foreign policy
in focus
Interhemispheric Resource Center
and
Institute for Policy Studies

International Financial Institutions

Immediately following World War II, the major capitalist powers, dominated by the U.S. and Britain, met at Bretton Woods, New Hampshire to establish multilateral institutions to manage the postwar restructuring and expansion of the global capitalist economy. Two international financial institutions (IFIs) emerged from the July 1944 meeting: the International Bank for Reconstruction and Development (World Bank) and the International Monetary Fund (IMF).

At first, the IFIs concentrated on the reconstruction of the war-devastated European nations. Soon, however, the U.S. reconstruction effort (known as the Marshall Plan) overshadowed the IFI's own initiatives in Europe, and by the late 1940s the IFIs had shifted their focus to former colonial regions. The integration of the low-income countries (LICs) of the South into the global capitalist market has been the chief objective of the IFIs for nearly a half century. Since the late 1970s the World Bank and IMF have also provided structural adjustment loans (SALs) that are used to support economic reforms.

Key Points

- The integration of the South into the global capitalist market has been the chief objective of the IFIs for nearly a half century.
- As the leading capitalist power, the U.S. sets the direction of IFI lending.
- Because of the increasing inability of countries in the South to meet their debt-servicing schedules, the IFIs have added structural adjustment conditions to their loans.

The IMF was originally designed to monitor the stability of the international financial system by assisting countries experiencing currency-exchange and short-term (3-5 years) balance-of-payments difficulties. When the dollar was delinked from the gold standard in the early 1970s, the original purpose of the IMF was lost, and the organization began acting as a short- and long-term creditor and an economic policy adviser.

The principal function of the World Bank is to provide development loans for projects that are too large or too risky for private banks to finance. Four regional multilateral development banks (MDBs) complement the work of the World Bank: the African Development Bank (AFDB, founded 1963), the Asian Development Bank (ADB-1966), the European Bank for Reconstruction and Development (EBRD-1991), and the Inter-American Development Bank (IDB-1959).

Vol. 1 No. 8
November 1996

The MDBs obtain 80 percent of their funds by tapping world capital markets and the remaining 20 percent by assessing member governments. Most of their loans are near commercial interest rates, although the poorest nations are eligible for low- or no-interest development loans from the World Bank and the regional MDBs. Unlike the MDBs, the IMF depends solely on quota payments from member nations.

Voting in the IFIs is proportional to assessment fees, which means that five Northern powers (U.S., Britain, Germany, France, and Japan) control more than 40 percent of the votes in the World Bank and IMF. The U.S. is the largest contributor to the World Bank, IMF, IDB, and EBRD—holding 17.4, 20, 34.7, and 10 percent respectively of the voting power in those institutions. In the ADB, both the U.S. and Japan have 5.9 percent of the votes.

Actual U.S. influence in the IFIs is much greater than its voting power, mainly because the other capitalist powers do not assume as active a role in daily IFI policymaking and because the U.S. is able to swing votes. As the leading capitalist power, the U.S. sets the direction of IFI lending.

Development and poverty alleviation are stated objective of the MDBs. But the underlying assumption shaping MDB lending is that the expansion and integration of the global financial system and global market are fundamental to economic development. Despite mounting criticism from nongovernmental organizations (NGOs) and LICs, the IFIs never question this assumption. Moreover, they have done little to pursue or evaluate the distributional impacts of their lending operations to ensure that their economic model is effective in reaching their stated goals of development and poverty alleviation.

Since the outbreak of the debt crisis in the late 1970s the IMF and the World Bank no longer have distinct roles. Because of the increasing inability of debtor countries in the South to meet their debt-servicing schedules, the World Bank and a few MDBs added structural adjustment conditions to their loans. The IMF has also played a major role in structural adjustment through increased medium- and long-term lending.

Problems With Current U.S. Policy

After a half century of managing international development and finances, the future direction of the IFIs is unclear. Many critics, citing Northern domination of the IFIs and denouncing their failure to foster sustainable and equitable development, say that "Fifty Years is Enough." Even within the IFIs there exists much skepticism about the practice of forcing LICs to adopt harsh structural adjustment programs in the name of development and financial stability.

