



The IMF's Disappointing "Reforms"

Morris Goldstein doubts that the Fund's attempt to reduce the stigma attached to its programs and expand lending for developing countries will accomplish either goal.

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Steve Weisman: This is Steve Weisman at the Peterson Institute for International Economics. Morris Goldstein, our guest today on Peterson Perspectives, has proposed a series of reforms to the international financial system to meet the global economic crisis. Today we're going to talk about those reforms as they relate to the International Monetary Fund. Thanks for joining us, Morris.

Morris Goldstein: Delighted to be here, Steve.

Steve Weisman: Morris, there's a consensus that the IMF needs to be reformed, that it has a stigma in the eyes of some of the countries that have bad memories of their experience with the IMF in the last crisis of a decade and more ago. What is your understanding of what the IMF is trying to accomplish with its announcement this week to change some of its lending practices?

Morris Goldstein: Steve, I think, given the crisis, they'd like more countries to come into the fund to borrow, and they'd like them to come in at an earlier stage when their difficulties aren't quite so severe. And in order to induce them to do that, they've in effect sweetened the terms of their lending.

Steve Weisman: Is this a good idea? Do they need to do that?

Morris Goldstein: They certainly need to do something. For example, in the late 1990s, they had a new facility to help countries facing large drops in inflows. They created this new facility, which was going to be easier in some ways to use than others, with less conditionality. But no one showed up to use it. Then a year ago, they created a successor to the original, one called the "Short-term Lending Facility" and they tried to make that attractive, and again no one came. And so this time they're making further modifications, not only to the facility for countries affected by decreases in capital flows, but more generally.

Steve Weisman: We have a global financial crisis. A lot of countries are facing insolvency. Where are they turning, if not to the IMF? Or are they just kind of frozen in the headlights?

Morris Goldstein: The most desperate ones—that is, the ones that really have no place else to go—are in fact turning to the Fund. But the thought is that there are many others who could use the Fund profitably. If they don't use the Fund, then what they tend to do is cut way back on government budgets. They tend to squeeze demand and try to deal with the crisis on their own. In some cases, they can get money from regional groups, but often not enough. So the worry is, if they don't come to the Fund, the adjustment will either have to be too sharp or they'll adjust in ways that aren't good for the world economy via protectionism and other things.

Steve Weisman: So what the Fund is trying to do may seem like a good idea, but in your analysis of the proposals, are they in fact good ideas? Do they make sense?

Morris Goldstein: I thought the reforms that they announced in the past few days were on the whole very disappointing, and let me explain why. One of the key problems we're facing in this crisis is that exports are declining everywhere by almost unprecedented rates, and this is so in a vast array of developing countries.

One of the things we needed is a lending window to deal with these dramatic declines in exports that are really temporary and beyond the control of most developing countries. They're declining because the demand in their export markets is falling. There's also been a problem with trade financing, which is being looked at. The IMF indeed had a facility to deal with temporary shortfalls in export earnings that were beyond countries' control, perfect really for this situation, called the "Compensatory Finance Facility," but they abolished it.

Steve Weisman: That was not what you had advised them to do.

Morris Goldstein: No, it was not. I advised them to expand it and strengthen it to make the access limits larger and to use it. The problem is they really didn't put in place something else that would substitute for it. They created a new facility called the "Flexible Credit Facility," but that is going to be restricted to countries that have the best track records on economic policy. So only a handful of countries will be able to qualify for that. And their standby arrangements, their traditional lending tool, is for conditional lending, so that won't do it either. I think they missed an opportunity to deal with one of the key problems of this crisis. And this is a problem that affects more than a hundred countries. So this was an important missed opportunity.

Steve Weisman: I take it you're worried that because of this missed opportunity we may be headed into bad practices as you mentioned before: retrenchment, protectionism. Will we be seeing that in the coming weeks even before the G-20?

Morris Goldstein: I think it's a longer-term process, but certainly, you wanted to do something to cushion export receipts. A second issue, if I could, they've introduced this flexible credit line, which will give countries access based on their past policy performance. So no new conditionality, you qualify based on what you've done in the past. And it has very high access, indeed there's no cap to the amount of money you can get from it.

But the problem is the one you mentioned earlier, Steve. There's a stigma associated with using it. One way to get around that stigma would be to have three or four very creditworthy countries agree to use it right at the outset. That would in a sense reduce the stigma, because people would say, well, if country A with its very good credit history and policies is willing to do it, I can do it also. It won't indicate that I'm in trouble.

Steve Weisman: What countries do you have in mind?

Morris Goldstein: The ones with really the best policy records, the real A-list in emerging economies. That might be a few large countries in Asia, a few in South America, ones with very good debt sustainability, good histories in dealing with crises. And the problem is they weren't able to do so. In fact, right after they announced the new facility, a couple of these economies, including some in Asia, said they weren't going to use it. So in a sense you still have the stigma issue. You can increase the amount of resources that the Fund has available and that's helpful. But it doesn't do you any good if in fact, in the end, countries don't come to borrow.

Steve Weisman: There's been bigger publicity over the question of how widely to expand IMF resources. Is that pointless if they don't accompany that step with these kinds of reforms?

Morris Goldstein: I think expanding the resources is a useful thing to do. We saw Secretary Geithner's proposal to expand the new arrangement to borrow, make it \$450 billion instead of \$50 billion. I think, in general, increasing resources, increasing the access limits, the amount countries could borrow from the Fund, is a good idea. But you have to use that money well and you have to get countries to come in and actually use it beyond the ones that are absolutely the most desperate. And on both those accounts, I think the proposals announced were disappointing.

Steve Weisman: When the G-20 leaders assemble in London at the beginning of April, what will be their reaction to these proposals? What are the chances of their understanding that more needs to be done in this area?

Morris Goldstein: I'm not that encouraged. I mean, in the sense, the same countries, many of the same ones, at least the larger ones, who voted for this in the IMF board a day or two ago will also be at the G-20. So I think, for better or worse, they've agreed to these changes in lending practices in the Fund and I think they'll only revise those based on experience. My worry is that we won't be dealing enough with these export declines, we won't be dealing adequately with the stigma problem, and therefore, a lot of the proposed increase in IMF resources either won't be used or won't be used in the right way.

Steve Weisman: What is the position of the Obama administration on this issue?

Morris Goldstein: It's not perfectly transparent I think. I think they've certainly been in favor of increasing Fund resources, as I am, and of increasing access limits. But I would hope that they feel the same way that I do that something more should have been done to cushion exports. I think there's also a legitimate question about the IMF easing conditionality for countries that have serious policy problems. In that case, we really don't want to ease up on conditionality. We want to make sure that the money is handed out, I think, in stages as the countries do what they promised to do.

Steve Weisman: Do you see the IMF doing some of that with the United States' approval?

Morris Goldstein: Well, that was a part of the lending reform packages on the traditional standby programs, which is the Fund's major lending instrument. They also agreed to soften conditionality there in a number of ways. It'll provide more of the money upfront rather than in stages. They've also agreed to drop performance criteria on structural policies in favor of reviews, which is also a softening.

I think they need a good deal of money for unconditional lending. That's what was supplied by the old compensatory finance facility exporters and they need to keep tough conditionality for the countries whose problems are really of their own making. It's the combination of the two that would be effective. I'm afraid that what we seem to have got was neither one.

Steve Weisman: Looks like they tried to do too many things and ended up doing them all not well.

Morris Goldstein: Well, that's my verdict.

Steve Weisman: Morris, thank you very much for clarifying it and it's always a pleasure to have you on this exchange. Thanks.

Morris Goldstein: Thank you.

