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# Drivers of Change: Explaining IMF Low Income Country Reform in the Post Washington Consensus

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## **Abstract**

Through use of rationalist, constructivist, and historical structural theory, this study of IMF Low Income Country (LIC) policy change from 1996 to 2010 identifies potential causal variables and mechanisms that drive contemporary reform in the institution toward its poorest member states. Patterns uncovered through principal-agent analysis suggest that coalition formation between at least two actors is a necessary condition for LIC policy reform. Principal-agent analysis also establishes that discontinuity among powerful states gives IMF management and staff greater openings to initiate or block reform efforts. Constructivist analysis assesses if shifts in thinking among IMF insiders and the broader epistemic community of development economists have causal effect on LIC policy reform. Evidence gathered through process tracing methods shows that reform occurred after economic ideas that underwrote previous policy positions lost legitimacy among influential elites within and outside the IMF. Thus while IMF staff self-identify as rational technocrats, they are also driven by concerns of pursuing what the broader elite community deems as appropriate policy choices. When the boundaries of appropriateness change, we can expect reforms that are consistent with new frames of acceptable policy choices to emerge.

Stepping outside of mainstream IR theory, historical structural analysis of IMF reform focuses on the interrelation of contemporary capitalist crisis, hegemony, and “inclusive neoliberal” development models. Here, the IMF is understood to hold a central role in the creation and perpetuation of the current geopolitical order underwritten by globalizing capitalism. Recent IMF LIC reforms that champion more participation, flexibility, and a nod toward Keynesian practices thus are seen as one component of a broader political project pushed by global elites to undermine potential challenges to the contemporary world order. Evidence gathered through discourse analysis and interviews shows

that IMF staff and management were cognizant of growing resistance to Washington Consensus reforms and embraced less coercive and more participatory means to increase LIC buy in into concessionary lending programs. The scope and character of contemporary IMF reforms paralleled similar calls for rethinking how to 'do' development among global elites. This suggests that a component of IMF policy response in LICs is tied to a broader political project focused on building a more inclusive and hegemonic form of globalizing capitalism.

The juxtaposition of three theoretical frameworks to examine the same phenomenon also provides a platform to evaluate current IR theory focused on IMF reform. Rationalist and positivist oriented constructivist approaches provide clear analytical roadmaps to cut through the complex dynamics found in the IMF, identify potential causal variables and mechanisms, and develop testable predictive hypotheses related to institutional reform. However, if studies of IMF LIC reform rely solely on current mainstream frameworks, explanation and analysis of how Fund policy change is interrelated with shifts and tensions in capitalist social structures and the power relations therein remain unexamined. This proves particularly critical when exploring why certain ideas considered market distorting remained off limits in contemporary IMF debates and how post Washington Consensus reforms reflect attempts by global elites to manage crisis points in the contemporary historical structure. In conclusion, I assess the merits of IMF research open to the use of positivist and historical relational paradigms. Such an approach will not produce one correct answer and suffers at some level from divergent baseline understandings of the social world. However, I maintain that despite this tension, the complexity of that world and processes of change within it merit space for mainstream and critical ontologies. Future studies of the IMF should explore more fully how diverse paths of inquiry can be effectively used to explain policy reform.

**DRIVERS OF CHANGE: EXPLAINING IMF LOW INCOME COUNTRY REFORM  
IN THE POST WASHINGTON CONSENSUS**

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## Abbreviations

AFR	African Department
APD	Asia and Pacific Department
CFF	Compensatory Financing Facility
EB	Executive Board
ECF	Extended Credit Facility
ED	Executive Director
EFF	Extended Funds Facility
ENDA	Emergency Natural Disaster Assistance
EPCA	Emergency Post-Conflict Assistance
EP	Economist Program
ESAF	Enhanced Structural Adjustment Facility
EU	European Union
Eurodad	European Network on Debt and Development
G-7	Group of Seven
G-20	Group of Twenty
GAB	General Arrangement to Borrow
GATT	General Agreement on Tariffs and Trade
GFSR	<i>Global Financial Stability Report</i>
HIPC	Highly Indebted Poor Country Initiative
HIPC II	Enhanced Highly Indebted Poor Country Initiative
IDA	International Development Agency
IEO	Independent Evaluation Office
IMF	International Monetary Fund
IMFC	International Monetary and Financial Committee
IOs	International Organizations
ISI	import substitution industrialization
LICs	Low Income Countries
LOI	Letter of Intent
MAP	Mutual Assessment Process
MCM	Monetary and Capital Markets Department
MD	Managing Director
MDGs	Millennium Development Goals
NAB	New Arrangements to Borrow
NBER	National Bureau of Economic Research
NGOs	non-governmental organizations
OECD	Organization for Economic Cooperation and Development
PA	principal-agent
PCDR	Post-Catastrophic Debt Relief Trust
PCL	Precautionary Credit Line
PFP	Policy Framework Paper

PRGF	Poverty Reduction and Growth Facility
PRSPs	Poverty Reduction Strategy Papers
PSI	Policy Support Instrument
RCF	Rapid Credit Facility
RES	Research Department
SAF	Structural Adjustment Facility
SAPs	Structural Adjustment Programs
SBA	Stand-By Arrangement
SCF	Stand-by Credit Facility
SDR	Special Drawing Rights
SPR	Strategy Policy and Review Department
SDDS	Special Data Dissemination Standard
SO	sociological organizational
TCC	Transnational Capitalist Class
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
WB	World Bank
WEO	<i>World Economic Outlook</i>
WEF	World Economic Forum
WTO	World Trade Organization

## Chapter 1- The IMF, LIC Reform, and the post Washington Consensus

The International Monetary Fund (IMF/Fund) is “back in business.”<sup>1</sup> Dismissed as incompetent or increasingly irrelevant following the Asian crisis of the late 1990s, fallout from the 2008 global economic crisis has restored the Fund’s prestige and policy influence across the globe. In the five year period since the crisis, the IMF has boosted its lending capacity by \$456 billion and lent out approximately \$75 billion annually to its member states.<sup>2</sup> This stands in stark contrast to its pre-crisis total lending portfolio in 2007 of \$10 billion.<sup>3</sup> Along with greater lending activity, the Fund has taken on a leading role in the coordination of multilateral policy response to the aftershocks of the 2008 crisis, particularly in its work with the G-20 and European Union.<sup>4</sup>

This rebirth of the IMF in the post-2008 period includes another notable trend that serves as the point of departure for this project. After several decades of involvement in low income countries (LICs),<sup>5</sup> the IMF has substantially increased resources and institutional focus on its poorest member states. Financing available for LIC concessional lending has doubled to \$17 billion since 2008 while lending to LICs from 2008 to 2012 totaled over \$13.6 billion. This level of lending in annual terms is four

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<sup>1</sup> Current IMF Managing Director Christine Lagarde made the following observation when serving as French Finance Minister in 2009: “The major thing that happened is that the IMF is back in business. Only two years ago, people were wondering whether the IMF was still serving a purpose. Now the IMF is busy with all sorts of things including its traditional mandate, which has to do with financing those countries that are really in trouble.” <http://www.forbes.com/2009/04/26/lagarde-imf-economy-business-washington-monetary-fund.htm>

<sup>2</sup> IMF, “IMF’s Response to the Global Economic Crisis”, 19 September 2013, available at <http://www.imf.org/external/np/exr/facts/changing.htm> (accessed 5 October 2013).

<sup>3</sup> For an overview of the pre-2008 diminished significance of the IMF, see Eric Helleiner and Bessma Momani, “Slipping Into Obscurity: Crisis and Institutional Reform as the IMF,” in *Can the World Be Governed? Possibilities for Effective Multilateralism*, ed. Alan Alexandroff (Wilfred Laurier University Press, 2008), pp. 353-388.

<sup>4</sup> At the 2009 G-20 summit, member states requested that the IMF coordinate the so-called Mutual Assessment Process (MAP). The MAP is designed to “identify objectives for the global economy, the policies needed to reach them, and the progress toward meeting these shared objectives.” Since 2009, the Fund has presented an annual MAP report at the G-20 meetings. See IMF, “The G-20 Mutual Assessment Process (MAP)”, 26 September 2013, available at <http://www.imf.org/external/np/exr/facts/g20map.htm> (accessed 7 October 2013).

<sup>5</sup> As of 2013, the Fund recognized 72 of its members as low income countries. The IMF defines LICs as states that have GNI/capita levels that qualify them for World Bank concessional lending ( up to \$1175/capita).

times the Fund's historical average.<sup>6</sup> Technical assistance programs, forums focused on LIC issues, and institutional outreach to LIC stakeholders also have expanded since the 2008 crisis.<sup>7</sup>

As is well documented, IMF policy choices impact development outcomes for a significant percentage of the world's poorest people.<sup>8</sup> Conditionality requirements tied to IMF loans to LICs include monetary and fiscal policy requirements and economic restructuring mandates that impact growth and poverty rates, education and health outcomes, environmental quality, and employment levels.<sup>9</sup> Fund technical support also impacts patterns of growth and economic redistribution.<sup>10</sup> Less well understood are dynamics that drive the formation of IMF LIC policy and episodes of reform. Given the recent increase of Fund resources and institutional attention toward LICs, addressing this gap in the literature is critical for policy makers and activists focused on shaping contemporary IMF policy direction and subsequent twenty first century development outcomes in poor states.

Several recent studies of the IMF have identified key actors involved in individual cases of LIC policy change that occurred in the 1990s. Kathryn Lavelle uncovered evidence that the U.S. Congress pushed the Fund to deepen its commitment to debt relief in processes leading up to the 1999 "enhanced"

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<sup>6</sup> See IMF, "Financing the Fund's Concessional Lending to Low-Income Countries," 13 May 2013, available at <http://www.imf.org/external/np/exr/facts/concesslending.htm> (accessed 7 October 2013).

<sup>7</sup> For an overview of LIC programs at the IMF and how these have become 'front and center' in the IMF's agenda, see the recently launched Fund website on LICs at <http://www.imf.org/external/np/exr/key/lic.htm>.

<sup>8</sup> As of 2012, approximately 847 million people live in LICs that participate in IMF and World Bank programs. See <http://data.worldbank.org/income-level/LIC>.

<sup>9</sup> Ngaire Woods, *The Globalizers: The IMF, the World Bank, and their Borrowers* (Ithaca, NY : Cornell University Press, 2006), pp. 141-178; Michael Barnett and Martha Finnemore, *Rules for the World: International Organizations in Global Politics* (Ithaca: Cornell University Press, 2004), pp. 45-72; Ian Taylor, "Hegemony, Neoliberal 'Good Governance' and the International Monetary Fund: a Gramscian Perspective," in *Global Institutions & Development: Framing the World?*, eds Morten Bøås and Desmond McNeill (London: Routledge, 2004), pp.124-136.

<sup>10</sup> Axel Dreher, "IMF and Economic Growth: The Effects of Programs, Loans, and Compliance with Conditionality," *World Development*, 34, no.5 (2006), pp.769-788; James Boughton and Domenico Lombardi, "The Role of the IMF in Low-Income Countries," in *Finance, Development, and the IMF*, eds. James Boughton and Domenico Lombardi (Oxford: Oxford University Press, 2009), pp. 3-11; Graham Bird, *IMF Lending in Developing Countries: Issues and Evidence* (London: Routledge, 1995) ; James Vreeland, *The International Monetary Fund: Politics of Conditional Lending* (New York: Routledge, 2007).

Highly Indebted Poor Country Initiative.<sup>11</sup> Antje Vetterlein traced how the IMF's Executive Board responded to broad external criticism of conditionality requirements and pushed the institution to approve the Poverty Reduction Strategy Paper framework in 1999.<sup>12</sup> Along with the Executive Board, there is evidence that suggests Fund staff and management played an integral role in past cases of LIC policy reform. IMF adoption of the Highly Indebted Poor Country Initiative in 1996, for example, was strongly influenced by senior staff members and then Managing Director Michel Camdessus.<sup>13</sup> André Broome also established that non-governmental organizations (NGOs) successfully reframed LIC debt relief as a moral issue in the 1990s, and in so doing, helped catalyse Fund reform.<sup>14</sup>

These investigations are an important first step as variables tied to individual episodes of IMF LIC change are identified. No comparative analysis across cases of LIC reform, however, has been undertaken. This limits understanding in several key areas. Can we observe, for example, any pattern of policy actors and conditions that promote or block IMF LIC change? Does the evidence from past cases of LIC policy reform point to any recognisable threshold conditions that must be met for reform to occur? Can we discern any generalizable patterns in these cases that can be used to predict future cases of IMF LIC policy change? Are these episodes of LIC reform reflective of deeper or broader shifting power dynamics and social forces in the early 21<sup>st</sup> century? And if so, what are the primary components of these structural changes that drive post Washington Consensus LIC policy and reform? Contemporary scholarship focused on the Fund also has not engaged with the most recent case of LIC

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<sup>11</sup> Kathryn Lavelle, *Legislating International Organization: The US Congress, the IMF, and the World Bank* (Oxford: Oxford University Press, 2011).

<sup>12</sup> Antje Vetterlein, "Lacking Ownership: The IMF and its Engagement with Social Development as a Policy Norm," in *Owning Development: Creating Policy Norms in the IMF and World Bank*, eds. Susan Park and Antje Vetterlein (Cambridge: Cambridge University Press, 2010), pp.93-112.

<sup>13</sup> Bessma Momani, "Internal or External Norm Champions: The IMF and Multilateral Debt Relief," in *Owning Development: Creating Policy Norms in the IMF and World Bank*, eds. Susan Park and Antje Vetterlein (Cambridge: Cambridge University Press, 2010), pp. 29-47.

<sup>14</sup> André Broome, "When do NGOs Matter? Activist Organizations as a Source of Change in the International Debt Regime," *Global Society* 23, no.1 (2009), pp.59-78.

reform that replaced the concessionary Poverty Reduction and Growth Facility in 2010. How did the processes that facilitated this policy shift following the 2008 global financial crisis compare with LIC reforms that occurred in the late 1990s? Inclusion of evidence drawn from this case is crucial, as it updates understanding of early 21<sup>st</sup> century LIC policy dynamics in the IMF and broader development outcomes.

Four major cases of IMF LIC reform occurred between 1996 and 2010 (see Figure 1.1 below).<sup>15</sup>

Figure 1.1: Four Cases of post-Washington Consensus IMF LIC Reform (1996-2010)

<i>Title of Reform</i>	<i>Year</i>	<i>Policy Change?</i>
Highly Indebted Poor Country Initiative (HIPC)	1996	-Limited debt relief for LICs
Enhanced Highly Indebted Poor Country Initiative (HIPC II)	1999	-Replaced HIPC -Introduces PRSPs
Poverty Reduction and Growth Facility (PRGF)	1999	-Replaced SAF & ESAF
Extended Credit Facility (ECF) Rapid Credit Facility (RCF) Stand-By Credit Facility (SCF)	2010	-Replaced PRGF

The 1996 Highly Indebted Poor Country Initiative (HIPC) introduced a series of policies designed to lower debt burdens of LICs. It also marked the first formal recognition by the institution that a decade and a half of structural adjustment programs (SAPs) instituted after the 1982 Mexican debt crisis failed to adequately address issues of severe poverty and poor economic performance in LICs. In 1999, the HIPC was replaced with the HIPC II. HIPC II called for significant debt forgiveness and support of

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<sup>15</sup> This project thus consciously selects on the dependent variable (LIC policy change). As outlined by Alexander George and Andrew Bennett, doing so is appropriate in early stages of research focused on identifying potential variables and mechanisms that impact the dependent variable in question: “Cases selected on the dependent variable...can help identify which variables are not necessary or sufficient conditions for the selected outcome. In addition, in the early stages of a research program, selection on the dependent variable can serve the heuristic purpose of identifying the potential causal paths and variables leading to the dependent variable of interest. Later, the resulting causal model can be tested against cases in which there is variation in the dependent variable.” See Alexander George and Andrew Bennett, *Case Study and Theoretical Development in the Social Sciences* (Cambridge, Massachusetts: MIT Press, 2005), pp.23-24.

“pro-poor” growth strategies. This was organized through the introduction of the Poverty Reduction Strategy Papers (PRSPs). PRSPs, still in use today, are individualized plans that spell out how the recipient LIC in question will use resources from the IMF (and World Bank) to reduce poverty in accordance with the United Nations’ Millennium Development Goals.<sup>16</sup>

1999 also witnessed the replacement of the major concessionary lending facilities for LICs.<sup>17</sup> The Structural Adjustment Facility (SAF) and Enhanced Structural Adjustment Facility (ESAF), adopted in 1986 and 1987 respectively, were replaced with the Poverty Reduction and Growth Facility (PRGF). Both the SAF and ESAF were controversial in that conditionality requirements included a three part policy cocktail of anti-inflationary stabilization, liberal market structural adjustment, and moves toward export-led growth that produced short term economic retraction and social upheaval in many poor states.<sup>18</sup> The PRGF, in contrast, embraced a more diverse policy response and also prioritized poverty reduction as an essential component of successful development strategy. As with the HIPC II, the PRGF required that recipient states develop a PRSP to ensure a focus on poverty reduction and ownership of policy decisions by various stakeholders in LICs.

2009-2010 saw the fourth major contemporary shift in Fund policy toward LICs. The PRGF was replaced with the Extended Credit Facility (ECF), along with the creation of the Rapid Credit Facility (RCF) and Stand-by Credit Facility (SCF). Loans under these initiatives are both highly concessional and contain more flexible conditional requirements than the previous PRGF. Most notably, monetary and fiscal policy conditions tied to ECF/RCF/SCF loans suggest a shift among IMF LIC policy makers

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<sup>16</sup> The success of these efforts led to further calls for debt reduction. In 2005, the G-8 proposed that the IMF, Bank, and African Development Fund cancel 100 percent of multilateral debt claims of states that had reached HIPC II completion points. Under the Multilateral Debt Relief Initiative (MDRI), the Fund formed two trusts (MRDI-I and MDRI-II) to pay off the full stock of debt owed to the IMF for loans disbursed prior to 2005.

<sup>17</sup> Loans that have a grant element equal to 35 percent are considered concessional.

<sup>18</sup> As discussed in chapter 5, Latin America experienced an upsurge in social movements and protests in the 1980s and 1990s that focused on IMF and World Bank structural adjustment policies.



toward more Keynesian practices. ECF programs, for example, advocate countercyclical fiscal and monetary stimulus during economic downturn and an increase in inflationary target rates and “pro poor” spending.<sup>19</sup> This position stands in stark contrast to nearly three decades of policy that prioritized price stability and advocated pro-cyclical austerity during recessionary periods.

