rest of the developing world.72 The IMF’s actions during the Asian Financial Crisis regarding Korea, Thailand, and Indonesia strongly hint at indiscriminate implementation of policy prescriptions of the Washington Consensus.

B. Negativity

It is virtually impossible to capture the width of criticism faced by the IMF but this section will provide a flavor.

It is useful to recall the words of Mr. Francois Gianviti, former General Counsel of the IMF:

The drafters of the Fund’s Articles were ambitious but they were also realistic. After the end of World War II, an immediate priority was the resumption of multilateral trade, which required a liberalization of current payments, but a premature liberalization of capital movements could have undermined the fragile post-war economies.

70. Latin American Adjustment, supra note 1, ch. 2.
71. Williamson, supra note 1, at 251.
72. Id.
Therefore, the sovereignty of members with respect to exchange controls on capital movements was preserved; restrictions on capital movements could be imposed without Fund approval.73

But after four decades of stabilization, the IMF and its major stockholders apparently thought it fit to require premature liberalization of capital accounts in other fragile developing countries. In fact, Budhoo Davison, who resigned as senior manager at the IMF in 1989 after twelve years service, stated:

President Reagan effectively told us to go out and make the Third World a bastion of free-wheeling capitalism... Everything we did from 1983 onward was based on our new sense of mission to have the 'south' privatize or die; towards this end we created economic bedlam in Latin America and Africa in 1983-88.74

Since the Asian Financial Crisis, the criticism of the IMF has been even more scathing, bitter, and unforgiving. Seen as an extension of the U.S. Treasury, the IMF has been considered intrusive and unfair, leveraging its position to push G-5 (or G-7) economic agenda on the developing world.75 The evidence against the IMF is overwhelming: an increase in structural Conditionalities after the Washington Consensus; indiscriminate prescription of liberalization of trade, investment, capital account convertibility, and privatization irrespective of the underlying facts and circumstances; and unfair extraction of extraneous concessions in crisis.

C. Monterrey Consensus; Conditionality Rollback

Many a crisis later, the International Conference on Financing for Development held in Monterrey, Mexico, in March 2002 had a more benign feel. Its goal was “to eradicate poverty, achieve sustained economic growth and promote sustainable development as we advance to a fully inclusive and equitable global economic system.”76 The Monterrey Consensus sought to build a new partnership between the developed and developing countries, whereby the reforms for globalization were implemented on a mutually beneficial basis and with a better comprehension of the issues faced in the developing countries.

Thereafter, in September 2002, the IMF revised its Conditionality

73. Gianviti, supra note 69, at 1375.
75. Dr. Walden Bello, Professor of Sociology and Public Administration at the University of Philippines, has been a staunch critic. See generally, Walden Bello, The Future in the Balance, Acceptance Speech at the Right Livelihood Award Ceremonies, Swedish Parliament, Stockholm (Dec. 8, 2003), available at http://www.international.ucla.edu/asia/article.asp?parentid=5008.
Guidelines\textsuperscript{77} with the objectives of sharply focusing on macroeconomic and financial sector policies based on principles of parsimony, criticality, and necessity; being less intrusive into countries' policy choices; requiring country ownership of policy programs; and having due regard to the social and political objectives, economic realities, and circumstances of the member countries.\textsuperscript{78} In particular:

Conditions will normally consist of macroeconomic variables and structural measures that are within the Fund's core areas of responsibility. Variables and measures that are outside the Fund's core areas of responsibility may also be established as conditions but may require more detailed explanation of their critical importance. The Fund's core areas of responsibility in this context comprise: macroeconomic stabilization; monetary, fiscal, and exchange rate policies, including the underlying institutional arrangements and closely related structural measures; and financial system issues related to the functioning of both domestic and international financial markets.\textsuperscript{79}

Subsequently, the IMF's de facto mission of seeking capital account convertibility in the developing world was modified to promote and support the gradual and orderly liberalization of the capital account with due regard to the domestic macro-economic, fiscal, social, and political factors.

To the extent that the 2002 Guidelines have, in fact, been implemented is outside the scope of this paper, but Mr. P. Chidambaram, Finance Minister for the Government of India, in his speech to the International Monetary and Finance Committee of the IMF on April 16, 2005,\textsuperscript{80} strongly hinted at the developing world's continuing discontent with the IMF, stating:

- [The] Fund's insistence on the pursuit of sound policies and institutions in low income countries should be grounded on the right premises. The primary focus of Fund support to low-income countries should be based on its core area of expertise, namely helping them establish and maintain macroeconomic and financial stability.
- It would be premature to bring capital account liberalization as a central focus of the Fund, on par with current account transactions.
- [I]t is also felt that the Fund is becoming increasingly intrusive in its approach and using surveillance as an instrument to rate country


\textsuperscript{79} Id.

performance, thereby subordinating its primary role of a confidential advisor and the co-operative principles underlying its existence.