Although the U.S. cannot be held directly accountable for the failures, shortcomings, and negative impacts of IFI programs, it does exercise significant influence in the IMF, World Bank, and IDB, and to a lesser extent in the ADB, AFDB, and EBRD. There is daily interaction between U.S. Treasury officials and the staff of the IMF and World Bank, both of which are headquartered in Washington, DC. Additionally, the U.S. president appoints the president of the World Bank and holds effective veto power over the appointment of the IMF director.

As the leader of the global capitalist system, the U.S. sets the direction for IFI development lending, debt relief, and monetary stabilization assistance. The economic stabilization and structural adjustment policies of the IFIs reflect U.S. policy, and the U.S. conditions its own bilateral economic and political aid on the implementation of the stabilization and structural adjustment programs specified by the IFIs. The interactive U.S.-IFI relationship is evident in IFI emergency loans to countries considered critical to U.S. foreign policy objectives, such as the $10 billion loan to Russia immediately prior to the June 1996 presidential election and the IMF loan package of $18 billion to Mexico following the December 1994 peso meltdown.

The main problem with the IFIs and related U.S. policy is that success is measured by narrow and short-term economic objectives, principally low inflation rates, regular flow of debt payments, and small budget deficits. Critical to meeting these objectives are economic reforms—privatization, trade and investment liberalization, prioritizing export production, and austerity social-service budgeting—that disproportionately impact poor people and extend a corporate agenda of global market integration.

The composition of the U.S. policy advisory group on IFI lending reflects the apparent lack of concern about the social and environmental impact of IFI lending and programs. Led by Treasury, the group also includes the secretary of state, assistant to the president for economic affairs, secretary of commerce, chairperson of the Federal Reserve's board of governors, and the president of Eximbank. Not included are government officials and NGO representatives with more knowledge about the politics and economics of broad-based and environmentally sustainable development. The executive directors (officials who directly represent the U.S. before the IFIs) have little or no expertise in LIC issues.

U.S. votes on IFI lending are guided by certain congressionally imposed restrictions. The executive directors are instructed to cast "no" votes or to abstain on loans to countries that attempt to develop nuclear weapons, fail to control narcotics exports, or routinely abuse basic human rights. Unfortunately, these policies are not consistently enforced. Even when the U.S. casts a negative vote or abstains, it often does not use its extensive influence within the IFIs to stop loan proposals from going forward. Moreover, the U.S. has used all its influence to stop loans to countries considered to be its enemies, as in the case of Sandinista Nicaragua (1979-90).

Some U.S. voting restrictions reflect narrow U.S. economic interests, such as the instructions to vote against loans that assist the production of certain commodities, such as citrus and sugar, that could financially harm U.S. agribusiness.

Environmentally, the U.S. talks a good line with the IFIs, but its actions are less commendable. It supported the creation of a Global Environmental Facility (GEF) to be managed in part by the World Bank. But the GEF's goals are largely limited to concerns like global warming and biodiversity that are the chief environmental priorities of the Northern countries. Even so, the U.S. has failed to meet its funding commitments to the GEF (see *In Focus: U.S. Environmental Aid*).

Symptomatic of the rising isolationist sentiment in Congress is the opposition to fully funding the International Development Association (IDA), the concessional loan facility of the World Bank that directs funds to the world's poorest nations. This lack of concern with the plight of the world's poor is also evident in the failure of the U.S. to take a more generous view on multilateral debt relief for the poorest nations (see *In Focus: Confronting Multilateral Debt*).

Key Problems

- The main problem with the IFIs and related U.S. policy is that success is measured by narrow and short-term economic objectives.
- There exists much skepticism about the practice of forcing LICs to adopt harsh structural adjustment programs in the name of development and financial stability.

Foreign Policy in Focus is a joint project of the Interhemispheric Resource Center (IRC) and the Institute for Policy Studies (IPS). It is supported by subscriptions, by financial support from the John D. and Catherine T. MacArthur Foundation, and by various church organizations. *In Focus* internships are available.