### **IMF and LICs in the post Washington Consensus**

These four cases of IMF LIC reform fall within what is described by development scholars as the current “post Washington Consensus” period. This term captures in broad terms a rejection of the Washington Consensus paradigm that heavily influenced IMF and the World Bank policies from the early 1980s to the late 1990s.<sup>20</sup> Supporters of the Washington Consensus maintained that price stability, privatization, and liberalization were the best strategy for poor states to successfully grow and integrate into the emerging global economy.<sup>21</sup> Specific to the IMF and LICs, this translated into conditionality requirements in SAF and ESAF loans focused on dismantling the remnants of state-centered Import Substitution Industrialization (ISI) strategies highly popular in developing capitalist states in Latin America, Africa, and Asia between the 1930s and 1980s.<sup>22</sup>

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<sup>19</sup>IMF, “Rethinking Macroeconomic Policy,” Staff Position Note SM/10/03, 12 February 2010 available at <http://www.imf.org/external/pubs/ft/spn/2010/spn1003.pdf> (accessed 10 March 2011).

<sup>20</sup> John Williamson, an economist at the Peterson Institute in Washington D.C., coined the term “Washington Consensus” in 1989. In its original context, the Washington Consensus was a description of what Williamson saw as the broad based consensus among “the political Washington of Congress and senior members of the administration and the technocratic Washington of the international financial institutions, the economic agencies of the U.S. government, the Federal Reserve Board, and the think tanks” around appropriate reforms needed in Latin American economies at the time. Williamson argues that the popular use of “Washington Consensus” that emerged in the 1990s equated the term with market fundamentalism and misrepresented his original meaning. He maintains, for example, that his conception of the Washington Consensus did not support carte blanche deregulation and privatization. Williamson also notes that he was staunchly opposed to capital account liberalization pushed by the IMF until the late 1990s. See John Williamson, “A Short History of the Washington Consensus,” in *The Washington Consensus Reconsidered: Towards a New Global Governance*, eds. Narcis Serra and Joseph Stiglitz (Oxford: Oxford University Press, 2008), pp. 14-30.

<sup>21</sup>Woods, *The Globalizers*, pp. 146-153.

<sup>22</sup> Proponents of ISI argued that developing states heavily involved in primary exports would see long-term decline in demand and price for their products compared to manufactured goods. ISI policies therefore focused on industrializing poor states through a series of measures that included: (1) Tariffs and quotas on imported consumer goods and overvalued

Facilitated in part by growing evidence that Washington Consensus reforms failed to produce expected growth outcomes in poor states and the Asian crisis, the late 1990s witnessed broad based challenges to the development policies pushed by the IMF and World Bank. Along with powerful political and institutional leaders including Kofi Annan and World Bank President John Wolfensohn, an ideologically diverse group of economists ranging from Joseph Stiglitz to free market advocate Jagdish Bhagwati<sup>23</sup> criticized the Washington Consensus model.<sup>24</sup> At the eve of the 2008 crisis, Stiglitz summed up the post-Washington Consensus thinking that emerged as follows: It rejects development models that advocate a minimal role of the state and carte blanche privatization and liberalization; it highlights the importance of effective market and state institutions; it emphasizes the importance of addressing poverty; it stresses diversity in policy response rather than a “one size fits all” development paradigm.<sup>25</sup>

As explored in the chapters below, these themes were prominently reflected in HIPC, HIPC II, and PRGF reform efforts. In addition, policy debates around the relationship between inequality and

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exchange rates to stimulate internal consumer demand for infant industries while allowing manufactures to import materials needed for production, (2) High investment by the state in infrastructure required by industry (roads, water, electricity), (3) Nationalization of key industries (oil, utilities) and/or creation of state-private consortiums, and (4) Support of urban workforce through price controls and subsidizing basics including food. As developed further in chapter 5, there was broad consensus within the IMF in the 1980s that ISI policies were the main cause of balance payment difficulties, economic inefficiency, and corruption seen in much of the developing world at the time.

<sup>23</sup> While Bhagwati is a staunch advocate of multilateral free trade, he is equally adamant in his critique of carte blanche financial liberalization and the IMF’s role in pushing for elimination of capital controls in the 1990s. For clarification of these two positions, see chapter 13 in Jagdish Bhagwati’s *In Defense of Globalization* (Oxford: Oxford University Press, 2004). Here, Bhagwati argues that the Asian crisis was caused by “hasty and imprudent financial liberalization” underwritten by “gung-ho international financial capitalism” pushed by the “Wall-Street Treasury Complex.” He describes the Wall Street- Treasury Complex as follows: “This is a loose but still fairly coherent group of Wall Street firms in New York and the political elite in Washington, the latter embracing not just Treasury but also the State Department, the IMF, the World Bank, and so on.” He made similar arguments in a 1998 publication in *Foreign Affairs*. See Jagdish Bhagwati, “The Capital Myth: The Difference between Trade in Widgets and Dollars,” *Foreign Affairs* 77, no.3(1998), pp.7-12.

<sup>24</sup> The term ‘post-Washington Consensus’ was first used by then Vice President and Chief Economist of the World Bank Joseph Stiglitz in a 1998 speech outlining his critique of the “market fundamentalism” of the Washington Consensus. See Joseph Stiglitz, “More Instruments and Broader Goals: Moving Toward the Post Washington Consensus.” The WIDER Annual Lecture, Helsinki, 7 January 1998.

<sup>25</sup> Joseph Stiglitz, “Is there a Post Washington Consensus Consensus?,” in *The Washington Consensus Reconsidered: Towards a New Global Governance*, eds. Narcis Serra and Joseph Stiglitz (Oxford: Oxford University Press, 2008), pp. 31-56 at pp.53-54.

growth in LICs have emerged within the IMF. This is perhaps best exemplified by the institutional signals sent by the Fund in the September 2011 issue of *Finance and Development* devoted exclusively to the subject.<sup>26</sup> Here, prominent Washington Consensus critic and former World Bank economist Branko Milanovic penned the lead article that highlighted the positive role states can play in reducing inequality and improving economic growth.<sup>27</sup> In the same issue, senior staff in the Fund's influential Research Department also argued that policy makers rethink the notion that inequality is good for growth and address severe and prolonged inequality as a necessary prerequisite for sustained development in LICs.<sup>28</sup>

Fallout from the 2008 crisis has introduced an additional dimension to the post Washington Consensus period that is linked to IMF LIC reform. As developed in detail in chapters 4 and 5, the crisis facilitated a reassessment of three decades of monetary and fiscal policy that prioritized price stability over all other macroeconomic outcomes. Within the Fund, this rethinking of monetary and fiscal policy response was first initiated by former Managing Director Dominique Strauss Kahn (2007-2011) and current chief economist Oliver Blanchard.<sup>29</sup> What emerged from what Strauss Kahn described as a “crisis of macroeconomics” are new IMF policy positions supportive of countercyclical fiscal response, higher inflationary targets, and automatic fiscal stabilizers in LICs. These policies were first formally integrated into LIC initiatives when the PRGF was replaced by the ECF/RCF/SCF lending framework.

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<sup>26</sup> *Finance and Development* is the quarterly publication of the IMF and is self-described as “publishing analysis of issues related to the international financial system, monetary policy, economic development, poverty reduction, and other world economic issues.”

<sup>27</sup> Branko Milanovic, “More or Less: Income inequality has risen over the past quarter-century instead of falling as expected,” *Finance and Development* 48, no.3 (2011), pp. 6-12.

<sup>28</sup> Andrew Berg and Jonathan Ostry, “Equality and Efficiency: Is there a trade-off between the two or do they go hand in hand?,” *Finance and Development* 48, no.3 (2011), pp. 12-15.

<sup>29</sup> See Dominique Strauss Kahn, “Opening Remarks: Macro and Growth Policies in the Wake of the Crisis,” Washington, D.C., 7 March 2011, available at <http://www.imf.org/external/np/speeches/2011/030711.htm> (accessed 10 April 2012).; and IMF “Rethinking Macroeconomic Policy”.

In sum, the post Washington Consensus period is characterized by a broad based rethinking of the relationship between states, markets, macroeconomic policy, and development. As described by Dani Rodrik and supported by evidence in this project, rejection of the Washington Consensus has been replaced by a diverse range of arguments on how best the IMF and World Bank should in fact “do” development.<sup>30</sup> The current flux of the post Washington Consensus period therefore represents a critical juncture in the relationship between the IMF, development, and 21<sup>st</sup> century outcomes in the world’s poorest states. Clarification of how and why the IMF has shifted positions in the recent past therefore is particularly pertinent for those interested in strategically pursuing future reform efforts and development policy trajectories in the global South.

### **Theoretical Approaches to IMF LIC Reforms**

This study of post Washington Consensus IMF policy reforms also presents an opportunity to evaluate strengths and weaknesses of theoretical frameworks focused on episodes of change in International Organizations (IOs). In chapters 3-5, I apply three distinct theoretical frameworks and their corresponding research methods to examine the same phenomenon of post-Washington Consensus IMF LIC change. Two mainstream frameworks divided along ontological lines of rationalism and constructivism currently predominate the literature of IO change. In chapter 3, I examine post Washington Consensus LIC change through the theoretical framework and methods currently used by rationalist inspired approaches. Here, I utilize principal-agent (PA) modeling to examine the external conditions that shape if and when the IMF (agent) has greater autonomy in development policies

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<sup>30</sup>See Dani Rodrik, “Goodbye Washington Consensus, Hello Washington Confusion? A Review of the World Bank’s *Economic Growth in the 1990s: Learning from a Decade of Reform*,” *Journal of Economic Literature* 44, no.4 (2006), pp.973-987.

primarily vis-à-vis the dynamics of member states (principals).<sup>31</sup> PA models make the following predictions: IMF policies should most directly reflect the preferences of the most powerful member states when preferences of these states are relatively homogenous and information asymmetry between states and the Fund is low. In the absence of these conditions, Fund management and staff are more likely to pursue an independent agenda but will not generally enact policy choices or reforms that would invite greater oversight and intervention by member governments. PA models focused on the IMF and World Bank also integrate the concept of delegation chains into their predictive models. The Fund is most likely to respond to demands for change from its most proximate principals (states) rather than distal principals (voters, NGOs).<sup>32</sup>

Rationalist scholars focused on IOs also have recently integrated components of sociological organizational (SO) theory to complement PA models.<sup>33</sup> SO theory assumes that institutions have their own unique organizational culture that impacts policy choices and processes of reform. Internal and external studies focused on the Fund's organizational culture describe the institution as rooted in a scientific, technocratic, and rational worldview consistent with the broader epistemic and professional economics field.<sup>34</sup> The Fund historically also has maintained a strong normative position against policies that are deemed market distortive. Despite the shifting ideological terrain of the post Washington Consensus, we should not expect that LIC policy change was packaged in a form that fundamentally challenged market based solutions to balance of payment and development issues.

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<sup>31</sup> Darren Hawkins, David Lake, Daniel Nielson and Michael Tierney, eds *Delegation and Agency in International Organizations* (Cambridge: Cambridge University Press, 2006).

<sup>32</sup> Daniel Nielson and Michael Tierney, "Delegation to International Organizations: Agency Theory and World Bank Environmental Reform," *International Organizations* 57, no.2 (2003), pp.241-276 at pp.249-250.

<sup>33</sup> Daniel Nielson, Michael Tierney, and Catherine Weaver, "Bridging the Rationalist-Constructivist Divide: Re-engineering the Culture of the World Bank," *Journal of International Relations and Development* 9, no.2 (2006), pp.107-139 at pp. 114-116.

<sup>34</sup> Bessma Momani, "Limits on Streamlining Fund Conditionality: The International Monetary Fund's Organizational Culture," *Journal of International Relations and Development* 8, no. 2 (2007), pp. 142-163.

In chapter 4, I examine IMF LIC change through the lens of “conventional” constructivism. Contemporary constructivist IO scholars focus their research on the impact of economic ideas, economic schools of thought, and development norms on policy choices.<sup>35</sup> Specific to the IMF, they highlight three major themes. First, while changes in ideas and norms that exist outside the institution matter in regard to potential shifts in policy direction, it is ultimately internal processes of how staff interpret these ideas and norms and act on them that determines if and when reform occurs.<sup>36</sup> Second, staff and management decisions are driven in large part by notions of legitimacy.<sup>37</sup> The economics profession, member states, and private market actors are the three constituencies identified that grant social acceptance to particular Fund ideas and policies.<sup>38</sup> Policy change is more likely to occur when these constituencies no longer grant legitimacy to particular economic ideas, economic schools of thought, or development norms. Third, ideational change that shapes policy outcomes is an ongoing process that involves stages of emergence, stabilization, and contestation. Here, three triggers undermine economic ideas and development norms and a subsequent increased probability that reform will occur: (1) acknowledgement that a particular policy doesn’t work; (2) an external shock; and (3) mass condemnation. In chapter 4, inquiry into why IMF LIC policy changes therefore focuses on how

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<sup>35</sup>Susan Park and Antje Vetterlein, eds *Owning Development: Creating Policy Norms in the IMF and World Bank* (Cambridge: Cambridge University Press, 2010). As developed further in chapter 4, Park and Vetterlein focus their analysis on impact of shifting development norms on IMF policy outcomes. Jeffrey Chwieroth instead focuses on shifts in economic ideas and the popularity or rejection of economic school of thought as driving IMF reform. See Jeffrey Chwieroth, *Capital Ideas: The IMF and the Rise of Financial Liberalization* (Princeton, New Jersey, Princeton University Press, 2010)

<sup>36</sup>Catherine Weaver, “The Meaning of Development: Constructing the World Bank’s Good Governance Agenda,” in *Constructing the International Economy*, eds. Rawi Adedal, Mark Blythe, and Craig Parsons (Ithaca: Cornell University Press, 2010), pp.47-67.

<sup>37</sup>Leonard Seabrooke, “Bitter Pills to Swallow: Legitimacy Gaps and Social Recognition of the IMF Tax Policy Norm in East Asia,” in *Owning Development*, eds. Susan Park and Antje Vetterlein (Cambridge: Cambridge University Press, 2010), pp. 137-149 at pp.137-141.

<sup>38</sup>Manuella Moschella, *Governing Risk: The IMF and Global Financial Crises* (Hampshire, UK: Palgrave MacMillan, 2010), pp.17-34.

economic ideas and development norms that shape IMF LIC staff evolve and identifies triggers that reshape them.<sup>39</sup>

Do these approaches sufficiently capture the dynamics involved with IMF LIC policy change? Two areas of concern merit broader theoretical investigation. In rationalist approaches, the state is often conceptualized as a unitary actor. This ignores the multiple forces and interests that shape state forms and their relations to multilateral institutions, including the Fund. A more dynamic approach that highlights this weakness is offered by Robert Wade.<sup>40</sup> In his study of the World Bank in the 1990s, Wade demonstrated that the institution was influenced by two contradictory forces: a “finance agenda” pushed by the U.S. Treasury and finance ministers from both the OECD and global South that advocated liberal market reform in all sectors of the economy, and a “civil society agenda” pushed by the U.S. Congress and NGOs generally more skeptical of liberal market development solutions. Conceptualization of the state as a unitary entity in rationalist approaches thus limits our understanding of diverging interests found within states that lobby for different policy direction in IMF.

Constructivists conceptually account for the impact of both outside forces and institution specific dynamics in their explanations of IMF change. Jeffrey Chwieroth, for example, argues that economic ideas and specific economic schools of thought shape how IMF staff conceptualize problems and appropriate policy response. Bessma Momani, Susan Park, and Antje Vetterlein, in a similar manner,

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<sup>39</sup> Susan Park and Antje Vetterlein, “Do Policy Norms Reconstitute Global Development?” in *Owning Development: Creating Policy Norms in the IMF and the World Bank*, eds. Susan Park and Antje Vetterlein (Cambridge: Cambridge University Press, 2010), pp. 137-149 at pp.137-141.

<sup>40</sup> Robert Wade, “US Hegemony and the World Bank: the Fight Over People and Ideas,” *Review of International Political Economy* 9, no.2 (2002), pp.201-229 at pp.218-220.

highlight that development norms formed outside the IMF shape staff decisions.<sup>41</sup> However, these scholars are adamant that ultimately it is “change from within” that drives policy reform. The Fund (and any institution) has its own unique organizational culture through which outside ideas and norms are processed. As articulated by Chwioroth, this should dissuade IO scholars from embracing accounts that prioritize the influence of broader structural change while ignoring the unique micro-dynamics of the institution under study.<sup>42</sup>

I maintain that heightened attention to institutional process to explain IMF reform, while a critical contribution, has downplayed how economic ideas and development norms are interrelated with broader shifts in 20<sup>th</sup> and early 21<sup>st</sup> century capitalist social structures. Why, for example, have we witnessed the replacement of the monolithic neoliberalism of the Washington Consensus with a diversity of ideas on how one should approach monetary and fiscal policy and structural reform in LICs? Can we accurately or fully explain LIC change within the Fund by focusing primarily on internal institutional culture? Or are there underlying macro-structural shifts that explain why certain economic ideas and development norms have become more or less influential in driving policy reform within the halls of the IMF?

In response to these concerns, I also explore if a theoretical framework that draws from Gramscian inspired historical materialism offers greater analytical leverage or unique insights into explanations of

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<sup>41</sup> Susan Park and Antje Vetterlein, “Owning Development: Creating Policy Norms in the IMF and World Bank.” in *Owning Development: Creating Policy Norms in the IMF and World Bank*, eds. Susan Park and Antje Vetterlein (Cambridge: Cambridge University Press, 2010), pp. 3-26 at p. 12; Momani, “Limits of Streamlining Fund Conditionality: The International Monetary Fund’s Organizational Culture,” p.146.

