Chapter 5

INTERNATIONAL INSTITUTIONS

Article 5.1

THE INTERNATIONAL MONETARY FUND AND WORLD BANK

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March/April 2000, last revised December 2016

The basic structure of the postwar international capitalist economy was created in 1944, at an international conference in Bretton Woods, New Hampshire. While the Bretton Woods conference included high-level negotiations between representatives of the U.S. and British governments, the Americans dominated the outcome.

The British delegation (including the legendary economist John Maynard Keynes) argued for an international currency for world trade and debt settlements. The Americans insisted on the U.S. dollar being the de facto world currency, with the dollar's value fixed in terms of gold and the values of other currencies fixed in relation to the dollar. The British wanted countries that ran trade surpluses and those that ran trade deficits (and became indebted to the "surplus" countries) to share the costs of "adjustment" (bringing the world economy back into balance). The United States insisted on a system in which the "deficit" countries would have to do the adjusting, and a central aim would be making sure that the debtors would pay back their creditors at any cost.

Among the institutions coming out of Bretton Woods were the World Bank and the International Monetary Fund (IMF). For this reason, they are sometimes known as the "Bretton Woods twins." Both institutions engage in international lending. The IMF was established to lend to countries facing current-account deficit problems, so that they could continue international trade without interruption, and avoid defaulting on debts, which would disrupt world economic stability. So the IMF primarily acts as a "lender of last resort" to countries (usually, but not always, lower-income countries) that have become heavily indebted and cannot get loans elsewhere. The World Bank, officially called the International Bank for Reconstruction and Development, was initially tasked to help rebuild post-World War II Europe through infrastructure lending. In the years since, it has continued to engage primarily in longer-term "development" lending, though its focus has moved to the developing world.

At both the World Bank and the IMF, the number of votes a country receives is closely proportional to how much capital it contributes to the institution, so the voting power of rich countries like the United States is disproportionate to their numbers. Eleven rich countries, for example, account for more than 50% of the voting power in the IMF Board of Governors. At both institutions, eight powerful countries—the United States, China, France, Germany, Japan, Russia, Saudi Arabia, and the United Kingdom—get their own representatives on the institution's executive board, with the rest of the directors (16-17) elected by the rest of the 180-odd member countries. The president of the World Bank is elected by the Board of Executive Directors, and traditionally nominated by the U.S. representative. The managing director of the IMF is traditionally a European.

The IMF and the World Bank wield power vastly greater than the share of international lending they account for because private lenders follow their lead in deciding which countries are credit-worthy. The institutions have taken advantage of this leverage—and of debt crises in Latin America, Africa, Asia, and even Europe—to push a "free-market" (or "neoliberal") model of economic development.

The IMF

The IMF was a key part, from the very start, of the "debtor pays" system the U.S. government had insisted on at Bretton Woods. When a country fell heavily into debt, and could no longer get enough credit from private sources, the IMF would step in as the "lender of last resort." This made it possible for the debtor to continue to pay its creditors in the short run. The typical IMF adjustment program, however, demanded painful "austerity" or "shock therapy"—elimination of price controls on basic goods (such as food and fuel), cuts in government spending, services, and employment, and "devaluation" of the country's currency. All of these austerity measures hit workers and poor people the hardest, the first two for fairly obvious reasons. The impact of currency devaluation, however, requires a little more explanation.

Devaluation meant that the currency would buy fewer dollars—and fewer units of every other currency "pegged" to the dollar. This made imports to the country more expensive. (Suppose that a country's peso had been pegged at a one-to-one ratio to the dollar. An imported good that cost $10 would cost 10 pesos. If the currency was devalued to a two-to-one ratio to the dollar, an imported good that cost $10 would now cost 20 pesos.) Devaluation caused domestic prices to rise, both because imports became more expensive and because domestic producers faced less import competition and so could more readily raise their own prices. Meanwhile, it made the country's exports less expensive to people in other countries. The idea was that the country would export more, earn more dollars in return, and—this is the key—be able to pay back its debts to U.S. and European banks. In other words, the people of the country (especially workers and the poor) would consume less of what they produced, and send more of it abroad to "service" the country's debt.

It is the poor who are hurt the most by devaluation. For instance, if a county's devalues its currency by 50%, then the poor will lose about half the purchasing power on their money savings (which they hold overwhelmingly in the national currency). However, the rich and ruling elite hold the bulk of their financial wealth abroad in other currencies. Once a devaluation has been carried out, they can use their foreign currency holdings to buy their country's currency, now at a more favorable rate due to the devaluation.

For many years, austerity measures like these were the core of IMF "adjustment" plans. Starting in the 1970s, however, the IMF broadened its standard program to include deeper "structural" changes to debtor countries' economies. "Structural adjustment programs" (SAPs) included not only the austerity measures described above, but also the elimination of trade barriers and controls on international investment, the privatization of public enterprises, and the "deregulation" of labor markets (including elimination of minimum wage laws, hours laws, occupational safety and health regulations, and protections for unions).

These were the basic ingredients for overturning "regulated" (or "interventionist") forms of capitalism in many lower-income countries, and replacing it with "free-market" (or "neoliberal") capitalism. Austerity, privatization, and deregulation kept the same elite-dominated government and bureaucratic institutions in place, while moving the epicenter of economic decisionmaking away from public institutions and into private hands. The fact that economic development was now under the control of private corporations—with their power over basic resources such as water, food, and energy—meant that the populations of these countries had still *less* way to hold elites accountable than they had before.