- [T]he ‘proliferation’ of Fund conditionality into areas outside the Fund’s core responsibilities based on the notion of ‘everything depends on everything else’ must be eschewed.
- [T]he prerogative of the Fund to protect its own resources, when its portfolio is highly exposed to a few select debtor members and should not be construed to justify the dilution of the principles of ‘criticality’, ‘parsimony’ and ‘clarity’ to the old ‘everything depends on everything else’ norm.\(^8^1\)

D. Regaining Credibility

Disconnects between the IMF and the developing countries are several and fundamental. The IMF's decision-making has always been dictated by the political and economic agenda of its major stockholders, with the United States, the United Kingdom, France, Germany, and Japan collectively cornering 39.1 percent of the voting power.\(^8^2\) While the IMF's operations have evolved and adapted since 1945 to new developments in the global economy, the institutional arrangements for decision-making still remain heavily weighted in favor of the developed countries.\(^8^3\) Biases in representation and voting power linked to quota contribution will therefore continue to impinge on the IMF's neutrality. As long as the IMF reflects the exclusive will of its major stockholders, it is unlikely to gain willing acceptance in the developing world. With the emergence of Brazil, Russia, India, and China,\(^8^4\) the changing world order will look for and establish alternative fund systems in due course of time.

It would therefore be expedient for the IMF to fundamentally review its governance structure. It could possibly follow the intrinsic U.S. corporate model (separating ownership from management) and de-link its governance from contributions of the member countries so that the management, as fiduciaries, could maximize decision-making and value in an unbiased manner for its member countries. It could further look at raising financing from the global capital markets instead of relying completely on the contribution of its members. The IMF could also look at the creation of regional sub-funds, partly capitalized by the countries in the region, and partly by accessing global financial markets. This way

\(^{8^1}\) Id.
\(^{8^3}\) See generally Statement by Honourable Finance Minister Mr. P. Chidambaram, supra note 81.
\(^{8^4}\) See Roopa Purushothaman & Dominic Wilson, Dreaming With BRICs: The Path to 2050, GLOBAL ECONOMICS PAPER No. 99 (Oct. 1, 2003), available at http://www.gs.com/insight/research/reports/99.pdf (BRIC economies, Brazil, Russia, India, and China, together could be larger than the G6 in U.S. dollar terms. By 2025 they could account for over half the size of the G6. Of the current G6, only the United States and Japan may be among the six largest economies in U.S. dollar terms in 2050).
there will be greater ownership among the heterogeneous group of countries within the region to resolve local issues that they have a far better understanding of. Regional funds and member countries will have the discretion to tap the IMF's immense reservoir of expertise in its core areas of responsibility. Either way, once an equitable governance structure is established, the IMF could look at expanding its articles to include international capital movements as part of the Fund Conditionality.

V. CONCLUSION

The IMF has a mandate to maintain a stable international monetary system and has oversight of the current account transactions of the member countries under its existing Articles of Agreement. But it has felt compelled to control international capital movements. It is undeniable that since Bretton Woods, global investment has become a major fuel for economic growth, and capital movements have an equally strong impact on balance of payments in any country. Additionally, most developing countries will not dispute the developmental advantages of a decentralized, deregulated, and private sector ordering. But it is for the respective countries to choose their pace of development consistent with domestic social objectives and economic realities, and that the IMF cannot possibly sit in judgment.

The stellar job done by the IMF since its inception was sullied by its biased and indiscriminate operations in the 1990s (and even earlier in the 1980s). The IMF's unrelenting obsession with capital account convertibility created foundation conditions for crisis after crisis in the developing world. Its package of reforms for countries hit by crises went beyond the macro-economic and financial sector remedies permitted under its Articles of Agreement. The IMF's justification that some strong structural measures were required to restore the confidence of the international investment community in these countries is meritorious, but was tainted by its opportunistic procurement of trade and capital account concessions for and on behalf of its major stockholders. The contagion looming large from a decade of continuing crises finally jolted the international financial community. In 2002, the IMF eventually concluded that capital account liberalization had to be a gradual process accompanied by an appropriate macro-economic framework, a strong and transparent domestic financial system, and sound structural policies.

The emerging markets are now strong drivers of growth in the world economy and have begun grumbling about the inequitable representation and governance at the IMF. The developing world will always see the IMF as playing the G-7 tune and are unlikely to forget the havoc caused by the decade of crises around the world. In the spirit of the Monterrey Consensus, it would be expedient for the IMF to restructure its governance to reflect the voice of both the developed and developing world. Thereupon it can, and it should, gain de jure, additional oversight of the international capital movements.
Comparative Perspective