<sup>42</sup> Jeffrey Chwioroth, “Normative Change “From Within”: The International Monetary Fund’s Approach to Capital Account Liberalization,” *International Studies Quarterly* 52, no.1 (2008), pp. 129-158 at pp.129-136.



contemporary Fund LIC change.<sup>43</sup> This historical structural approach highlights how shifting social structures and productive relations within 20<sup>th</sup> and early 21<sup>st</sup> century capitalism have reshaped contemporary power structures, state forms, and multilateral institutions, including the IMF.<sup>44</sup> The unit of analysis in this framework consists of an identifiable constellation of mutually constituted and reinforcing social forces that make up a historical structure reproduced in part by a historic bloc.<sup>45</sup> A historical structure consists of three interrelated, reinforcing social forces (ideas/ideology, material capabilities, and institutions) that set the broad context of political possibilities and agency within a particular world order. These social forces, in turn, interact dialectically at three interlocking levels of activity: social relations of production, state forms, and world order.<sup>46</sup> By historic bloc, neo-Gramscian scholars refer to a complex of productive relations, classes, and ideology that underwrite and give cohesion to particular state forms and world orders.<sup>47</sup> Historical structures and historical blocs, while

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<sup>43</sup> I draw primarily from the work of Robert W. Cox and neo-Gramscian scholars in chapter 6. Examples of neo-Gramscian scholarship include: Stephen Gill, *American Hegemony and the Trilateral Commission* (New York: Columbia University Press, 1990); Craig Murphy “Global Governance Poorly Done and Poorly Understood,” *International Affairs* 76, no.4 (2000), pp.789-803; Mark Rupert, *Producing Hegemony: The Politics of Mass Production and American Global Power* (Cambridge University Press, 1995); Magnus Ryner, *Capitalist Restructuring, Globalization and the Third Way: Lessons from the Swedish Model* (London: Routledge, 2002); and Andreas Bieler and Adam Morton, “A Critical Theory Route to Hegemony, World Order, and Historic Change: Neo-Gramscian Perspectives in International Relations,” *Capital and Class* 82 (2004), pp.85-113. Works of Cox include Robert W Cox, “Social Forces, States, and World Orders: Beyond International Relations Theory,” *Millennium: Journal of International Studies* 10, no.3 (1981) , pp. 126-155; Robert W Cox, “Gramsci, Hegemony, and International Relations: An Essay in Methods,” *Millennium: Journal of International Studies* 12, no.2 (1983), pp.162-175; Robert W Cox, *Production, Power, and World Order: Social Forces in the Making of History* (New York: Columbia University Press, 1987); Robert W Cox, “Multilateralism and World Order,” *Review of International Studies* 18, no. 2 (1992), pp.161-180; Robert W Cox, “Towards a Post-hegemonic Conceptualization of World Order: Reflections on the Relevancy of Ibn Khaldun,” in *Approaches to World Order* ed. Robert W Cox and Timothy J Sinclair (Cambridge: Cambridge University Press, 1996), pp. 144-173; and Robert W Cox, *The New Realism: Perspectives on Multilateralism and World Order* (London: Macmillan, 1997).

<sup>44</sup> A focus on human material life is understood to encompass a broad range of historically contingent productive relations and processes - “entailing political, cultural, and economic aspects of social life”- that allow humans to reproduce and “remake their world and themselves. Mark Rupert “Marxism and Critical Theory” in *International Relations Theories: Discipline and Diversity*, eds. Tim Dunne, Milja Kurki, and Steve Smith (Oxford: Oxford University Press, 2007), pp.150-151.

<sup>45</sup> As outlined by Rupert, social relations, while not empirically observable as things, have structures that can be explained through analysis of “identifiable constellations of dominant social forces” in prevailing historical structures. See Mark Rupert, *Ideologies of Globalization: Contending Visions of a New World Order* (London: Routledge, 2000), p.42.

<sup>46</sup> Cox, *Production, Power, and World Order*, pp.395-398.

<sup>47</sup> Mark Rupert, “Producing Hegemony: State/Society Relations and the Politics of Productivity in the United States,” *International Studies Quarterly* 34 no.4 (1990), pp.427-456 at p.433.

broadly cohesive, are never fully stable or uncontested. Contradictory tendencies and tensions within historical structures and historic blocs produce periodic crises that may serve as flashpoints of change.

Historical structural studies of the contemporary world order and its relationship to the IMF frame their analyses in four interrelated themes that characterize the past five decades: the shift from a world economy made up of linked national economies to a globalized economy characterized by the transnationalization of production and accumulation; the dismantling of Keynesian welfare state forms in the global North and ISI state forms in the global South; the rise of a “globalist” historic bloc dominated by an emerging transnational capitalist class that has been unsuccessful in its attempt to build a hegemonic world order; and counter-tendencies that have emerged that challenge this non-hegemonic order.

For neo-Gramscians, the turmoil and crisis of the late 1990s and early 2000s and the global financial crisis of 2008 serve as the contextual foundation to explain post Washington Consensus policy change. Specific to the IMF, the HIPC and HIPC II initiatives, the PRGF, and the post 2008 ECF/RCF/SCF reforms are seen as components of a larger project initiated by progressive elements of the globalist bloc to secure a hegemonic global order. William Robinson, for example, contends that the post Washington Consensus period is an expression of an emerging “inclusive neoliberalism” that ultimately serves the purpose to “...attenuate some of the sharpest social contradictions of global capitalism...” in the interest of undermining challenges to the current historical structure.<sup>48</sup> Arne Rückert makes similar claims.<sup>49</sup> Through post Washington Consensus reforms, “...the World Bank

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<sup>48</sup> William Robinson, *A Theory of Global Capitalism: Production, Class, and State in a Transnational World* (Baltimore: Johns Hopkins Press, 2004), p.163.

<sup>49</sup> Rückert has published widely on World Bank policy in the post-Washington Consensus period from a Gramscian perspective. See Arne Rückert, “The World Bank and the Transformations of Neoliberalism: The Poverty Reduction

and the IMF play an increasingly important role in the attempt to promote hegemony around inclusive-neoliberal practices, particularly in “weak” developing countries.”<sup>50</sup> Chapter 5 assesses these claims.

### **Organization and Findings of Dissertation**

This dissertation has five main goals. First, through a comparative case study of the four major cases of IMF LIC reform from 1996 to 2010, it identifies potential causal variables and mechanisms that drove these instances of policy change. Second, it assesses if the evidence gathered from these cases suggests any generalizable patterns relative to LIC policy reform. Third, it analyzes if and how policy reform is interconnected to changing social relations and social forces in the contemporary historical structure. Fourth, it evaluates the relative strengths and weaknesses of rational, constructivist, and Gramscian inspired historical materialist frameworks focused on IMF reform. And fifth, it explores if we gain any additional analytical leverage in the study of contemporary IMF behavior through a research model open to mainstream and critical ontological and epistemological frameworks.

Chapter 2 provides the institutional and historical context for the four cases of post Washington Consensus LIC reform examined in chapters 3-5. The chapter first outlines the Fund’s formal operations and LIC programs. This is followed by a focus on the IMF’s organizational culture. Evidence gathered from interviews and internal Fund survey data highlights that LIC staff diverge from a broader institutional culture characterized by a silo mentality and ideological conformity. This suggests LIC staff exhibit a greater willingness to engage alternative ideas and policy positions than their colleagues in other departments in the Fund. The second section of chapter 2 includes a brief

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Strategy of Honduras,” *Canadian Journal of Latin American and Caribbean Studies* 36, no.70 (2011); Arne Rückert, “The Forgotten Dimension of Social Reproduction: The World Bank and the Poverty Reduction Paradigm,” *Review of International Political Economy* 17, no.5 (2010), pp.816-839; Arne Rückert, “A Decade of Poverty Reduction Strategies in Latin America: Empowering or Disciplining the Poor?,” *Labour, Capital, and Society* 42, no. 1&2 (2009), pp.56-81; and Arne Rückert, “Producing Neoliberal Hegemony? A neo-Gramscian Analysis of the Poverty Reduction Strategy Paper (PRSP) in Nicaragua,” *Studies in Political Economy* 79 (2007), pp.91-118.

<sup>50</sup> Rückert “Producing Neoliberal Hegemony? A neo-Gramscian Analysis of the Poverty Reduction Strategy Paper (PRSP) in Nicaragua,” p.96.

historical overview of the IMF's relationship with LICs from the creation of the institution in 1945 up to the post Washington Consensus period. It highlights three trends. First, prior to the breakdown of the Bretton Woods system in the early 1970s, the IMF's role in poor states concerned itself primarily with balance of payments correction. From the 1970s forward, IMF resources and focus on LICs have substantially increased. Fund "mission creep" into areas of development also emerged in the 1970s. Along with a focus on balance of payment correction, IMF conditionality evolved to include structural conditionality requirements designed to reform LIC state institutions and legal systems. The nature of structural conditionality took a radical liberal market turn through the introduction of SAF and ESAF programs in the mid-1980s and set the stage for post Washington Consensus LIC reform efforts.

Second, the IMF exerted – and continues to exert- its power in LICs. Formal surveillance over LIC activities and conditionality requirements demonstrates that the IMF has established what Michael Barnett and Raymond Duvall describe as direct "compulsory" and indirect "institutional" power in its relationship with its poorest member states.<sup>51</sup> In regard to the former, the Fund's influence in LICs is rooted primarily in conditionality requirements tied to concessionary lending. The IMF also evolved to fill an informal role as gatekeeper for LIC access to World Bank loans, other multilateral assistance, and private bank lending. Agenda setting through its conditional lending programs also shapes what poor states and development economists consider as legitimate policy positions. This ability to frame the relative appropriateness of policy choices is a key mechanism of power that remains entrenched in the relationship between the IMF and LICs.

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<sup>51</sup> See Michael Barnett and Raymond Duvall "Power in Global Governance," in *Power in Global Governance*, ed. Michael Barnett and Raymond Duvall (Cambridge.: Cambridge University Press, 2005) pp.1-22.

Third, a formula for dealing with balance of payment deficits emerged in the Fund in the 1960s that highlighted the need for states with balance of payment deficits to undergo short term economic contraction and governmental belt tightening. Known as the “Polak model,” this framework shaped how the institution perceived economic problems in LICs and the general formula for corrective action. Balance of payment problems and broader economic performance were considered primarily the fault of deficit states, rather than an outcome that also involved the behavior of surplus states or instability in global markets. As developed further in chapter 4, a key aspect of the Polak model has been challenged in the post Washington Consensus period that has shaped LIC policy reforms. Rather than focus primarily on balance of payment correction, an increase in balance of trade deficits may be necessary in the medium term in LICs to allow for poverty reduction and subsequent improvements in growth and development.

In Chapter 3, four cases of post Washington Consensus IMF LIC reform are studied through application of principal-agent modeling and sociological organizational theory. Evidence from these cases uncovers the following patterns. Two tiers of actors with different levels of influence shaped LIC outcomes. Primary actors included the Managing Director (MD), powerful states, and staff. Secondary actors included LICs, NGOs, and the U.S. Congress. In all the cases examined, LIC policy shift was successful either when a coalition formed between at least one primary and one secondary actor or at least two primary actors. Evidence from these cases also suggests that a primary actor can’t initiate reform alone. Without the support of other primary actors, staff, powerful states, and the MD must have backing from a secondary actor to successfully produce policy change.

As predicted by PA models, increased division among powerful state principals provided openings for management and staff to initiate, resist, or shape LIC policy. This was most salient when staff and the Managing Director shared preferences. In future scenarios, increased preference heterogeneity between powerful states on the Executive Board should result in greater leverage from management and staff to initiate or resist reform efforts. In regard to the impact of NGOs in delegation chains and the impact of pressure applied distally to principals, the evidence is inconclusive. Disaggregating the impact of direct and indirect lobbying on Fund policy choices requires further study before any conclusions can be drawn. More conclusively, evidence from these cases demonstrates greater success of direct lobbying when the NGO has at least one primary actor supporting their position. Finally, strategically situated individuals in the Strategy, Policy, and Review Department and African Department reinforce or block coalitions of change in the institution if the LIC reform in question substantially challenges the Fund's culture.

In Chapter 4, post Washington Consensus LIC reform is examined through the lens of constructivist theory. In broad terms, this framework is rooted in the notion that humans are social and reflexive emotional beings driven by the "logic of appropriateness" and make decisions based on shifting contexts of social identity and notions of legitimacy. Applied to this study, the role of economic ideas and development norms that inform what are deemed appropriate policy choices relative to LICs thus take center stage. Consistent with current trends in the constructivist literature focused on the IMF, I adopt a positivist epistemological position in Chapter 4.

Evidence from interviews and policy documents points to two categories of ideas within the IMF that shaped post Washington Consensus LIC policy reform. The first consists of ideas that have remained

fairly stable and uncontested since the creation of the IMF and set the broad boundaries of what is considered legitimate policy debate. These include the notion that transparent, market based mechanisms are the best tools to allocate resources efficiently, support growth, and reduce poverty and inequality in LICs.<sup>52</sup> An aversion to market distortive policies and support of free trade also fall within this non-debatable category. Within the boundaries of acceptable debate, IMF staff have been influenced by a diversity of economic ideas related to two distinct policy areas where the Fund is actively involved: (1) monetary and fiscal policy to stabilize short term balance of payment disequilibria; and (2) structural reform that improves economic efficiency and stimulates growth and development.

Constructivists argue that the primary constituency outside of the institution that reinforces the legitimacy of particular ideas or development choices pursued by the IMF is the economics profession. As such, chapter 4 then explores how the Fund has come to accept particular economic ideas that constitute appropriate macroeconomic and development policy and how challenges to these frameworks of thinking in the post Washington Consensus period have impacted policy reform efforts. I outline five mainstream schools of economics that have influenced the economics profession and IMF staff and management. These include traditional Keynesianism, the neoclassical synthesis, monetarism, new classical economics, and New Keynesianism.

Constructivist analysis points to three prominent trends concerning the role of economic ideas and LIC policy reform. A highly stable framework of what constituted appropriate monetary and fiscal policy response (known as the “New Consensus”) emerged in the early 1980s and was not significantly

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<sup>52</sup> Wilfred David, *The IMF Policy Paradigm: The Macroeconomics of Stabilization, Structural Adjustment, and Economic Development* (New York: Praeger Publishers, 1985), pp 7-11.

challenged until the 2008 financial crisis. The New Consensus – influenced primarily by monetarism, new classical economics, and New Keynesianism – argued against expansionary countercyclical monetary and fiscal policy response. The 2008 crisis delegitimized the New Consensus among development economists and IMF staff and has ushered in a new framework of economic ideas supportive of more Keynesian inspired macroeconomic policy. As previously noted, this helped drive replacement of the PRGF with the ECF/RCF/SCF in 2010. The Asian crisis of the late 1990s, in contrast, had little impact on monetary and fiscal policy reform efforts. However, fallout from the late 1990s led to the reevaluation of the role of the state in its relation to market efficiency, growth, and development. Along with challenges to the Polak model, an emphasis on poverty reduction, investment in human capital, and issues of inequality facilitated the replacement of the SAF/ESAF with the PRGF. Despite this shift in thinking in the late 1990s, an aversion to market distortive practices remains. LICs are advised to avoid protectionism, over or undervalued exchange rates, subsidies, and large-scale government managed redistribution.

Chapter 5 examines LIC reform in the post Washington Consensus through the lens of a historical structural framework. Given that this approach sits outside the mainstream of contemporary political science, the first section of Chapter 5 outlines the differences between what Robert Cox describes as “critical” and positivist “problem-solving” frameworks. In broad terms, a critical approach conceptualizes the world as constituted by human agents dialectically interrelated with time specific social structures that shape – and are shaped by – their action. Human nature and structures of human interaction thus are never fully static or characterized by essential, timeless qualities. As such, critical approaches reject the notion that generalizable causal patterns can be teased out from a series of cases in one particular historical era and then used as a template to predict future outcomes. Explanation in



this context instead focuses on revealing the historical structures that produce regularities in one particular era and how and why historical structures and subsequent world orders change over time.

Within this context, Chapter 5 then examines the interrelationships between shifting productive relations, state forms, and historic blocs of the first half of the 20<sup>th</sup> century that forged the post-World War II world order of *pax Americana* and its demise throughout the late 1960s and 1970s. During *pax Americana* (roughly 1945-1973), the IMF played a central role in the establishment and reproduction of a hegemonic global order rooted in a U.S. based “Fordist” historic bloc. Fordism describes the social structures, ideology, and practices that facilitated the emergence and consolidation of mass based factory production and consumption in the United States in the first several decades of the 20<sup>th</sup> century. Following World War II, Fordism was internationalized through various U.S. supported initiatives, including the IMF.

A critical factor that facilitated the internationalization of Fordist hegemony and the U.S. centered liberal order in the post WW II era involved the emergence of class compromise between American corporate capital and moderate elements of labor in the interwar years. Along with a series of laws supportive of organized labor in the 1930s and 1940s, the emergence of a New Deal Keynesian welfare state model committed to full employment policies helped undermine socialist and communist elements in the American union movement.<sup>53</sup> As highlighted by Mark Rupert and developed further in chapter 5, a de-radicalized labor movement that identified in Fordist “politics of productivity” and liberal notions of “free trade unionism” was a key element of the post-World War II U.S. centered

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<sup>53</sup> Mark Rupert, *Producing Hegemony: The Politics of Mass Production and American Global Power* (Cambridge: Cambridge University Press, 1995), p.173.

historic bloc.<sup>54</sup> IMF policy during the hegemony of *pax Americana* reflected the interests and tensions between elements and interests of this historic bloc. While sympathetic to notions of liberal trade pushed by the U.S. government and major industrial capitalists, the IMF did not actively push for structural reforms that undermined the politics of class compromise embedded in Keynesian welfare state models in the global North and ISI state models in the global South.

Chapter 5 then traces how the internationalist Fordist historic bloc and the hegemonic liberal world order of *pax Americana* began to unravel in the late 1960s and 1970s. Liberalized global markets and the spread of Fordist production methods and consumption patterns throughout Western Europe and Japan in the 1950s and 1960s produced excess industrial capacity and increased competition between wealthy capitalist states.<sup>55</sup> As U.S. competitiveness fell and trade surpluses turned into deficits by the early 1970s, American industrial capitalists and labor grew increasingly skeptical of free trade. This skepticism also focused on the perceived unfairness of the Bretton Woods monetary regime that required the U.S. to maintain fixed value for the dollar while other capitalist states enjoyed greater flexibility to devalue their currencies.<sup>56</sup> Richard Nixon (1968-1974) shared these sentiments. Between 1971 and 1973, Nixon opted for dollar devaluation that subsequently dismantled the Bretton Woods modified gold standard regime. The spirit of positive sum game liberal internationalism of Bretton

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<sup>54</sup>*Ibid.*, p.176.

<sup>55</sup>Jeffrey Frieden, *Global Capitalism: Its Fall and Rise in the Twentieth Century* (New York: W.W. Norton & Company, 2006), pp.346-347.

<sup>56</sup> As discussed in detail in chapter 2, the Bretton Wood regime was centered on the fixed value of the US dollar at \$35/ounce of gold. Other states pegged their currencies to the dollar, but were free to devalue if deemed necessary within a narrow range. As US trade surpluses shrank in the 1960s and turned into trade deficits by the early 1970s, US export manufacturers and the ALF- CIO lobbied to devalue the dollar. President Nixon complied in August 1971. Along with a subsequent 10 percent devaluation of the dollar in 1971, Nixon imposed a series of import tariffs. Despite attempts to revise Bretton Woods in 1972 and 1973, Nixon once again devalued the dollar by 10 percent in 1973. *Ibid.*, pp.349-342.