Editors
Martha Honey (IPS)
Tom Barry (IRC)

Production
Grant Moser

Communications Director
Erik Leaver (IRC)

Orders and subscription information:
Mail: PO Box 4506
Albuquerque, New Mexico 87196-4506
Phone: (505) 842-8288
Fax: (505) 246-1601
Email: resourcectr@igc.apc.org

Editorial inquiries and information:

IRC Editor
Phone: (505) 388-0208
Fax: (505) 388-0619
Email: resourcectr@igc.apc.org

IPS Editor
Phone: (202) 234-9382/3 ext. 232
Fax: (202)387-7915
Email: ipsps@igc.apc.org

Website: http://www.zianet.com/infocus

Clearly, the IFIs need reform. The widening gap between the North and most of the countries of the South together with the intensifying class polarization within the LICs underline the failure of the IFIs to spark broad economic development. The recent wave of structural adjustment has left impoverished and dysfunctional societies in its wake. The recurring debt crisis is another sign that the IFIs have failed to establish stable economic partners in the South. The IFIs should accept a major degree of responsibility for these problems. As one of the key founders and a leading patron of the IFIs, the U.S. should also acknowledge responsibility for the failures of IFI development policies.

More importantly, the U.S. should use its considerable influence to work with member nations to encourage efforts to restructure and reform the IFIs. The notion of abolishing the IFIs has received some marginal support from groups on the left and the right, but new financing channels would have to be established in their absence to make certain that the LICs have access to development financing.

Key Recommendations

- The U.S. should use its considerable influence to work with member nations to encourage efforts to restructure and reform the IFIs.
- The IFIs should be subject to UN oversight.
- The U.S. should work to redefine the IFIs development assistance strategy, giving greater attention to eliminating the divide between North and South. The economic stabilization and structural adjustment policies of the IFIs reflect U.S. policy.

Reform will be meaningless, however, unless it follows from a new conceptualization of development. In its relations with the IFIs, the U.S. should adopt a more enlightened concept of advancing U.S. national interests. U.S. national interests would be better served by aid policies that help narrow the North-South income gap and promote equitable, environmentally sustainable development than by policies that place a premium on increased procurements by U.S. firms, maintain onerous debt-servicing schedules, and promote economic reforms that mainly benefit local elites and foreign investors and traders.

Global economic progress and political stability—the stated aims of U.S. foreign policy—will not be possible without this commitment to people-centered and environmentally sustainable development. The policy measures recommended below would help the IFIs move toward this new vision:

- The IFIs should be subject to UN oversight. As it is, although the IFIs are technically part of the UN system, they respond almost exclusively to the interests of Northern donors. Bringing these Bretton Woods institutions under the umbrella of the UN would enable LICs to help set the policy direction of the IFIs.
- The U.S. should work with other shareholder governments to redefine IFI development assistance strategy, so as to give greater attention to eliminating the divide between North and South. The U.S. should urge the IFIs to seek local input, offer appropriate infrastructure investments, promote end-use efficiency, provide integrated resource planning, and support sustainable agriculture practices.
- The U.S. should act to separate the functions of the IMF and the MDBs by calling for an end to the IMF's involvement in long-term development through its medium- and long-term structural adjustment programs. The IMF, which does not have the capacity to serve as a development institution, needs to focus on technical advice and short-term balance-of-payment support. It should be the task of the MDBs to promote long term sustainable development and alleviate poverty. Dramatic reform of MDB-led adjustment programs is crucial to ensure that these institutions effectively concentrate on improving socioeconomic conditions in the South.
- The U.S. should support immediate and extensive multilateral debt relief for the 41 most severely indebted nations. This debt reduction should not be subject to implementation of the current type of structural adjustment programs.
- The U.S. should encourage the MDBs to search for ways to keep development funds in the South. As it is, Northern domination of capitalist development is evident in IFI procurement practices: nearly 70 percent of all IFI disbursements flow to the North in the form of purchase agreements and consulting contracts. Directing MDB funding to low-technology, people-centered development projects would enable more of the supplies and consulting fees to stay in the South and within the target communities.
- U.S. restrictions on loan approvals to countries with systematic human rights violations should be consistently enforced. In this regard, the U.S. should use not only its voting power but also its influence over loan formulation and review. Moreover, the U.S. should encourage the IFIs to adopt a review process that considers factors such as human rights abuses, levels of military spending, and governmental commitment to equitable and sustainable development.
- Finally, future U.S. allocations to the IFIs (except for IDA replenishments) should be withheld until the IFIs refocus on just and sustainable development.