Structural adjustment also prepared the ground for the system of globalized production—making it easier for multinational companies to locate operations in affected countries (thanks to the removal of restrictions on foreign investment), employ a relatively cheap and controllable workforce (thanks to the removal of labor regulations), and export the goods back to their home countries or elsewhere in the world (thanks to the elimination of trade barriers). Structural adjustment programs became the lance-point of "free-market" reform, especially in Latin America during the 1980s debt crisis, but also in other low-income regions.

The World Bank

In its early years, just after World War II, the World Bank mostly loaned money to Western European governments to help rebuild their war-ravaged economies. This was an important factor in the postwar reconstruction of the world capitalist economy. European reconstruction bolstered demand for exported goods from the United States, and ultimately promoted the reemergence of Western Europe as a global manufacturing powerhouse.

During the long period (1968-1981) that former U.S. Defense Secretary Robert S. McNamara headed the World Bank, however, the bank turned toward "development" loans to lower-income countries. McNamara brought the same philosophy to development that he had used as a chief architect of the U.S. war against Vietnam: big is good and bigger is better. The World Bank came to favor large, expensive projects regardless of their appropriateness to local conditions, and with little attention to environmental and social impacts. The Bank became especially notorious, for example, for supporting large dam projects that flooded wide areas, deprived others of water, and uprooted the people living in affected regions. The Bank's support for large, capital-intensive "development" projects has also been a disguised way of channeling benefits to large global companies. Many of these projects require inputs—like high-tech machinery—that are not produced in the countries where the projects take place. Instead, they have to be imported, mostly from high-income countries. Such projects may also create long-run dependencies, since the spare parts and technical expertise for proper maintenance may only be available from the companies that produced these inputs in the first place.

While the Bank's main focus is long-term "development" lending, it has also engaged in "structural adjustment" lending. The Bank's structural adjustment policies, much like those from the IMF, have imposed heavy burdens on workers and poor people. In the 1980s and 1990s, during its "structural adjustment era," the Bank went so far as to advocate that governments charge fees even for public primary education. (Predictably, in countries that adopted such policies, many poor families could not afford the fees and school enrollment declined.) The Bank has since then publicly called for the abolition of school fees. Critics argue, however, that the shift is at least partly rhetorical. Katarina Tomasevski, founder of the organization Right to Education, argues that the Bank presents itself as opposing fees, but does not oppose hidden charges, as for textbooks, school uniforms, and other costs of attending school.

The World Bank has also made development loans conditional on the adoption of "free-market" policies, like privatization of public services. Most notoriously, the Bank has pushed for the privatization of water delivery. Where privatization of water or other public services has not been possible, the Bank has urged governments to adopt "cost-recovery" strategies—including raising fees on users. Both privatization and cost-recovery strategies have undermined poor people's access to water and other essentials.

Recent developments

Since the 1990s, opposition to World Bank and IMF policies have shaken the two institutions' credibility and economic policy influence—especially in Latin America, the world region to which "neoliberalism" came first and where it went furthest. This is part of a broader backlash against neoliberal policies, which opponents (especially on the Latin American left) blame for persistent poverty and rising inequality in the region. The 1990s and 2000s saw a so-called "pink tide" in Latin America, with "center-left" parties coming to power in Argentina, Bolivia, Brazil, Chile, Ecuador, and Venezuela. (The center-left has since lost and then regained the presidency in Chile, and has recently lost the presidencies of Argentina and Brazil.) Different governments have adopted different policies in power, some staying close to the neoliberal path, others veering sharply away from it. Venezuela has, along with several other countries, withdrawn from the World Bank-affiliated International Centre for the Settlement of Investment Disputes (ICSID). Several South American governments, including those of Argentina, Brazil, and Venezuela, have also jointly formed a new regional lending institution, the Bank of the South, which aims to act as an alternative lender (for both long-term development and short-term "liquidity crises") to the IMF and World Bank.

On the other hand, the IMF has emerged, surprisingly, as a powerful influence in Western Europe. For many years, acute debt crises seemed to be confined to lower-income economies, and most observers did not dream that they could happen in Europe or other high-income regions. (For this reason, the IMF was widely criticized as a hammer that high-income countries used on low-income countries.) During the current economic crisis, however, several Western European countries have fallen deeply into debt. The IMF has stepped in as part of "bailout" programs for Greece, Iceland, and Ireland. True to its origins, it has also pushed for austerity—especially cuts in public spending—in highly indebted countries. Many economists—especially proponents of "Keynesian" views—have argued that weakness in total demand is the main cause of the current economic crisis in Europe and the rest of the world. Under these conditions, they argue, cuts in government spending will only reduce total demand further, and likely cause the crisis to drag on. ❑

Sources: International Monetary Fund, "IMF Members' Quotas and Voting Power, and IMF Board of Governors" (www.imf.org); International Monetary Fund, "IMF Executive Directors and Voting Power" (www.imf.org); World Bank, "Executive Directors and Alternates" (www.worldbank.org); World Bank, "Cost Recovery for Water Supply and Sanitation and Irrigation and Drainage Projects (www.worldbank.org); Zoe Godolphin, "The World Bank as a New Global Education Ministry?" Bretton Woods Project, January 21, 2011 (www.brettonwoodsproject.org); Katerina Tomasevski, "Both Arsonist and Fire Fighter: The World Bank on School Fees," Bretton Woods Project, January 23, 2006 (www.brettonwoodsproject.org); Katerina Tomasevski, "Six Reasons Why the World Bank Should Be Debarred From Education," Bretton Woods Project, September 2, 2006 (www.brettonwoodsproject.org).