Wood was further undermined in the early 1970s by the rise of protectionist measures across the OECD.<sup>57</sup>

High productivity levels that had facilitated both increased profits for capital and real wage growth for labor since 1945 also began to fall in the mid-1960s.<sup>58</sup> Increased tension between capital and labor born from drops in economic growth, lowered productivity, and real wage stagnation by the late 1960s<sup>59</sup> was further exacerbated by a series of crises in the early 1970s that produced periods of stagflation throughout much of the OECD economies in the mid and late 1970s.<sup>60</sup> With the subsequent rise of neo-conservative political movements and elections of Margaret Thatcher (1979) and Ronald Reagan (1980), Fordist class compromise forged through the interwar and Bretton Woods eras quickly eroded. Corporate restructuring efforts, designed to revise productivity and profit, prioritized weakening the bargaining power of organized labor through multiple means.<sup>61</sup>

NeoGramscian scholars point to the “crisis of capitalism” in the 1970s as the catalyst that sparked the demise of the hegemonic world order of *pax Americana*. Starting roughly in the 1980s, a non-hegemonic world order has emerged that includes the following key dynamics. First, capitalist processes of production and accumulation have increasingly globalized. Second, the establishment of

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<sup>57</sup> Along with a 10 percent devaluation of the dollar in 1971 and 1973, Nixon also embraced protectionist measures. As competition and crises increased in the capitalist core throughout the 1970s, calls for increased protectionism reemerged across the OECD.

<sup>58</sup> Rupert, *Producing Hegemony: The Politics of Mass Production and American Global Power*, pp.178-179.

<sup>59</sup> Frieden notes that between 1968 and 1973, the rate of labor strikes across Western Europe was “five to twenty times the normal level.” Frieden, *Global Capitalism: Its Fall and Rise in the Twentieth Century*, p.350.

<sup>60</sup> Following the demise of the Bretton Woods fixed exchange regime, states across the industrial world rapidly increased spending to stimulate their economies. Increased government spending in combination with the 1973 oil shock pushed inflation across the OECD to average rates of over 10 percent by the mid-1970s.

<sup>61</sup> One key development from the new industrial model pushed by capital focused on producing ‘flexible’ workers able to manage and adapt in real time to the needs of consumers and market demand. This required the dismantling of Fordist collective bargaining agreements that had negotiated narrow job categories for workers. Corporate profit levels also were also increased through an upsurge of non-union and part time labor and subcontracting of production processes to non-union shops. See Rupert, *Producing Hegemony: The Politics of Mass Production and American Global Power*, pp.180-183.

globalized circuits of production and accumulation produced a new dominant “transnational capitalist class.” The ascendant transnational capitalist class (TCC) forms the core of a “globalist” historic bloc that also includes elite technocrats from multilateral institutions, including the IMF and World Bank, politicians of powerful states, and popular cultural and media figures. Third, Keynesian welfare states in the global North and ISI states in the global South have been dismantled and replaced with neoliberal state forms. Neoliberal state forms, in contrast to the Keynesian welfare state forms of *pax Americana*, are characterized by open hostility to organized labor and policy positions that have increased the intensity and extensity of commodification. Fourth, while powerful, the globalist historic bloc has been unable to produce a unified social vision to legitimate the restructuring of workplaces and state forms in accordance to their interests. For NeoGramscians including Stephen Gill, the current world order is therefore characterized by a more coercive and less consensual “politics of supremacy.”<sup>62</sup>

Applied to a study of the IMF and LICs, its adoption of Washington Consensus thinking in the 1980s and 1990s was interrelated with a world order shifting from hegemony and Fordist class compromise to a globalized neoliberal order. This was expressed in SAF and ESAF structural adjustment lending programs that helped dismantle the remaining vestiges of ISI state forms in these societies and reorganized economies along liberal market lines.<sup>63</sup> Secondary sources and internal Fund documents highlight that the IMF sensed growing pushback from SAF and ESAF programs in LICs in the late 1980s and 1990s and pursued a program focused on “good governance” to rationalize structural reform efforts. As resistance to neoliberal reform increased throughout the 1990s, neo-Gramscians

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<sup>62</sup> Gill, *Power and Resistance in the New World Order*, p.85

<sup>63</sup> After two decades of strong growth in Latin America, Asia, and Africa between 1940 and 1960, economies in the majority of non-oil producing ISI states witnessed increased debt levels, an increasing number balance of payment crises, higher inflation, and lower growth in the 1960 and 1970s. Levels of debt increased substantially in the late 1970s when U.S. raised interest rates dramatically and helped lead to the Mexican Debt Crisis of 1982.

focused on the Bretton Woods institutions argue that social upheaval and crisis caused by these dynamics in LICs are one key component that explains current post-Washington Consensus reform efforts. In order to facilitate long term support of market based development, IMF (and World Bank) policy over the past decade has become more sensitive to concerns of weak economic growth, poverty, and increased inequality in LICs. On an even broader scale, neo-Gramscians also hypothesize that contemporary IMF reforms are a by-product of elements within the globalist bloc that hope to (re)establish a hegemonic world order through a more inclusive form of globalizing capitalism.

Evidence from interviews with IMF staff and Executive Directors, internal Fund documents, and secondary sources lends initial support to these hypotheses. The rollout of the HIPC, HIPC II, and PRGF initiatives in the late 1990s was underwritten in part by two internal goals articulated by the Fund's LIC staff and management. First, there was a concentrated effort to increase support from multiple civil society stakeholders in LICs to IMF reform efforts. Second, the IMF staff highlighted a need to engage in a more consensual decision-making process with LIC stakeholders. Fallout from the 2008 crisis strengthened these trends. This was expressed most concretely in the elimination of "structural performance" criteria in Fund lending arrangements in 2009 that has given LICs greater flexibility and control over domestic reform efforts. Along with shifts in how LIC policy processes are implemented by the IMF, World Bank-IMF annual meetings and the annual World Economic Forum meeting in Davos over the past decade demonstrate that elements of the globalist bloc were increasingly concerned with poverty and increased global inequality.

Chapter 6 briefly first summarizes the evidence uncovered in chapters 3-5. It then analyzes

the relative strengths and weaknesses of rationalist, constructivist, and historical structural frameworks in regard to the study of the IMF and IOs more generally. It finds that rationalist and constructivist approaches to contemporary IMF LIC reform share the advantages common to positivist-oriented research. These include an ability to conceptually simplify the phenomenon under study, tease out potential causal relationships, and form predictive models. Rationalist models offer the best opportunity for practical application of knowledge gained. Contemporary constructivist studies, focused on the interplay between identity, legitimacy, economic ideas, and organizational culture, have pushed IO scholarship in a much more empirically sound direction. Here, the focus on internal micro-dynamics of the institution under study requires IO scholarship to be more careful in making monolithic claims about IMF behavior.

A critical framework rooted in a social ontology examines three areas of Fund behavior that mainstream frameworks are unable to engage. First, it introduces a causal story that sees processes of contemporary Fund policy change as dialectically related to the multiple and often contradictory dynamics embedded in the transnationalization of capitalist social relations. Second, it recognizes the role that IMF reform plays in the production and reproduction of hegemonic or more overtly coercive world orders. Third, the social relational roots of historical structural theory provide a foundation to evaluate where and why certain ideas have been folded into post Washington Consensus reforms while others have not, and what that signifies about the contemporary role that the IMF plays in the early 21<sup>st</sup> century world order. As developed in chapter 6, the Marxist and Gramscian roots of a historical structural framework is uniquely suited to explore why market distortive ideas remain off the table of post Washington Consensus “pro-poor” reforms and why a technocratic self- understanding remains at the core of IMF thinking around policy reform. It also may provide clues as to why this

identity is essential to how the Fund participates in (re)building hegemony in the contemporary historical structure through its policy choices in LICs. In short, while recognizing that IMF policy and market based development more broadly need to “work” for the poor, the boundaries of what is open for debate do not include policies that challenge deeply held beliefs in market efficiency. Following the logic of Marx, this makes sense as debating the efficacy of market distortive policies would bring politics into the arena that liberal market economists argue don’t belong. This, in turn, could potentially open up more radical challenges to the current historical structure underwritten by globalizing capitalist social relations.

Chapter 6 then assesses the potential benefits and drawbacks of research position open to use of rationalist, constructivist, and historical structural frameworks focused on IMF change. It opens this discussion by first affirming that each theoretical framework presents a reasonable causal story when explaining contemporary IMF policy reform. Evidence uncovered in this project also does not significantly undermine any major claims each framework makes that should disqualify it from future research. For example, evidence suggests that policy change is impacted by the formation of coalitions that either block or facilitate reform, shifts in how particular economic ideas gain or lose legitimacy among IMF staff, and broader tensions in the current historical structure of globalizing capitalism.

If each theoretical framework presents a reasonable causal story on its own terms, does it therefore make sense to study the phenomenon of multilateral institutional change through use of a diverse ontological and epistemological arsenal? Such an approach will not produce one correct answer and suffers at some level from divergent baseline understandings of the social world. However, as I explore in the conclusion of Chapter 6, I maintain that despite this tension and at some level

incompatible understandings of the world, the complexity of that world and processes of change within it merit space for mainstream and critical ontologies. Future studies of the IMF should explore more fully how diverse paths of inquiry can be effectively used to explain policy reform.



## **Chapter 2- The IMF and LICs**

Analysis of post Washington Consensus IMF LIC policy reform first requires basic institutional literacy in three areas: formal operations; informal dynamics of operational culture with focus on LIC staff; and the evolving role of the IMF in LICs. Chapter 2 first summarizes the Fund's formal operations and institutional structure with an overview of the IMF and its contemporary role in member surveillance, technical support, and lending. It then focuses on more informal characteristics of the institution's operational culture and explores several areas where LIC staff and procedures diverge from broader institutional trends. The chapter then examines the evolution of the Fund's relationship with LICs from its birth nearly seven decades ago to the end of the Washington Consensus period.

### **The International Monetary Fund**

The International Monetary Fund came into force on December 27, 1945. Article I includes the following "purposes":

(i) To promote international monetary cooperation... (ii) To facilitate the expansion and balanced growth of international trade... (iii) To promote exchange stability... and to avoid competitive exchange depreciation... (iv) To assist in the establishment of a multilateral system of payments in respect to current transactions... and... elimination of foreign exchange restrictions which hamper the growth of world trade. (v) To give confidence to members by making the general resources of the Fund temporarily available to them... to correct maladjustments in their balance of payments without resorting to measures destructive of national or international prosperity. (iv) To shorten the duration and lessen the degree of balance-of-payment disequilibria.<sup>64</sup>

At the organizational level, the Fund is best conceptualized as an international credit union made up of member states. Upon initial acceptance to the Fund, members are assigned a quota (currency contribution) that is held as a deposit at the Fund. Quotas are determined by the relative size of the

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<sup>64</sup> <http://www.imf.org/external/pubs/ft/aa/aa01.htm>

economy and engagement with international trade,<sup>65</sup> and shape two key aspects of members' relationships with the IMF. First, quota share determines how much the member must contribute in full when initially joining the institution. Once the overall currency contribution is established, the initial 25 percent of the quota must be paid in hard currency.<sup>66</sup> Referred to as the "reserve tranche" or "first tranche," these resources can be accessed by a member state without any conditionality requirements. The remaining three quarters ("upper credit tranches") are paid in member-specific currency and access to this credit is generally only granted with conditionality. Second, the quota amount sets the limit on how much a member can borrow from the Fund. For non-concessionary loans, this currently stands at 200 percent of its quota annually and 600 percent cumulatively.<sup>67</sup> In addition, the quota size determines the voting power of the member. As of 2013, the U.S. has the largest quota and percentage of votes (17.69 percent) of the Fund and holds unilateral veto power over significant Fund policy reform.<sup>68</sup> Germany, Japan, France, and the UK have quota sizes in the five percent range.

Quota shares are reviewed approximately every five years. Any change must be approved by 85 percent of the total voting power in the Fund. The 14<sup>th</sup> review, completed in November 2010, doubled overall quota requirements to a total of approximately \$756 billion.<sup>69</sup> Quotas were initially denoted in US dollar equivalents but were replaced with Special Drawing Rights (SDRs) in 1969. Today, the value of the SDR is determined by a basket of four currencies (euro, yen, pound sterling, and US

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<sup>65</sup> The current quota system formula involves four components: GDP (50 percent), openness (30 percent), economic variability (15 percent), and international reserves (5 percent).

<sup>66</sup> Prior to 1973, the reserve tranche was paid in gold. Today, countries must pay in currencies including the U.S. dollar, the euro, yen or pound sterling.

<sup>67</sup> <http://www.imf.org/external/np/exr/facts/quotas.htm>

<sup>68</sup> Any major initiative can be blocked by 15 percent of the total allocated voting shares.

<sup>69</sup> This review was portrayed by the Fund as a major victory for developing states in several areas. Quotas for LICs were preserved while six percent of quotas were shifted to "emerging market and developing countries" (EMDCs) including China, Russia, Brazil, and India.

dollar) and one unit currently hovers around the equivalent value of \$1.50.<sup>70</sup> A member state in need of hard currency in world markets can obtain it through two mechanisms. It can voluntarily exchange SDRs for usable currency with another member, or the Fund can designate states with balance of payment surpluses to buy SDRs from those with payment deficits.

Along with quota subscriptions, two additional programs are implemented on an ad hoc basis to supplement Fund resources for lending purposes. The “General Agreement to Borrow” (GAB), established in 1962, allows the IMF to borrow up to \$27 billion from 11 industrial countries on a short-term basis. The “New Arrangement to Borrow” (NAB) serves as a source of funds to supplement quota resources, particularly in times of financial crisis. Initiated after the Asian crisis, the NAB currently involves 39 members who have committed \$580 billion in resources to the arrangement as of 2011. Under NAB rules, proposals to access NAB resources must be approved by both 85 percent of states that have contributed to the fund and the Executive Board. In March 2011, the NAB was activated for six months in the amount of \$334 billion.<sup>71</sup>

## **Organizational Structure**

Voting formally takes place at two levels in the Fund. The Board of Governors is comprised of finance ministers or central bank heads of each of the 187 member states (see Figure 2.1 below). The Board of Governors retains the right to vote on policies including quota increases, SDR allocations, member admittance and withdrawal, and amendments to Fund Articles of Agreements and By-Laws.<sup>72</sup> This body meets twice a year, at the fall Annual Meeting and Spring Meeting, and much of its business is allocated to the International Monetary and Financial Committee (previously the Interim Committee).

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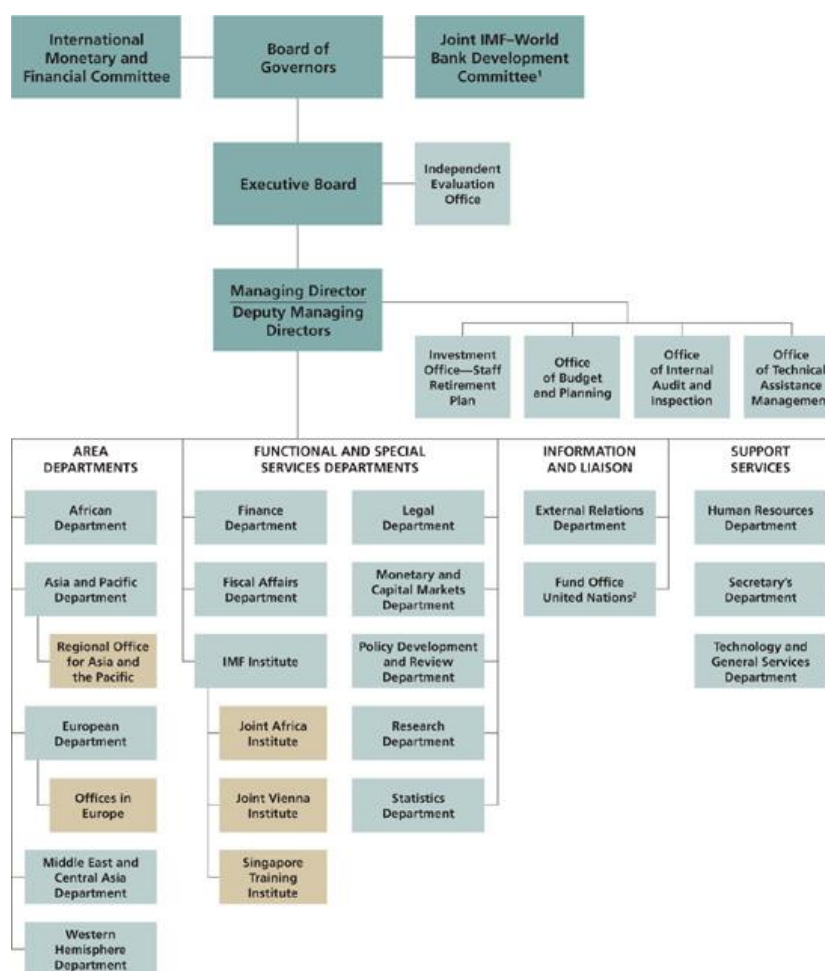
<sup>70</sup> <http://www.imf.org/external/np/exr/facts/sdr.htm>

<sup>71</sup> <http://www.imf.org/external/np/exr/facts/pdf/gabnab.pdf>

<sup>72</sup> <http://www.imf.org/external/about/govstruct.htm>

The International Monetary and Financial Committee (IMFC) “monitors developments in global liquidity and the transfer of resources to developing countries; considers proposals by the Executive Board to amend the Articles of Agreement; and deals with unfolding events that may disrupt the global monetary and financial system.”<sup>73</sup> The Development Committee, made up of Fund and Bank members, is tasked with advising both institutions’ Board of Governors on economic development issues in emerging and low-income states.

Figure 2.1: IMF Organizational Chart



(Source: <http://www.elibrary.imf.org>)

<sup>73</sup> <http://www.imf.org/external/np/exr/facts/groups.htm#IC>

Day to day operations are delegated to a 24 member Executive Board whose Executive Directors (EDs) are elected or appointed to two year terms. Eight appointed EDs currently represent individual countries with the largest quotas (the U.S., Germany, France, Britain, Japan, China, Russia, and Saudi Arabia) while 179 members are represented by the remaining sixteen. The Managing Director (MD) is appointed by the Executive Board, serves a five year term, and by convention is European. Christine Lagarde (see Figure 2.2 below) serves as the current MD and is assisted by the First Deputy Manager (by convention a U.S. citizen) and two Deputy Managing Directors. The Independent Evaluation Office (IEO), founded in 2001, sits outside the IMF and conducts ongoing reviews of Fund policies and programs.<sup>74</sup>

Figure 2.2: IMF Managing Directors: 1946-2013

<u>Managing Director</u>	<u>Tenure</u>
Camille Gutt	1946-1951
Ivar Rooth	1951-1956
Per Jacobsson	1956-1963
Pierre-Paul Schweitzer	1963-1973
H. Johannes Witteveen	1973-1978
Jacques de Larosière	1978-1987
Michel Camdessus	1987-2000
Horst Köhler	2000-2004
Rodgiro de Rato	2004-2007
Dominique Strauss-Kahn	2007-2011
Christine Lagarde	2011-present

The Fund staff of approximately 2500 individuals is distributed across eight functional and five area departments. Functional departments include: Finance; Fiscal Affairs; IMF Institute; Legal; Monetary and Capital Markets; Strategy, Policy, and Review; Research; and Statistics. Area departments include: Africa, Asia and Pacific, European, Middle East and Central Asia, and Western Hemisphere. Staff members across all departments are formally involved in three primary activities for member states: monitoring economies, providing technical assistance, and designing short-term loan packages

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<sup>74</sup> <http://www.ieo-imf.org/#>

for states with balance of payments difficulties. In regard to the former, under Article IV of the Articles of Agreement, members agree to collaborate with the IMF and one another to promote international economic stability. The Fund is charged with monitoring both individual member economies (“bilateral surveillance”) and reporting on global and regional economic trends (“multilateral surveillance”). Bilateral surveillance is accomplished through Article IV consultations. IMF staff travel to individual member states to evaluate monetary, fiscal, financial, and exchange rate policies and meet with various stakeholders to discuss and advise future policy direction. Upon return to the Fund, a report is filed with the Executive Board and then forwarded to the member state in question. Multilateral surveillance efforts include publication of two semi-annual reports, the *World Economic Outlook (WEO)* and the *Global Financial Stability Report (GFSR)*.