Written by Erik Leaver (IRC)

sources for more information

Organizations

Bank Information Center
2025 I Street NW, Ste. 522
Washington, DC 20006
Voice: (202) 466-8191
Fax: (202) 466-8189
Email: bicusa@igc.apc.org

Center of Concern
3700 13th St. NE
Washington, DC 20017
Voice: (202) 635-2757
Fax: (202) 832-9494

Development Gap for Alternative Policies
927 15th Street NW, Fourth Floor
Washington, DC 20005
Voice: (202) 898-1566
Fax: (202) 898-1612
Email: dgap@igc.apc.org

50 Years is Enough: U.S. Network for Global Economic Justice
1025 Vermont Avenue NW, Ste. 300
Washington, DC 20005
Voice: (202) 879-3187
Fax: (202) 879-3186
Email: wb50years@igc.apc.org

Friends of the Earth
1025 Vermont Avenue NW, Ste. 300
Washington, DC 20005
Voice (202) 783-7400
Fax (202) 783-0444
Email foedc@igc.apc.org
Contact: Marijke Torfs

Publications

BankCheck Quarterly
1847 Berkeley Way
Berkeley, CA 94703

Walden Bello, *Dark Victory: The United States, Structural Adjustment, and Global Poverty,* (London, Pluto Press, 1994).

John Cavanagh and Daphne Wysham, eds. *Beyond Bretton Woods: Alternatives to the Global Economic Order*, (London, Pluto Press, 1994).

Center of Concern, *Rethinking Bretton Woods* (3 vols., $15.95 per volume.)

Kevin Danaher, ed., *50 Years is Enough: The Case Against the World Bank and the International Monetary Fund*, (Boston, South End Press, 1994).

Duncan Green, *Silent Revolution*, (New York, Monthly Review Press, 1995).

Catherine Gwin, *U.S. Relations with the World Bank: 1945-1992, (*Washington D.C., Brookings Institution, 1994).

Jonathan Sanford, *Multilateral Development Banks: Issues for Congress,* CRS Issue Brief 1996 (Updated periodically).

World Wide Web

World Bank
http://www.worldbank.org

International Monetary Fund
gopher://imfaix3s.imf.org

Asian Development Bank
http://www.asiandevbank.org

Inter-American Development Bank
http://www.iadb.org

Subscription Information

You can subscribe to *In Focus* at one of three levels, you can receive *In Focus* in one of five ways, and you can choose which categories of *In Focus* you want to receive. Please mark the level of subscription you want, how you want *In Focus* delivered to you, and the topic categories you want. There is no extra charge for email delivery to mail and fax subscribers. (Individual copies of *In Focus* are $2.50, postpaid; bulk orders of *In Focus* are $12.00 for 10 copies, postpaid; orders for delivery outside the US are double the listed prices.) Make checks payable to the Interhemispheric Resource Center. We also accept VISA and MasterCard.

Level

❑ $15 10 briefs
❑ $30 20 briefs
❑ $60 50 briefs

Delivery

❑ Regular mail only
❑ Regular mail and email
❑ Fax only
❑ Fax and email
❑ Email only

Topic Categories

❑ All (receive all briefs)
❑ Foreign Policy Overview
❑ Trade and Investment
❑ Government Agencies
❑ Military and Peace
❑ Human Rights and Democracy
❑ Environment
❑ Labor
❑ Economic Aid
❑ Global Governance/United Nations
❑ International Financial Institutions (IFIs) and Debt
❑ Food and Farm
❑ Border and Immigration
❑ Central America
❑ Caribbean
❑ Mexico
❑ South America
❑ Africa
❑ Middle East
❑ Asia/Pacific
❑ Western Europe
❑ Central and Eastern Europe
❑ Former Soviet Union

Name **Institution**

Street Address

City **State** **Zip Code**

VISA/MasterCard Number **Expiration Date**

Signature **Daytime Phone** **Fax Number** **Email Address**