Technical assistance is primarily geared toward developing countries. It includes staff support for creating and managing macroeconomic policy, monetary and fiscal policy design and implementation, banking systems, taxation reform, financial systems, fiscal management, and foreign exchange policy. Delivery of assistance takes various forms. Staff missions are sent to member states for short term analysis and advice or may also remain for longer in-house placements. Training programs are also offered at the IMF Institute in Washington, D.C. and seven new regional technical assistance centers throughout the global South.<sup>75</sup> Funding for technical assistance makes up approximately one fifth of the Fund’s operating budget, with two thirds of these funds provided by external sources.<sup>76</sup>

## **Lending Facilities**

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<sup>75</sup> These are located in Fiji, Barbados, Tanzania, Mali, Gabon, Lebanon, and Guatemala.

<sup>76</sup> Multilateral donors include: the African Development Bank, the Asian Development Bank, the Caribbean Development Bank, the Inter-American Development Bank, the Islamic Development Bank, the European Investment Bank, the European Commission, and the United Nations Development program.

As of 2013, IMF loan instruments (“facilities”) are divided into three main categories. Non-concessional loans (Figure 2.3 below) are made available through either the Stand-By Arrangements (SBA), the Flexible Credit Line (FCL), the Extended Fund Facility (EFF), or Precautionary Credit Line (PCL). The interest rate charged on non-concessional loans (“rate of charge”) is based on the SDR interest rate and is adjusted on a weekly basis. Non-concessional lending arrangements with member states are facilitated through a Letter of Intent (LOI). Through the LOI process, Fund staff meet with country authorities and draft what the government plans to pursue in return for financial support. The LOI is then presented to the Executive Board for approval.

Although the Executive Board is formally empowered to reject or veto lending arrangements, staff have considerable autonomy in setting and monitoring member agreements. Staff assessment determines if a member has abided by conditions and qualifies for further lending. Staff can also require member states to implement “prior action” or “preconditions” before forwarding LOIs to the Board. Directors on the Executive Board also do not have access to confidential documents between staff and member governments during the LOI process. As such, Executive Board influence on LOIs is mostly informal, while formal control is limited to minor changes in staff proposals.<sup>77</sup>

Concessional loans designed for LICs include the Extended Credit Facility (ECF), the Standby Credit Facility (SCF) and the Rapid Credit Facility (RCF).<sup>78</sup> All concessional loans sit at below market interest rates and reflect policy commitments developed through Poverty Reduction Strategy Papers (PRSPs). PRSPs involve Fund and World Bank co-sponsored efforts to work with “domestic

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<sup>77</sup> Jeffrey Chwieroth, “The Silent Revolution: Professional Characteristics, Sympathetic Interlocutors, and IMF Lending,” pp 8-9.

<sup>78</sup> Concessional loans carry a very low or no interest. As of 2014, for instance the interest rate for ECF, SCF, or RCF loans was zero.

Figure 2.3: IMF Lending Facilities

Non-concessional IMF Lending Facilities

<u>IMF Loan Instruments</u>	<u>Introduced</u>	<u>Description</u>
Stand By Arrangement	1952	-1-2 year loan/ Repayment due 3-5 years -Designed to address short-term balance of payments deficits -Bulk of IMF conditional lending
Extended Fund Facility	1974	-3 year loan/ Repayment due 4-10 years -Designed to address longer –term balance of payments problems -Often focuses on deeper structural reform
Flexible Credit Line	2009	-1-2 years/Repayment due 3-5 years -Line of credit for crisis prevention for states with “strong fundamentals” -No conditionality requirements
Precautionary Credit Line	2009	-1-2 years/ Repayment due 3-5 years -Renewable line of credit for crisis prevention for states with “sound fundamentals” but facing “moderate vulnerabilities.” -Commitment to address vulnerabilities identified in qualification process

Concessional IMF Lending Facilities

<u>IMF Loan Instruments</u>	<u>Introduced</u>	<u>Description</u>
Extended Credit Facility	2010	-Succeeds Poverty Reduction and Growth Facility -Main tool for medium-term support for LICs -Zero interest rate/5.5 year grace period/10 year final maturity
Standby Credit Facility	2010	-Short-term support for LICs -Zero interest rate/4 year grace period/ 8 year final maturity
Rapid Credit Facility	2010	-Rapid, limited conditional support for LICs -Zero interest rate/5.5 year grace period/ 10 year final maturity

Emergency Resources

<u>IMF Loan Instruments</u>	<u>Introduced</u>	<u>Description</u>
Post-Catastrophic Debt Relief Trust	2010	-Assistance for LICs who have suffered a natural disaster -May involve debt flow relief or debt stock cancellation
Emergency Natural Disaster Assistance	1962	-3-5 year non-conditional assistance for natural disaster -Standard interest rate/ Up to 50 percent of quota
Emergency Post Conflict Assistance	1995	-3-5 year non-conditional assistance for post-conflict emergency -Standard interest rate/ Up to 50 percent of quota



stakeholders” to develop “macroeconomic, structural, and social policies and programs to promote growth and reduce poverty.”<sup>79</sup> Emergency resources for poor states that qualify for concessional lending are also available via the Post-Catastrophic Debt Relief Trust (PCDR). Non-LICs are eligible for crisis assistance through either the Emergency Natural Disaster Assistance (ENDA) or Emergency Post-Conflict Assistance (EPCA) programs.

Since the mid-1990s, the Fund also has increased initiatives focused on global financial stability. Along with promoting “codes of best practice” regarding fiscal and monetary policies, the IMF has developed and lobbied states to abide by a Special Data Dissemination Standard (SDDS) and General Data Dissemination Standard (GDDS) “as guidelines for government production of economic and financial data, with a view to improving the operation of global capital markets.”<sup>80</sup> Following the 2008 crisis, the Fund has worked in partnership with the G-20 on its Mutual Assessment Process (MAP) focused on how best to restructure the global economy.<sup>81</sup>

### **Operational Culture**

The current IO literature recognizes four major components of organizational culture. Routines include the standard operating procedure that over time produce patterns in behavior in an institution. Ideology is defined as the underlying belief system that sets the agenda and parameters of policy choices. Norms include collectively shared principles and values. Constructivist scholar Catherine Weaver additionally maintains that an institution also develops its own internal language “which enables the

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<sup>79</sup> <http://www.imf.org/external/np/exr/facts/psrp.htm>

<sup>80</sup> Jan Arte Sholte, *Civil Society Voices and the International Monetary Fund* (Ottawa: North-South Institute, 2002), p.5.

<sup>81</sup> <http://www.imf.org/external/np/exr/facts/surv.htm>

organization to create a common and efficient means of communicating the shared meaning of ideology and to consistently identify, categorize, and apply standard solutions to tasks.”<sup>82</sup>

I maintain the relationship between organizational culture of the Fund and its impact on policy shift is most effectively analyzed if organizational culture is separated into two components. Operational culture includes the routines as defined above. Standard operating procedures and the reproduction of “how things are done” produces specific patterns of behavior that shape how calls for reform move through the institution irrespective of the substance or ideological slant of the policy reform in question. Normative culture instead consists of predominant economic ideas, development norms, and language found in the organization. Evidence from this project points to procedural and ideological patterns among LIC policy makers that are at some levels distinct from the broader operational and normative culture of the Fund. I outline the Fund’s operational culture below and explore dynamics of normative culture in chapter 4.

Momani, in her 2007 study of the Fund, highlights an evaluation completed in 2006 by the Independent Evaluation Office (IEO) that documents several prominent characteristics of the IMF’s operational culture.<sup>83</sup> In the study, staff members were asked to assess if various categories of behavior accurately described the Fund.<sup>84</sup> The survey response points to four primary cultural characteristics: bureaucracy, hierarchy, homogeneity, and technical/economistic thinking.

### *Bureaucratic*

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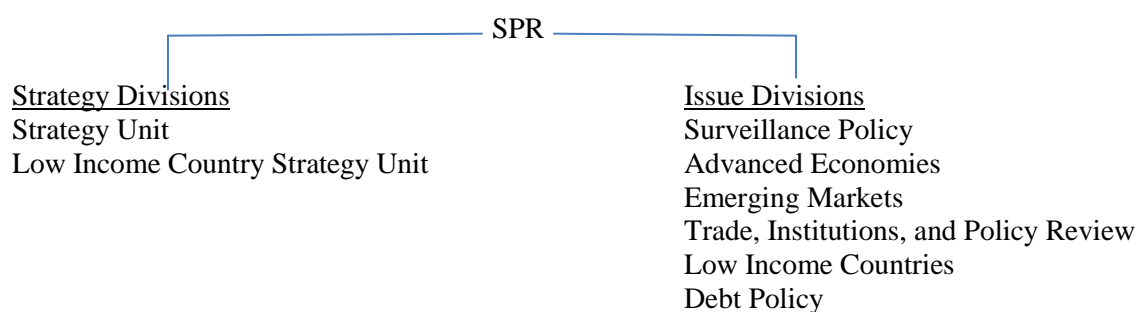
<sup>82</sup> Catherine Weaver, *Hypocrisy Trap: The World Bank and the Poverty of Reform* (Princeton: Princeton University Press 2008), p.37.

<sup>83</sup> Bessma Momani, “IMF Staff: Missing Link in Fund Reform Proposals,” *Review of International Organizations* 2, no. 1 (2007), pp.39-57.

<sup>84</sup> Karin Lissakers, Ishrat Husain, and Ngaire Woods, *Report on the External Evaluation of the Independent Evaluation Office* (Washington, D.C.: IMF, 2006), p.49.

The Fund follows a series of standard operating procedures with new proposals and country reports that produce and reinforce bureaucratic tendencies in the institution. Country reports follow a chain of command within area departments (e.g., African, European) starting with the desk officer and moving upward to division chiefs and then to the responsible area department’s senior staff.<sup>85</sup> Following review by senior staff in the area department, the document in question then is sent to the Strategy, Policy, and Review (SPR) department for review. SPR consists of two strategy divisions and six issue divisions (see Figure 2.4 below), two of which are solely focused on LIC issues. SPR serves as the main gatekeeper of Fund policy positions and also is seen as the main generator of new initiatives.

Figure 2.4: Strategy Policy and Review Department



SPR is designed to maintain institutional coherence in its policy recommendations. Relative to its role as gatekeeper, SPR’s review process focuses on two objectives. First, through its extensive review and editing process, SPR reinforces coherence in application of the Fund’s institutional mission. Second, as SPR is not tied to any particular member-state or area department, its review process provides a more objective take on policy choices.<sup>86</sup> Once approved by SPR, the policy document is forwarded to the Managing Director and finally to the Executive Board for adoption or rejection. If rejected by the Executive Board, the report or policy recommendation is returned down the chain of command for the next round of review and revision.

<sup>85</sup> Momani, “IMF Staff: Missing Link in Fund Reform Proposals,” p.45.

<sup>86</sup> Richard Harper, *Inside the IMF: An Ethnography of Documents, Technology, and Organizational Action* (San Diego, CA.: Academic, 1998), p.238.

Extensive documentation is thus a common complaint from staff. Specific to mission chiefs and others involved with LICs, the PRSP process and coordination with the World Bank on LICs has added multiple layers of review and bureaucracy to the policy making process.<sup>87</sup> Demands for timely documentation within the bureaucracy also produce a dynamic where “need for speed” are often in conflict with “need for local knowledge.”<sup>88</sup> Staff are often not given sufficient time to understand the particular dynamics of countries and also feel pressure to quickly report findings and issue recommendations to their superiors.

### *Hierarchical*

Several studies of Fund dynamics highlight that an institutional mandate focused on short term crisis management reinforces a hierarchical culture in the institution. Former UK Executive Board director Ian Clark, in an internal 1996 study focused on the Fund’s adaptability, noted how the institution prized and identified in its “crisis management capability” and how this favored hierarchical tendencies: “A prized element of the Fund’s culture...is its organizational discipline and crisis management capability. The goal of presenting a single corporate line in negotiations with countries requires a somewhat hierarchical managerial style and highly developed internal procedures to encourage questioning and debate at an early stage but to act with Cabinet-like solidarity after decisions are made.”<sup>89</sup>

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<sup>87</sup> Author interview with Fund staff member from Africa Department, Washington D.C., 21 September 2011.

<sup>88</sup> Peter Evans and Martha Finnemore, *Organizational Reform and the Expansion of the South’s Voice at the Fund* (New York: United Nations, 2001), p.9.

<sup>89</sup> IMF, “Should the IMF Become More Adaptive?” IMF Working Paper WP/96/17 (Washington, D.C.: IMF, 1996), pp.24-25.

Momani's investigation of Fund staff culture highlights how hierarchical tendencies in the Fund produce a "silo-mentality" that discourages coordination and communication across departments.<sup>90</sup> Several studies support this claim. An internal 1991 report concluded that Fund staff had "a sense of allegiance to an individual department, which rewarded loyal service and was protective of staff. [This] produced a situation in which departments were reluctant to explicitly identify or address performance problems, or sought to arrange for the transfer of weak performers to other less influential departments which tended to become repositories for problem cases."<sup>91</sup> A 1999 review of surveillance noted how lack of communication between the Research Department (RES) and the Asia and Pacific Department (ADP) didn't allow for concerns around South Korea's poorly regulated financial sector to be properly explored and may have led in part to the Asian crisis.<sup>92</sup> A 2006 IEO report also concluded that the Monetary and Capital Market Department (MCM) seeks little input from area departments when it creates its annual *Global Financial Stability Report (GFSR)*.<sup>93</sup> And finally, a 2011 IEO report focused on the IMF's failure to identify risks in the global financial system in the run-up to the 2008 crisis was due in part to staff reluctance to share information or seek consultation outside of their departments.<sup>94</sup>

Despite silo thinking broadly found within the institution, LIC staff interviewed for this project maintained that there is collaboration between the SPR and area departments, particularly the African

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<sup>90</sup> Momani, "IMF Staff: Missing Link in Fund Reform Proposals," p.45.

<sup>91</sup> IMF, *The Fund's Personnel Policies and Objectives*, EPAP/91/46, March 1, 1999 (IMF Archives), pp.4-5 as cited by Momani "IMF Staff: Missing Link in Fund Reform Proposals," p.45.

<sup>92</sup> IMF, *External Evaluation of IMF Surveillance* (Washington, D.C.: IMF, 1999), p.65 as cited by Momani "IMF Staff: Missing Link in Fund Reform Proposals," p.45.

<sup>93</sup> IEO, *Evaluation Summary: Multilateral Surveillance* (Washington, D.C.: IMF, 2006), pp.2-3, 11, 13, 21, 27-30 as cited by Chwieroth, *Capital Ideas*, p.36.

<sup>94</sup> IEO, *IMF Performance in the Run-Up to the Financial and Economic Crisis: IMF Surveillance in 2004-07* (Washington, D.C.: IMF, 2011), p.18.

Department, when designing new policy directives.<sup>95</sup> As articulated by a senior staff member of the African Department,

SPR carries the pen in terms of policy development but they do so quite collaboratively with other departments. The department that has the biggest stake is us [African Department]. The initiative typically comes from them. But we can play and have played a role when we see a particular need.<sup>96</sup>

Based on their career tracks in the Fund, senior level staff involved with LICs interviewed have not remained in one department. Rather, the general trend was that senior staff moved between SPR, Research, and the Africa departments during their tenure. This dynamic may also guard against the extensivity of silo mentality seen more broadly in the institution.

#### *Homogenous/Conforming*

60 percent of staff surveyed in the 2004 IEO report characterized the Fund as homogenous and conforming. A 2011 IEO evaluation focused on research at the Fund found that conformity to “IMF views” and “pre-set policy prescriptions” remains. 43 percent of staff noted that research at the Fund shunned alternative perspectives while 62 percent reported that research and conclusions had to be aligned with IMF views.<sup>97</sup> A series of Fund evaluations identify several standard operating procedures that reinforce conformist tendencies. First, extensive review processes within departments often hamper inter- and intra- department communication and innovation. A 1999 external report noted that staff complained that “the process [of internal departmental reviews] hinders innovation and flexibility; departments are inhibited from trying to do things differently.”<sup>98</sup> Second, staff reports forwarded to SPR and the Executive Board are designed to present a team view, and thus represent areas where staff have only found general agreement on the topic of concern. As reported by staff, this

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<sup>95</sup> Author interview of Fund staff member from Strategy, Policy, and Review Department, Washington D.C., 20 September 2011.

<sup>96</sup> Author interview of Fund staff member from Africa Department, Washington D.C., 14 June 2011.

<sup>97</sup> IEO, *Research at the IMF: Relevance and Utilization* (Washington, D.C.: IMF, 2011), p.87.

<sup>98</sup> IMF, *External Evaluation of IMF Surveillance*, p.33 as cited by Chwieroth, *Capital Ideas*, p.39.

produces a process “preoccupied with getting their analysis agreed and accepted internally.”<sup>99</sup> Third, all staff documents must conform to an accepted writing style. Staff reports that have reached the Executive Board, for example, are first given to the Fund Secretary who standardizes them. Momani argues this is one additional process where dissenting or critical staff voices may be toned down or even eliminated.<sup>100</sup> Chwioroth also notes that a focus on team work and assimilation is reinforced by Fund protocol with new recruits. Here, a two-year training program commonly includes time abroad where the new staff members are expected to assimilate and work with mission teams.<sup>101</sup>

The Fund’s hiring practices are also a variable that reinforces a homogenous culture in the Fund. Since 1970, the primary recruiting tool for new staff has been through the Economist Program (EP). From an annual initial recruitment pool of between 1500 and 2000 applicants, roughly 20-50 economists are hired through the EP each year. Comparison of data from 1985-87, 1991-97, and 2007-10 (see Figure 2.5 below) shows a prominent increase in percentage of women (from 5 percent to 44.4 percent) and those from “underrepresented” regions (from 33 percent to 59.3 percent) brought into the Fund through the EP program.<sup>102</sup>

Figure 2.5: Economist Program Recruits (1985-2010)

	1985/87	1991/97	2007/10
Female	5%	22%	44.4%
Underrepresented regions	33%	34.7%	59.3%

(Source: Momani, 2005 and IMF, 2010)

However, recruitment data also shows that the majority of new recruits from underrepresented regions comes from East Asia and the former Soviet and Eastern European communist states. On average,

<sup>99</sup> *Ibid.*

<sup>100</sup> Momani, “IMF Staff: Missing Link in Fund Reform Programs,” p.50.

<sup>101</sup> Chwioroth, *Capital Ideas*, p.39.

<sup>102</sup> Data compiled from Bessma Momani, “Recruiting and Diversifying IMF Technocrats,” *Global Society* 19, no. 2 (2005), pp. 167-187 at p.174 and IMF, *Diversity Annual Report 2010* (Washington, D.C.: IMF, 2010), p.23.

only two new economists from Africa and the Middle East were recruited into the Fund annually between 2007 and 2010 through the Economist Program.<sup>103</sup>

Longer term trends charted by the Fund's Diversity Office that focused on staff make-up also show the percentage of Africans working at the Fund has remained between 6 and 7 percent between 1995 and 2010. In the same time period, the share of economists from the Middle East fell from 5 percent to 4.4 percent. Nationals from former communist states (2 percent to 9.5 percent) and East Asia (7 percent to 10 percent) increased their representation in the Fund during this period. Comparing trends among industrialized regions, European representation increased from 38 percent to 44 percent while U.S. and Canadian nationals declined from 24 percent to 15 percent.

Despite efforts to increase staff diversity by national origin and gender, staff remain predominately male (74.5 percent) and from industrial countries (53.7 percent). The U.S. (12 percent) and UK (5.2 percent) have the greatest representation among staff by nationality. Only 6.5 percent and 4.4 percent of economists working at the Fund are from Africa and the Middle East respectively.<sup>104</sup> Along with the greatest representation of staff by nationality, the majority of IMF staff receives their academic training in the U.S. and UK. As of 2010, 72.2 percent had earned their PhDs from the U.S. (63 percent) or UK (9.2 percent) while 1.2 percent of staff held doctoral degrees from universities outside of the U.S., Canada, or Europe.<sup>105</sup> The majority of new recruits currently are graduates from 15 universities in the U.S. and 4 universities in the UK.<sup>106</sup>

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<sup>103</sup> IMF, *Diversity Annual Report 2010*, p.23.

<sup>104</sup> *Ibid.*, pp.44-5.

<sup>105</sup> *Ibid.*, p.28.

<sup>106</sup> *Ibid.*, p.68. U.S. universities include: University of Pennsylvania, Princeton, Columbia, New York University, Yale, University of Minnesota, University of Chicago, University of Michigan, Northwestern, Harvard, Boston University, MIT, UCLA, UC Berkeley, and Stanford. UK universities include: Cambridge, Oxford, Warwick, and the London School of Economics.



As articulated by a senior staff member involved in hiring processes, lack of diversity in training has produces problematic dynamics of group-think in the institution:

You have people who are normally argumentative and have their own views. Why do they agree with each other so easily? It could be that the mind-set is very similar. A problem we have is that the economists are all trained roughly in the same place, either in Europe or the U.S. Even though we may come from different parts of the world, we are filtered through the U.S. and European system. Just because we look different doesn't mean we think different. There is some sense that this needs to change. We are giving a lot of attention to diversity in all dimensions including intellectual diversity. We need people who think different as well.<sup>107</sup>

An effort to intellectually diversify through hiring and recruitment appears to be gaining traction in the institution but “is at an early stage”:

We are trying to hire a little bit more from institutions outside of the U.S. and Europe. We have people now with PhDs from Asia, from Latin America, from Russia. But it is at an early stage. I am not saying we have succeeded in making it intellectually diverse but we have succeeded in recognizing that this is an issue we need to address. And that is the first step that needs to happen before anything can change.<sup>108</sup>

Specific to LIC policymakers, two IEO studies provide evidence that staff involved with LICs are less homogenous and conforming in their thinking and interactions with country authorities than the institution at large. A 2011 IEO survey shows that 21 percent of authorities from LICs “strongly agreed” that Fund research was open to alternative perspectives and was not driven by pre-set policy prescriptions. In comparison, only 4 percent of authorities from advanced states and 8 percent of emerging states responded in the same fashion.<sup>109</sup>

### *Technocratic/Economistic*

Architects of the IMF, including John Maynard Keynes and Dexter White, were wary of the influence that states would exert on policy choices of the institution. In response, the Fund was structured in a

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<sup>107</sup> Author interview of Fund staff member from Asia and Pacific Department, Washington D.C., 26 September 2011.

<sup>108</sup> *Ibid.*

<sup>109</sup> IEO, *Research at the IMF: Relevance and Utilization*, p.24.

manner where the staff remained separate from the Executive Board.<sup>110</sup> This has translated into a policy process in which the staff is mainly responsible for key aspects of Fund functions, including loan negotiations, program monitoring, designing conditionality, and communicating Fund policies. Although the Executive Board has the ultimate power to approve policy decisions, it is normally not involved in the “nuts and bolts” of particular terms and conditions for loan arrangements or policy reform.<sup>111</sup> By design, it is the Fund’s staff of macroeconomists that ideally set policy.

The institutional power granted to a staff dominated by macroeconomists has reinforced a technocratic operational culture that historically has focused primarily on issues of economic efficiency when developing policy for member states. Drawing primarily from macroeconomic modeling, policy recommendations tend to downplay or sometimes ignore country-specific political and institutional dynamics. Internal and external reviews point to a history of complaints from member state representatives on the practicality of Fund recommendations. A 2004 study reports that “Fund advice fails to take into account existing political constraints, or is so optimistic about the ability of the governments to overcome them that it does not consider second-best policy choices that would be consistent both with maintenance of macroeconomic stability and country-specific realities.”<sup>112</sup>

According to a senior SPR staff member heavily involved in LIC policy design, there also has been a slow evolution within the Fund to think about macroeconomic advice more holistically and within a broader context of other social and development goals:

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<sup>110</sup>Momani, “Recruiting and Diversifying IMF Technocrats,” p.169.

<sup>111</sup> For cases when the Executive Board has intervened to set policy outcomes, see Bessma Momani, “American Politicization of the International Monetary Fund,” *Review of International Political Economy* 11, no. 5 (2004), pp.880-904.

<sup>112</sup> IMF, *Biennial Review of Implementation of the Fund’s Surveillance and the 1977 Surveillance Decision Modalities of Surveillance* (Washington, D.C. : IMF, 2004), p.12 as cited by Chwieroth, *Capital Ideas*, p.37.

Where there has been a real cultural change is that if you go back to the late 70s and early 80s, the conventional view in the Fund was that there is a clear separation between macroeconomic policies and everything else. Development policies, things like composition of spending, income distribution, and the social effects of policies we saw as important but felt that the Fund had no business in those areas. These were political issues and were for other people to worry about and we could pursue our macroeconomic policy agenda completely independently of those kind of considerations. That is what has really changed in the Fund. No one really believes that anymore.<sup>113</sup>

Despite this shift, the same staff member also articulated that this change in operational thinking is not complete and has produced some confusion as to how the Fund now engages in its policy work:

We are still learning that we need to make linkages between politics and economics. I don't think we are all the way there yet. Recent events in North Africa, for example, have been a wakeup call again that you cannot ignore factors like lack of opportunity, perception about corruption and subsequent legitimacy of the state if you're going to be concerned about stability and sustainability of economic policies. Political factors can undermine the macro-stability that we are trying to achieve. We are still trying to figure what that implies for the nature of our engagements and the policy work we get into.<sup>114</sup>

LIC staff also still see themselves as practical economists who objectively evaluate data and focus on “what works” rather than ideologues pushing a particular agenda. A senior staff member responsible for the design of current ECF/SCF/RCF framework described this dynamic as follows:

I would not pin the Fund's position too much on any internal change in culture and thinking but perhaps more of an evolution also of the countries that we work in. So there has been a shift in what's possible because many countries have made a lot of progress in macroeconomic stabilization. Probably more circumstances have shifted than internal views of people. I can assure you that within the staff there have no debates where terms including “neoliberal” or “Keynesian” have been uttered.<sup>115</sup>

This sentiment was reiterated by a current Executive Director representing LICs:

I would try to correct a sense that the IMF is ideologically driven.... Within the institution, every view is available. There is not a particular ideology within the institution that policies align to, but for the IMF is it rather “what can work today.”<sup>116</sup>

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<sup>113</sup> Author interview of Fund staff member from the Strategy, Policy, and Review Department, Washington D.C., 20 September 2011.

<sup>114</sup> *Ibid.*

<sup>115</sup> Author interview with Division Chief in the Low-Income Division in the Strategy, Policy, and Review Department, Washington, D.C., 14 June 2011.

<sup>116</sup> Author interview of Executive Board Director, Washington, D.C., 26 January 2012.

In sum, prominent aspects of the Fund's organizational culture and several trends that diverge from these norms found in LIC staff are as follows. First, the Fund operates in a bureaucratic, hierarchical fashion. Policy review follows a standard process that moves up the chain of command that includes various points of review. At the staff level, SPR serves as the main gate-keeper of potential policy reform for the Fund. Specific to LIC policy makers, three divisions within SPR (Low Income Country Strategy Unit, Low Income Countries, and Debt Policy) are responsible for review of all LIC policy documents before these are passed up the chain of command to the Managing Director and Executive Board.

Second, a culture of "silo mentality" exists between departments in the institution. There is, however, evidence of collaboration between the African, Research, and SPR departments concerning LIC issues that diverges from the broader institutional trend. Third, the staff is made up of economists primarily trained in elite universities in the U.S., UK, and Europe who identify themselves as non-ideological, practical technocrats. Fourth, despite recruiting patterns and institutional design that reinforces homogeneity in staff thinking, survey evidence demonstrates that LIC policy makers are more open to alternative perspectives than other departments. Adoption of the PRSP process in 1999, for example, has widened the variables included in policy design in the first decade of the 21<sup>st</sup> century. Greater openness to alternative perspectives also appears to give LIC staff greater intellectual room to explore ideas that historically stood outside the norm of Fund thinking. As explored in chapter 4, for example, LIC staff have been the main institutional actors pushing the institution to seriously address issues of poverty in policy design.

Based on its formal operations and operational culture, an argument can be made that the Fund is simply a technocratic institution that objectively responds to facts on the ground to alleviate balance of payment crises and promote international economic stability and growth. As is the general consensus among IO scholars focused on the IMF, I argue that the institution is much more than a technical support instrument for its member states' monetary and fiscal concerns. Since 1945, the IMF's power in the international system also makes it a key political actor that formally and informally shapes development outcomes across much of the global South.<sup>117</sup> To support this claim and to give context to my focus on the post-Washington Consensus period in chapters 3-5, I outline below the evolution of the Fund's relationship with LICs from its birth nearly seven decades ago to the mid- 1990s.

#### **1944-1952: The Bretton Woods Framework and the rise of IMF Conditionality**

At the end of the Second World War, U.S. and British policy makers led negotiations with allied states to reconstruct the international monetary and financial system. Several areas of concern marked these deliberations. Since the Great Depression, states had abandoned the classic gold standard of foreign exchange rates for floating exchange rate systems.<sup>118</sup> This shift had dramatic effects in multiple policy areas. Under the fixed exchange rate of the gold standard, states generally implemented deflationary monetary and fiscal policy when currencies came under pressure from balance of trade deficits.<sup>119</sup> With floating exchange rates, states instead corrected deficits through currency depreciation and increased trade barriers. Along with disruptions from two major wars, this pattern of competitive,

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<sup>117</sup> See Woods, *The Globalizers: The IMF, the World Bank, and Their Borrowers*; Vreeland, *The International Monetary Fund: Politics of Conditional Lending*; and Barnett and Martha Finnemore, *Rules for the World: International Organizations in Global Politics*.

<sup>118</sup> Under the leadership and pressure of Great Britain, most economies adopted the gold standard by the 1870s. Following World War I, a weakened gold standard was reinstated in 1925 and lasted until speculative attacks on the British pound in 1931 pushed the UK and leading states to abandon the policy.

<sup>119</sup> See Barry Eichengreen. *Globalizing Capital: A History of the International Monetary System* (Princeton: Princeton University Press, 1996), pp.25-27. In what David Hume described as the self-correcting dynamic of "price-specie flow mechanism," states with balance of trade deficits could only maintain currency value by decreasing money supply. Fiscal tightening and increased interest rates would also help reverse deficits by attracting short term capital to finance temporary balance of payments imbalance.

“beggar thy neighbor” devaluations and protectionism resulted in major contractions of global trade and production.

Shifts in domestic political forces also pushed states away from the gold standard in the interwar years. While deflationary monetary and fiscal policy to support fixed currency value was relatively easy to implement in the pre-WW I period, increased electoral franchise and the growing power of organized labor made such measures less politically tenable. Governments instead came under increased pressure to implement countercyclical monetary and fiscal measures during economic downturns and deficit spending more generally in support of emerging welfare states. Following the Great Depression, governments also began instituting capital controls to support domestic expansionary policy initiatives and counter increased speculation in the run-up to the global economic collapse of the 1930s.<sup>120</sup>

Key then for those given the task of rebuilding the international financial order was a multilateral institutional framework that would reconcile domestic priorities of emerging social welfare states and full employment policies with a desire to move away from protectionism and competitive devaluations seen in the interwar period. This tension between domestic welfare state policy objectives and desire to restore a liberal, international trade framework manifested itself in what John Ruggie describes as the compromise of “embedded liberalism” adopted by capitalist states through the Bretton Woods arrangement: “The embedding of commitment to economic openness – the liberal element – within domestic economic and political objectives was attained through the inclusion of provisions in the rules of international trade and finance that would allow governments to opt out, on a temporary basis,

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<sup>120</sup> Eric Helleiner, “The Evolution of the International and Monetary and Financial System,” in *Global Political Economy* ed. John Ravenhill (Oxford: Oxford University Press, 2008), pp. 213-240 at pp. 217-8.

from their international commitments should these threaten fundamental domestic economic objectives.”<sup>121</sup>

Within this context, the Bretton Woods framework was built around three pillars. To encourage trade liberalization, states committed to reducing protectionist barriers through the multilateral framework of the General Agreement on Tariffs and Trade (GATT).<sup>122</sup> Currency stability would be reestablished through a flexible gold standard arrangement built around IMF monitoring and support. States pegged their currencies to the US dollar convertible at \$35/ounce and agreed to hold exchange rates within one percent of those levels. With IMF consultation, member states could correct a “fundamental disequilibrium” by up to 10 percent devaluation of currency. States contributed to an IMF monitored stabilization fund from which members could borrow to finance temporary balance of payments deficits rather than be reliant on private funds. These policies would substitute for harsh domestic austerity adjustments as seen under the classic gold standard. Finally, states could control short term capital flows as deemed necessary under the new Bretton Woods regime, facilitating individual state autonomy in instituting monetary and fiscal policy that would support full employment policies and the subsequent stability needed for long-term liberalization.<sup>123</sup>

In its original institutional form, the Fund had no mandate to deal with development issues. This was left to the International Bank for Reconstruction and Development (the World Bank). While given

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<sup>121</sup>John Ravenhill, “The Study of the Global Political Economy,” in *Global Political Economy* ed. John Ravenhill (Oxford: Oxford University Press, 2008), pp.3-25 at p.13.

<sup>122</sup> The original Bretton Woods arrangement called for the creation of an “International Trade Organization.” These efforts were abandoned when the U.S. Senate refused to ratify the agreement in 1950.

<sup>123</sup> Without capital controls, states would not be able to implement deflationary or expansionary monetary policy under the Bretton Wood arrangements. For example, if state A instituted a monetary stimulus via increased money supply and lower interest rates without controls, capital would flow to other states with higher rates of return and counteract the initial stimulative effect. In the same scenario, if state A wished to slow down the economy via increased interest rates, capital would flow in. Capital controls under a fixed exchange rate system thus allowed states to implement monetary and fiscal policy without concerns that the inflows or outflows would counteract initial policy goals.

clearly distinct roles, the Bretton Woods design also directly linked the two institutions via a provision in the Bank's Articles of Agreement making membership to the Bank preconditioned on membership to the Fund. For the Bretton Woods framers, this linkage was driven by two concerns. Fund membership required that states agree to exchange rate and currency restrictions and surveillance of domestic economic policy. Bank membership, in contrast, involved only the benefit of access to development loans. Linkage would therefore reduce the risk of freeriding behavior. The framers also argued that monetary stability was an essential prerequisite for successful Bank lending. Fund membership served as leverage to push states to have their fiscal and monetary "houses in order" as a precondition of Bank development loans.

The Bretton Woods framework also reflected different tensions seen among powerful states at the time. The U.S., as the clear political and economic hegemon, advocated for economic liberalization. European powers, particularly a weakened Britain, focused more on issues of long-term stability, regulation, and a framework that supported post-war reconstruction.<sup>124</sup> Another controversial area specific to Fund activity involved conditional lending for short term balance of payments deficits. Britain and European states argued that conditionality requirements on short-term balance of payments deficits be strictly limited. By 1950, conflict between Fund staff pushing for conditionality and European resistance to these efforts set off a crisis in the institution as no members drew on Fund resources for the year. In response, Managing Director Ivar Rooth (1951-1955) proposed and ultimately persuaded member states to agree to a system of tiered conditionality. Each member state

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<sup>124</sup> See James Boughton, "Harry Dexter White and the International Monetary Fund," *Finance and Development* 35, no. 3 (1998), pp.12-25 for a detailed discussion of the differences between plans put forth by U.S representative Harry Dexter White and UK representative John Maynard Keynes. Keynes pushed several ideas that were ultimately defeated by White and US policy makers. These included a much larger "Clearing Union" from which states could draw from to finance balance of payments deficits, a new international currency (the "bancor"), and greater control of IMF decisions by the U.S. and UK.



would have conditional free access to the first 25 percent of its quota paid to the Fund in gold (the “gold tranche” at the time).<sup>125</sup> Any loan amounts greater than the gold tranche would be subject to Fund conditionality and surveillance. Approved in 1952, tiered conditionality arrangements would be negotiated via Stand-By Arrangements (SBAs). In return for access to “upper credit tranches,” states agreed to implement specific policies laid out in SBAs. SBAs remain the primary non-concessionary lending tool of the Fund.

### **1954-1962: IMF common sense, the Polak Model, and SBAs**

Poor states were not the primary concern of the early Bretton Woods system. Only five of the original members of the Fund and Bank would be considered low income by today’s standard. Several factors quickly broadened the institutional focus of the Fund to include the concerns of developing states in the 1950s. First, the IMF was shut out of European reconstruction efforts as Marshall Plan aid was conditional on *not* tapping Fund (or Bank) resources. As such, the IMF was eager to broaden its membership.<sup>126</sup> Decolonization movements also increased the number of poor states in the international system and subsequently membership in the Fund and Bank. The role the Bretton Woods institutions played in the emerging Cold War was perhaps most crucial in early Fund activity in the global South. Here, the Fund and Bank pushed an evolutionary model of development that rejected non-capitalist approaches espoused by the Soviet Union and a growing number of leftist and nationalist revolutionary movements. The values and thinking of “modernization theory” pushed by

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<sup>125</sup> Michael Barnett and Martha Finnemore, *Rules for the World: International Organizations in Global Politics* (Ithaca, NY: Cornell University Press, 2004), p.58.

<sup>126</sup> Two US led initiatives sidelined the Fund and Bank in the early postwar years. In 1946, the US pressured the UK to restore currency convertibility between the sterling and dollar through a \$3.75 billion “Anglo-American Loan Agreement”. Designed to last for five years, loan resources and British reserves were exhausted in six weeks after pound-dollar convertibility was declared. With American consent, convertibility was suspended on in August, 1947. The “sterling crisis” served as one of the major catalysts for the US led Marshall Plan and the subsequent sidelining of the Fund in European reconstruction efforts. Here, Marshall Plan aid was only forthcoming for states that agreed not to seek Fund resources to service balance of payments issues, reinforcing direct US control over European financial affairs. The Bank was also largely absent from reconstruction. While the Marshall plan funds totaled over \$18 billion from 1947-1953, the Bank made loans of only \$753 million while \$812 million was drawn from Fund resources during the same time period. See Woods, *The Globalizers*, p.32 and Eichengreen, *Globalizing Capital: A History of the International Monetary System*, pp.105-108 for further detail.

the Fund and Bank are best captured in U.S. economist Walt Witman Rostow's highly regarded *The Stages of Economic Growth: A Non-Communist Manifesto*. Rostow outlined key prerequisites necessary for successful development and "economic take-off" in poor states. These included technological and scientific expertise; appropriate infrastructure; education; the rule of law; private property rights; and the rejection of both traditional values *and* communism.<sup>127</sup> John McCloy, the first president of the World Bank, was even more explicit in his description of the role that Bretton Woods institutions played in the support of U.S. and Western geopolitical imperatives. The World Bank "... would create markets for US trade...[and] stop Communism."<sup>128</sup> Within this context, the Fund formally entered its first agreement with a developing state in 1954 (a \$12.5 million SBA arrangement with Peru) and steadily increased its activities in Latin America, Africa, and Asia in the 1950s.<sup>129</sup>

A critical driver of the emerging "common sense" behind Fund conditionality found in SBA lending at the time, and arguably still at some level today, is the work of IMF's Research Department under the leadership of Jacques Polak (1959-1979). In the early post-War period, economists at the Fund and the broader economics field had not developed the analytical and theoretical tools to engage with the new Bretton Woods system. In response, the Research Department under Polak developed a model that drew from the "absorption" and monetarist approach to balance-of-payments. In regard to the former, much of the work in the interwar period that concerned the impact of currency devaluation on balance of payments deficits focused its analysis on shifts in supply and demand of imports and exports in the

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<sup>127</sup> Walt Witman Rostow, *The Stages of Economic Growth: A Non-Communist Manifesto* (Cambridge: Cambridge University Press, 1961).

<sup>128</sup> As quoted by Knut Nustad, "The Development Discourse in the Multilateral System" in *Global Institutions & Development: Framing the World?* eds. Morton Bøås and Desmond McNeill (London: Routledge, 2004) pp.13-23 at p.16.

<sup>129</sup> SBAs were signed in Mexico (1954), Bolivia (1956), Chile (1956), Cuba (1956), Nicaragua (1956), Columbia (1957), Honduras (1957), Paraguay (1957), Argentina (1958), Brazil (1958), El Salvador (1958), Haiti (1958), the Dominican Republic (1959), Iran (1956), India (1957) Pakistan (1958), South Africa (1958) and Morocco (1959).

devaluing country.<sup>130</sup> Polak rejected this approach. Rather than focus on multiple elastic variables, he instead proposed a “simple social accounting” premise regarding balance of payment deficits:

...the existence of balance-of-payments deficit implies that the country absorbs more resources in consumption and investment than it produces. Therefore, if devaluation is to cure this deficit, it must either increase production with consumption and investment constant, or decrease consumption and investment with output constant, or achieve some combination of the two.<sup>131</sup>

Polak’s focus on level of consumption as the primary variable that impacts balance-of-payments deficits served as the foundation of the Fund’s focus on domestic policy choices of its members.

While the absorption approach shifted the analysis of Fund economists onto features of the domestic economy, no model existed to examine how different components of economies contributed to balance of payments problems and what policy tools could be used for correction. Polak’s “monetary model” demonstrated that states could not correct balance of payment deficits in the long term solely through either increases in exports or import restrictions. Correction of deficits instead only occurred if the rate of monetary expansion remained below growth rates of real gross national product. Deficit correction therefore required either decreases in domestic consumption or increases in productivity. Given that substantive productivity increases were difficult to obtain within the time frame of Fund short-term lending, the Polak Model pushed for reduction in government spending, deflationary monetary policy, and/or tax increases. Along with narrowing policy focus for Fund staff, Polak argued that this model

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<sup>130</sup> These models assumed devaluation would initially lower prices for exports and increase prices for imports. Subsequent upward shifts in demand for exports and downward shifts in imports would result in a ‘correction’ pushing export prices back up and import prices back down at least partially to pre-devaluation levels. The degree to which devaluation ultimately impacted balance-of-payments deficits in a state thus required estimating four different ‘elastic’ variables: foreign demand for a state’s export, the supply of export, demand for imports, and supply of imports from the rest of the world.

<sup>131</sup> Polak, 1951 as cited in Barnett and Finnemore, *Rules for the World*, p.53.

was practical as information needed for the model (banking and trade statistics) was generally available while data needed for elasticity models was incomplete and often inaccurate.<sup>132</sup>

Polak's model and subsequent Fund thinking thus clearly placed the onus of correction on deficit states and their domestic policy choices. It is important to note there were other ways Fund thinking may have evolved concerning deficits and adjustment. Since the 2008 financial crisis, for example, the Fund has focused greater attention on the role of surplus states in creating global imbalances and called on these governments to adjust.<sup>133</sup> Another possible framing of balance of payments issues is the role of exogenous, systemic conditions that undermine the ability of states to increase export earnings to correct trade imbalances. In the 1950s, however, the analytical framework of the Fund did not emphasize the policies of surplus states as causes of global disequilibria. Instead, a focus on domestic issues in deficit states produced a series of anti-inflationary policy choices and operating procedures that became standard for Fund engagement with LICs.<sup>134</sup> Ngaire Woods contends this framework resonated most strongly due to the fact that it was easier for the IMF to deal with domestic causes of balance of payments deficits over which it could apply institutional leverage than with broader systemic issues. Powerful member states including the United States also were supportive of Polak's framework.<sup>135</sup>

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<sup>132</sup> Jacque Polak "The IMF Monetary Model: A Hearty Perennial," *Finance and Development* 34, no. 4 (1997), pp.16-18.

<sup>133</sup> IMF, "What Caused the Global Financial Crises?-Evidence of the Drivers of Financial Imbalances: 1997-2007 (Washington D.C.:IMF, 2010), pp. 29-30.

<sup>134</sup> Barnett and Finnemore, *Rules for the World*, p.55. Barnett and Finnemore describe the impact of the Polak's model on the Fund as follows: "...the Polak model and absorption approach...strongly shaped Fund action over the coming years. They shaped the contacts Fund officials had with member states. National officials who controlled the money supply-central bankers and finance ministers-became the chief interlocutors of Fund officials. They shaped the kinds of data the Fund collected and what Fund staff, as well as national bureaucrats, knew about member state economies."

<sup>135</sup> Woods, *The Globalizers*, pp.42-43.

By the late 1950s, there was also evidence of early engagement with development issues tying Polak's deflationary model to areas of growth in poor states. This is captured in excerpts from the Fund's 1959 Annual Report defending the need for short-term anti-inflationary adjustment:

Notwithstanding the realization that is now fairly general that sound economic development is not compatible with the distortions that rapid or chronic inflation always creates, a number of less developed countries have had great difficulty in abating or slowing down the rates of inflation... The temporary deterioration of the standard of living [due to] a stabilization program is inevitable [and] may be interpreted by some sections of the public as an indication of the failure of the program, and give rise to the claim for prompt upwards adjustments in wages and salaries and form more liberal credit terms, which, if granted will again generate inflationary pressures.<sup>136</sup>

In the 1961 Annual Meeting, Fund Managing Director Per Jacobsen (1956-1963) reinforced this vision of the Fund as a tool for stabilization for long term gaps of capital inflow during periods of adjustment.<sup>137</sup>

### **1962- 1971: Push Back, Early Concessionary Lending, and LIC Technical Assistance**

The implementation of Polak-inspired adjustment in developing states was not without its critics. Conservative voices including the *Economist* argued that restrictive monetary policy pushed by the Fund was undermining Western influence in the Cold War. In a 1961 article, Per Jacobsen was described as “Mr Khrushchev’s secret weapon” overseeing potential “serious social eruption” in developing states.<sup>138</sup> Pushback from the left came in two primary varieties. Deflationary prescriptions in Fund policy and a push to eliminate multiple exchange rates<sup>139</sup> stood in sharp contrast to ISI theory popular in Latin America and much of the global South at the time. Among other policies to stimulate

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<sup>136</sup> IMF, 1959 as cited by Harold James, “Bretton Woods and the Debate About Development,” in *Finance, Development and the IMF*, ed. James Boughton and Domenico Lombardi (Oxford.: Oxford University Press, 2009), pp. 15-50 at pp.22-23.

<sup>137</sup> *Ibid.*, p.36.

<sup>138</sup> The *Economist* (1961: 329) as cited by James, “Bretton Woods and the Debate About Development,” p.40.

<sup>139</sup> Multiple exchange rates for developing states at the time often included overvalued exchange rates for essential imported items and undervalued exchange rates for luxury items or imported goods also produced by protected industries. Lower exchange rates also were applied to select industries for export. The Fund argued that the multiple exchange rate system was essentially a subsidy to support select industries and thus created economic distortions and inefficiency. Lower exchange rates also created inflationary pressure as central banks printed money to make up for losses.

industrialization for developing states, ISI frameworks embraced heavy government intervention in the economy. Inflation for ISI advocates was simply a by-product of state-driven investment and subsequent monetary expansion, and remained desirable within limits.<sup>140</sup> More radical critiques tied IMF policy to broader attempts by wealthy countries and capitalist elites to undermine efforts of poor states to diversify and industrialize. Here, dependency theorists including Celso Furtado pointed to the fact that U.S. aid and access to private capital were often linked to states first agreeing to anti-inflationary SBAs.<sup>141</sup> For Furtado, the IMF “operated primarily as a U.S. serving control instrument over the economic and financial policies of other countries, especially the so-called underdeveloped countries.”<sup>142</sup>

Concern over SBAs also emerged within the Fund and Washington policy establishment in the early 1960s. An internal IMF staff document focused on Colombia, for example, concluded it was “not too strong to say that the Colombian case tends to support many of the recent criticisms of the Fund.”<sup>143</sup>

In 1966 a Bank paper harshly criticized Fund policy in regard to short-term stabilization and called for “urgent reconsideration of the IMF’s approach to the performance of developing countries.”<sup>144</sup>

External and internal critiques and the attention created by a new concessionary branch of the World Bank (the International Development Group or IDA<sup>145</sup>) pushed the Fund to create its first loan facility focused on the needs of poor states in 1963. The “Compensatory Financing Facility” (CFF)

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<sup>140</sup> James, “Bretton Woods and the Debate About Development,” p.23.

<sup>141</sup> Following Peru’s 1954 SBA, for example, the U.S. sent development assistance to Peru and opened a credit line with Chase National Bank of New York.

<sup>142</sup> Celso Furtado, *The Economic Growth of Brazil: A Survey from Colonial to Modern Times* (Berkeley: University of California Press, 1963), pp.252-253.

<sup>143</sup> IMF Archives (1963) as cited by James, “Bretton Woods and the Debate About Development,” p. 40.

<sup>144</sup> *Ibid.*, p. 41.

<sup>145</sup> Established in 1960 in response to the concerns of poor states, the IDA provides interest free, long term loans to so-called “Part II” member states. As of 2013, 137 Bank members qualified for IDA loans. IDA funding comes primarily from wealthy member states and is seen as a major point of leverage to shape Bank policy. See Catherine Weaver, *Hypocrisy Trap: The World Bank and the Poverty of Reform*, pp.46-47.

acknowledged that volatility in primary commodity prices did in fact impact balance of payments issues in states dependent on agricultural and mineral exports. Temporary low conditionality funding to accommodate downturns in commodity prices thus could be more appropriate than short term austerity.<sup>146</sup> Under the CFF, overall Fund lending to LICs increased from \$243 in 1963 to \$723 million in 1967.<sup>147</sup>

By the mid-1960s, a growing number of developing states also pressured the Fund to address causes of commodity price fluctuations. This was a major goal shared by states that formed the United Nations Conference of Trade and Development (UNCTAD) in 1964. UNCTAD also pushed the IMF to focus on the drop of global liquidity seen throughout the 1960s. Developing states argued that inconsistent access to short term lending resources was a key element in causing disruptive balance of payment crises. Pressure from developing states and emerging European economies helped catalyze the 1969 adoption of “special drawing rights” (SDRs):

One vision of what would eventually become the SDR saw an important role for what came to be called the “link” with development, on the grounds that the effects of liquidity shortage in dealing with short-term balance of payments problems were felt most acutely outside the developed world.<sup>148</sup>

Growing tension between the Fund and Bank also emerged during this period. A series of Bank loans in Latin America and Asia in the early and mid-1960s, for example, included conditions on exchange rate policies and macroeconomic initiatives. In response to growing turf wars, Bank and Fund leadership reached an agreement that clarified the primary responsibilities of each institution in late

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<sup>146</sup>James Boughton, *Silent Revolution: The International Monetary Fund 1979-1989* (Washington, D.C.: IMF, 2001), pp.724-725. States could qualify for funds “if exports over the previous twelve month period had fallen short of the estimated medium- term level of exports defined as a moving five year average.” At its height of CFF lending in 1983, 29 states drew over \$4.1 billion from the Fund through this facility.

<sup>147</sup>James Boughton, “Lending to and for the Poor: How the IMF’s Role has Evolved,” in *Finance, Development and the IMF*, ed. James Boughton and Domenico Lombardi (Oxford.: Oxford University Press, 2009) pp.51-63 at p.53.

<sup>148</sup> James, “Bretton Woods and the Debate About Development,” p.43.

1966. The IMF was given jurisdiction over “exchange rates and restrictive systems, for adjustment of temporary balance of payments disequilibria and for evaluating and assisting members to work out stabilization programs as a sound basis for economic advice.” The Bank’s primary responsibilities would involve “composition and appropriateness of development programs and project evaluation, including development priorities.” Areas “of interest to both institutions” included “the structure and functioning of capital markets, the actual and potential capacity of a member country to generate domestic savings, the financial implications of economic development programs...foreign debt problems, and so on.”<sup>149</sup> As outlined further below, the breakdown of the Bretton Woods system and the oil shocks of the 1970s would chip away at the clear roles outlined in the 1966 concordat.

The Fund role in providing technical assistance to LICs also expanded in the 1960s. In response to the fact that most new African states at the time had no central banks, the Fund created its “Central Banking Service.” In 1964, the IMF Institute was opened in Washington, D.C. “Prominent in the curriculum were courses on financial programming, which taught national officials how to use the Fund’s analytical techniques in their own policymaking at the national level.”<sup>150</sup> Increased Fund missions to LICs “demanded certain kinds of data for their analysis from members” that in turn shaped what those member states would examine in their societies. In reaction to weak data collection seen in LICs, the Fund also opened its Bureau of Statistics in 1969.<sup>151</sup>

### **1971-1982: Breakdown of Bretton Woods and Early Structural Conditionality**

While the Fund’s role in the global South was established by the early 1970s, several factors pushed the institution more firmly into the realm of LIC development. The most influential factor was the

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<sup>149</sup> “Fund-Bank Collaboration,” in “Bank/Fund Collaboration on Missions and Meetings, 1966” as cited in Boughton, *Silent Revolution*, p.997.

<sup>150</sup> Barnett and Finnemore, *Rules for the World*, pp.60-61.

<sup>151</sup> *Ibid.*



collapse of the Bretton Woods system of adjustable pegged exchange rates between 1971 and 1973. As industrialized states adopted floating exchange rates, a primary component of the Fund's original institutional responsibility evaporated. An institutional focus on chronic balance of payments issues in developing states filled this vacuum. The Fund also found itself marginalized in its role of financing balance of payments deficits in middle income states. Major commercial banks flush with OPEC petrodollars accelerated lending to the global South and undermined the IMF's presence in emerging and middle-income countries.<sup>152</sup> By the mid -1970s, the IMF's main policy interventions were in the world's poorest states deemed too risky for private investment.

As the Fund's clientele became poorer, three initiatives were introduced to meet LIC needs: the Oil Facility, the Trust Fund, and the Extended Fund Facility (EFF). Both the Oil Facility (1975-1983) and Trust Fund (1976-1981) were financed outside the Fund's general account and represented the first generation of Fund concessional lending.<sup>153</sup> The EFF (introduced in 1974) signified a watershed moment in regard to the Fund's contemporary role in LICs. The three year EFF loan was designed by Fund staff to fill a gap between short-term SBA financing and long-term World Bank development aid.<sup>154</sup> Unique to the EFF was its focus on correcting long term structural issues in member states that produced "slow growth and an inherently weak balance of payments position" that undermined "an active development policy."<sup>155</sup> While Polak inspired macroeconomic policy conditionality focused on short term issues, structural conditionality went deeper as it pushed for substantial reform in national

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<sup>152</sup> For these states, 'no-questions-asked' private loans were more desirable than conditional SBAs. See Jacques Polak, "The World Bank and IMF: A Changing Relationship," in *The World Bank: Its First Half Century, Volume 2*, ed. Devesh Kapur, John P. Lewis, and Richard Webb (Washington, D.C. :The Brookings Institute, 1997), p.478.

<sup>153</sup> Following the 1973-4 oil shock, 25 countries contributed \$195 million to the Oil Facility to lower the interest rates on loans for poor states most severely impacted by rising oil prices. The Trust Fund, financed by a selloff of 16 percent of IMF's gold reserve between 1976-1980, provided low condition (loans were subject only to first tranche-conditionality), low interest loans for 55 LICs.

<sup>154</sup> EFF "medium term" lending provided member states funds for three years, a seven year grace period, and a ten year repayment period.

<sup>155</sup> Polak, "The World Bank and IMF," p.480.

economies and their legal systems and linked reform to broader issues of development.<sup>156</sup> Structural conditionality focused on liberalizing economies became the new norm of Fund and Bank policies following the 1982 Mexican debt crisis.

### **1982-1996: The Washington Consensus and Liberal Market Restructuring**

By the early 1980s, LICs accounted for 44 percent of the IMF's membership and over 60 percent of its borrowers.<sup>157</sup> These states faced a series of daunting challenges sparked by a perfect storm of events from 1979-1982. The second oil crisis of the decade cut into national income for non-oil producing states and reinforced already existing patterns of high inflation across the global South. Inflationary concerns were not limited to LICs, as the U.S. Federal Reserve dramatically curtailed monetary supply from 1979 to 1982. The subsequent combination of higher interest rates for global debtors and reduced demand from industrialized states for their products pushed up unemployment, increased balance of payments deficit and debt levels, and reduced access to cheap private financing.

The initial response to the 1979 oil shock included increased pressure from borrowers and creditors on the Fund to increase LIC lending. Managing Director Jacques de Larosière (1978-1986) responded in kind with a strategy pushing for increased conditional lending. With a move toward greater use of SBAs and the EFF for LICs, overall Fund upper tranche conditionality lending grew from an annual average of \$1.25 billion in 1973-1978 to \$3.23 billion from 1979-1984.<sup>158</sup>

Fall out of the 1982 Mexican debt crisis also proved a significant factor in the Fund's relationship with its poorest member states. Here, IMF conditionality requirements that emerged worked to dismantle

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<sup>156</sup>Nitsan Chorev and Sarah Babb, "The Crises of Neoliberalism and the Future of International Institutions: A Comparison of the IMF and the WTO," *Theory and Society* 38 (2009), pp.459-484 at p.465.

<sup>157</sup> Boughton, "Lending to and for the Poor," p 55.

<sup>158</sup> Boughton, *Silent Revolution*, p.563.

the remnants of state-heavy ISI strategies seen as responsible for high inflation, corruption, inefficiency, and chronic balance of payment problems across much of the developing world at the time. As introduced in chapter 1, these were described as “Washington Consensus” reforms and included trade and financial liberalization; privatization of state enterprises; reduction and elimination of subsidies; liberalization of labor markets, restructuring taxation toward consumption based systems; and strengthened institutional protection of private property rights.

Washington Consensus reforms were pursued in LICs through two concessionary lending arrangements. In 1986, the IMF introduced the Structural Adjustment Facility (SAF). The SAF merged concessionary lending (0.5 percent interest, ten year maturity, and repayment in 5 ½ years) and structural conditionality requirements into one loan program for the first time. Using IDA eligibility as the income criterion for access to the three-year SAF, 60 LICs qualified to draw from approximately \$3.2 billion in lending resources.<sup>159</sup> Conditionality requirements of the SAF were designed to be stricter and broader than those previously enacted under the Trust Fund. Whereas the Trust Fund was designed to “carry out programs of balance of payment adjustment,” policy reforms in SAFs were spelled out in a Policy Framework Paper (PFP) where the member state in question would outline “a three-year adjustment program...to correct macroeconomic and structural problems that have impeded balance of payment adjustment and economic growth.”<sup>160</sup> The PFP process also included World Bank participation at various steps. After a state requested a SAF loan, Fund and Bank staff collaborated to draft an initial PFP to be negotiated with country authorities. Once the PFP negotiation process was complete, the Bank’s Executive Board would review the agreement and

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<sup>159</sup> Ngaire Woods, “Governance Matters: The IMF and Sub-Saharan Africa,” in *Finance, Development and the IMF*, ed. James Boughton and Domenico Lombardi (Oxford.: Oxford University Press, 2009) pp.229-246 at p.235.

<sup>160</sup> Jacques Polak, “The Changing Nature of IMF Conditionality,” *Essays in International Finance*, no.184 (1991), pp.18-19.

forward its recommendation to the Fund's Board. Despite low funding levels, stricter conditionality, and a cumbersome review process, 29 countries borrowed a total of \$2.4 billion through the SAF program from 1987 to 1999.<sup>161</sup>

The Enhanced Structural Adjustment Facility (ESAF), initiated in 1987, tripled the resources available to qualifying states through the establishment of the ESAF Trust. LICs applying to the ESAF also could draw on a substantially higher percentage of their quota (140- 185 percent over three years) than under the SAF (63.5 percent). To strengthen conditionality requirements, the ESAF introduced procedures that linked semiannual disbursement of funds to successful completion of PFP negotiated “structural benchmarks” and “structural performance criterion.” Performance criteria, eliminated in 2009, were easily measurable benchmarks set by the Executive Board that a member state was expected to adopt before further disbursement of loans. Failure to meet performance criteria required a waiver from the Executive Board for any future distribution of loan resources. Structural benchmarks, also approved by the EB, “are applied to measures that cannot be specified in terms that are objectively monitorable, or to measures where non-implementation to a single component would not be judged sufficient to derail the program.”<sup>162</sup> Between 1988 and 1999, the ESAF became the primary concessional loan instrument of the Fund, disbursing over \$10.7 billion in lending through 90 arrangements to 52 LICs.<sup>163</sup>

## **Conclusion**

Six trends from 1945-1996 highlight the Fund's contemporary role in formally and informally shaping LIC policy choices. First, the focus of the Fund shifted from industrial economies to poor states during

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<sup>161</sup> Boughton, *Silent Revolution*, p.654.

<sup>162</sup> IEO, “Evaluation of Structural Conditionality in IMF-Supported Programs,” (Washington, DC: IMF, 2008), p.4.

<sup>163</sup> <http://www.imf.org/external/np/exr/facts/esaf.htm>

this time. By the 1960s, less than 10 percent of Fund lending went to OECD members, and from 1975 to 2007, no Western industrialized states received Fund loans.<sup>164</sup> Second, since the establishment of Polak-inspired conditionality in the 1950s, members are granted access to resources contingent on implementation of Fund-directed policies. While these conditions changed over time, the leverage of the Fund to impose rules or reform remains in place in LICs. Third, the Fund evolved to fill an informal role as gatekeeper for member access to World Bank loans, other multilateral assistance, and private banks. Fourth, adoption of the Polak model shaped how the institution perceived economic problems in LICs and the general formula for corrective action. Balance of payments problems and broader economic performance were considered primarily the fault of deficit states. Adjustment and belt tightening in LICs, rather than a focus on the behavior of surplus states or instability in global markets, is the primary lens through which policy is developed and implemented.

Fifth, the Fund's focus on statistics and technical data as the basis of policy decisions influenced what data member states measured and the rules and procedures undertaken to collect this information.<sup>165</sup> Member governments, in turn, responded by creating new categories of measurement and subsequent policy focus. And finally, the framing of Fund policy choices and technical assistance as based on objective, apolitical "facts" and econometric modeling helped established the Fund as a legitimate authority in LICs. As outlined by Barnett and Finnemore,

The IMF uses rules to reason and also to justify and explain its decisions to its publics, and in this way is no different from the UN Secretariat or UNHCR...But its form of reasoning is different because of its reliance on quantitative analysis...Because analyses based on numbers, models, and rules seem impartial and fair, they are a defense against accusations of politicized and unprofessional behavior that can undermine bureaucrats' authority as experts. Indeed, it is the objective and depoliticized nature of these policy

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<sup>164</sup> Chorev and Babb, "The Crises of Neoliberalism and the Future of International Institutions: A Comparison of the IMF and the WTO," p.470.

<sup>165</sup> Barnett and Finnemore, *Rules for the World*, p.70.

recommendations that allows them to garner political support and mobilizes people to implement the recommended policies.<sup>166</sup>

Establishment of legitimate authority in turn supplemented the Fund's growing power in shaping LIC outcomes.<sup>167</sup>

This power remains today and is manifested in multiple forms.<sup>168</sup> As outlined above, the Fund exhibits compulsory power in its ability to directly alter LIC behavior through denial of funds or categorization of a member state as off the "right track." Its more indirect institutional power stems primarily from its bilateral and multilateral surveillance and technical support activity. The Fund also has a specific way of categorizing economies and their progress, and uses particular data points to determine if a LIC is meeting benchmarks necessary for continued or future funding. Through data collection and determination of what problems exist in LICs to be solved and how these problems should be addressed, the Fund exhibits productive power in helping to constitute "what matters" in these societies. Finally, the Fund's engagement in LICs also reflects broader structural power relations highlighted by neo-Marxist scholars. As developed further in chapter 5, the IMF's policy directive in LICs can be interpreted as one component of broader processes that facilitate and reproduce the state forms and policy choices necessary for globalizing capitalism.<sup>169</sup>

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<sup>166</sup>*Ibid.*, p.69.

<sup>167</sup> For a discussion of different forms of authority seen in post -World War II international organizations ("rational-legal, delegated, moral, and expert"), see Michael Barnett and Martha Finnemore, "The Power of Liberal International Organizations" in *Power in Global Governance*, eds. Michael Barnett and Raymond Duvall (Cambridge: Cambridge University Press, 2005), pp.161-175.

<sup>168</sup> I draw from Barnett and Duvall's typology of power that divides power into four primary forms: compulsory, institutional, structural and productive. See Michael Barnett and Raymond Duvall "Power in Global Governance," in *Power in Global Governance*, ed. Michael Barnett and Raymond Duvall (Cambridge.: Cambridge University Press, 2005), pp.1-22.

<sup>169</sup> Mark Rupert "Class Power and the Politics of Global Governance," in *Power in Global Governance*, ed. Michael Barnett and Raymond Duvall (Cambridge.: Cambridge University Press, 2005), pp.200-214.

Two prominent themes developed in chapters 1 and 2 thus highlight the rationale for an in-depth study of contemporary post Washington Consensus IMF LIC reform. First, the Fund “matters” in regard to LICs and will continue to play a prominent role in early 21<sup>st</sup> century development outcomes. It is in the best interest of those inside and outside the IMF to understand what dynamics facilitate change in its policy directives. Second, while the role of the IMF in LICs is firmly established, the post Washington Consensus period has produced a more complex landscape of how the Fund expresses its power and leverage in LICs. Rather than a strict top-down, “one size fits all” development model pushed by IMF during the Washington Consensus period, the past two decades are marked by a more consensual and multilayered reality. The complexity of this dynamic is reinforced further by LIC staff that exhibit greater openness and flexibility than their peers in other more prominent departments in the institution. In chapter 3, we begin unpackaging the multiple layers of post Washington Consensus LIC policy reform.

### **Chapter 3 - Coalitions of Change: Rationalist Explanations of LIC Reform**

Chapter 3 investigates four cases of post Washington Consensus LIC reform through a framework that combines principal agent modeling and elements of sociological organizational theory. It identifies four patterns in regard to LIC policy reform. First, two tiers of actors were involved in LIC change. Primary actors included powerful states, the Managing Director, and senior staff. Secondary actors consisted of poor states, NGOs, and the U.S. Congress. Policy change occurred only when a coalition made up of two primary actors or a primary actor and secondary actor formed. Second, as hypothesized by principal agent theory, increases in powerful state preference heterogeneity granted staff and management greater room to initiate or resist policy change. Third, direct NGO pressure proved most effective when a sympathetic primary actor was present. Fourth, individuals in the Strategy, Policy, and Review Department and African Department and the Managing Director were key actors who reinforced coalitions around LIC change.

#### **Theorizing IO Change: PA Modeling and SO Theory**

IO scholars Daniel Nielson, Michael Tierney and Catherine Weaver contend that stand alone rationalist and sociological organizational (SO) approaches fail to effectively explain change in multilateral institutions. Rationalist approaches, grounded in principal-agent (PA) theory, have difficulty explaining why some patterns of institutional behavior remain in place even when heavily targeted for change by powerful state actors or management. SO approaches reciprocally fail to explain why staff opposed to certain reform initiatives concedes to powerful state or management demands seemingly at odds with the institution's culture. Nielson et al. call for an "empirical



synthesis” of PA modeling and SO theory to best capture the interplay of “top down” and “bottom up” dynamics.<sup>170</sup>

PA models ground their analysis in the following two assumptions. First, IOs are not simply manifestations of powerful state preferences in the international system.<sup>171</sup> Rather, they are entities in and of themselves and exhibit relative autonomy from powerful states: “We emphasize the importance of IOs as *actors* that implement policy decisions and pursue their own interests strategically.”<sup>172</sup>

Despite political agency, IOs face constraints on policy direction, as they are ultimately granted conditional authority by states to perform tasks in the international system. In PA parlance, states are “principals” that delegate authority to IOs through formal or informal “contractual” agreement.<sup>173</sup> IOs are “agents” that function within the constraints of conditional grants of authority. This dynamic sets up a fluid situation witnessed by changing degrees of “agency slack” and “autonomy.” Agency slack refers to “independent action by an agent that is undesired by the principal.” Autonomy is the range of potential independent action available to an agent after the principal has established mechanisms of control.<sup>174</sup>

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<sup>170</sup> Daniel Nielson, Michael Tierney, and Catherine Weaver, “Bridging the Rationalist-Constructivist Divide: Re-engineering the Culture of the World Bank, pp.107-111.

<sup>171</sup> Nielson and Tierney, for example, argue that realist frameworks simply ignore IOs or argue they are best thought of as direct extensions of powerful state preferences in the international system. PA proponents are also critical of neoliberal institutional framing of state agency. While focused on the role of IOs as important actors in lowering transaction costs and producing internal cohesion between states, neoliberal institutionalists historically have conceptualized IOs as reactive and unable to produce policy independent and outside the will of member states. See Daniel Nielson and Michael Tierney, “Delegation to International Organizations: Agency Theory and World Bank Environmental Reform,” *International Organizations* 57 (2003), pp.241-276 at pp.243-244.

<sup>172</sup> Darren Hawkins, David Lake, Daniel Nielson and Michael Tierney, “Delegation Under Anarchy: States, International Organizations, and Principal-Agent Theory,” in *Delegation and Agency in International Organizations*, ed. Darren Hawkins, David Lake, Daniel Nielson and Michael Tierney (Cambridge.: Cambridge University Press, 2006), pp.3-38 at p.5.

<sup>173</sup> Contracts in this context are defined as “self-enforcing agreements that define the terms of the relationship between the two parties.” See Hawkins et al., “Delegation Under Anarchy: States, International Organizations, and Principal-Agent theory,” p.7.

<sup>174</sup> *Ibid.*, p.8.

PA theory maintains that the nature of the contractual relationship produces predictable dynamics concerning institutional behavior and change. For the principal, the main concern is how authority is delegated without losing control. Agents are opportunistic and commonly engage in several forms of behavior to increase slack and autonomy. Most common are processes that hide information or involve taking action behind the back of the principal.<sup>175</sup> For their part, states reduce “agency slippage” through five primary mechanisms. First, they formally determine what authority is delegated to the IO and have the power to alter contracted agreements. Second, principals have control of the selection, hiring, and firing of IO management. Third, agents also can monitor principals directly or through third parties. Fourth, principals can structure IOs in a manner that keeps individuals in the institution in check. This is accomplished through creation of institutional checks and balances or through empowering more than one agent with the same mandate (e.g., adjustment lending in both the Bank and Fund). Finally, states can punish or reward the IO. In the case of the IMF, states ultimately can withhold funding of quota resources.<sup>176</sup>

PA models also focus on the form of principal agent relationships. At its simplest, PA models involve a single principal delegating to a single agent (see Figure 3.1 below). In reality, delegation of authority to agents often involves a principal made up of multiple actors (“collective principal”) or a situation where a single agent has more than one contract with organizationally distinct principals (“multiple principals”).<sup>177</sup> All else being equal, PA models predict greater agency slack and autonomy as the number of principals increases. Room for agents to shirk principal demands also is predicted to increase as divergence in preferences among principals (“preference heterogeneity”) increases.

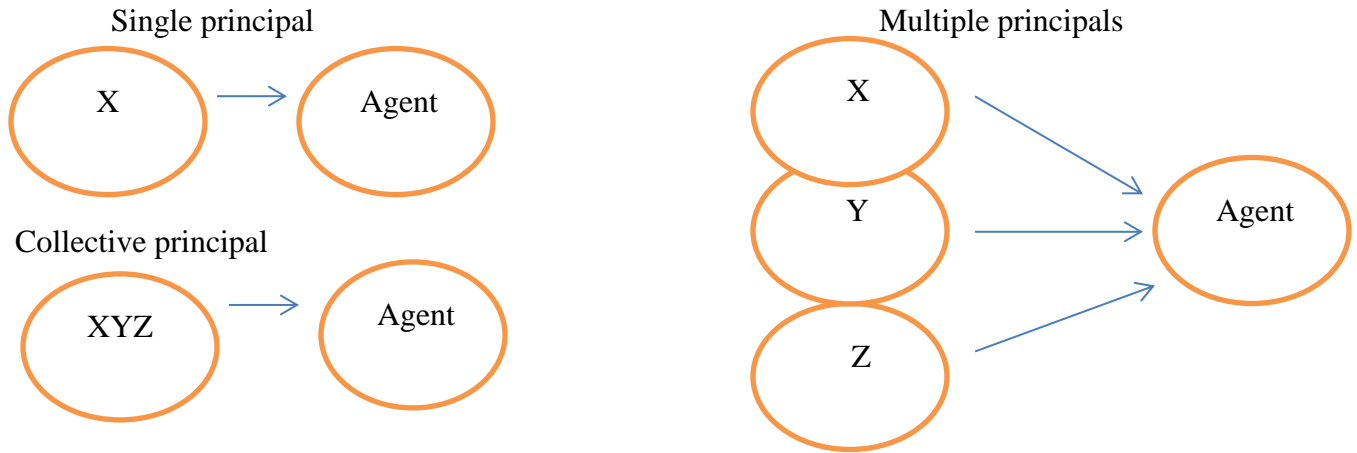
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<sup>175</sup> Nielson and Tierney, “Delegation to International Organizations: Agency Theory and World Bank Environmental Reform,” p.246.

<sup>176</sup>Hawkins et al., “Delegation Under Anarchy: States, International Organizations, and Principal-Agent Theory,” pp.26-30.

<sup>177</sup> Mona Lyne, Daniel Nielson, and Michael Tierney, “Who Delegates? Alternative Models of Principals in Development Aid,” in *Delegation and Agency in International Organizations*, ed. Darren Hawkins, David Lake, Daniel Neilson and Michael Tierney (Cambridge: Cambridge University Press, 2006), pp. 41-76 at pp. 43-45.

Figure 3.1: Types of PA Relationships



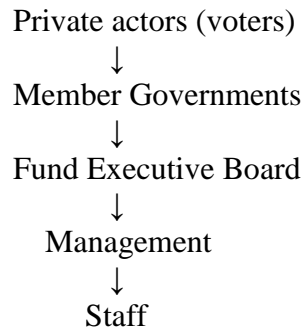
(Source: Lyne et al., “Who Delegates?,” p.45)

PA models also focus on what are termed “proximate” principals in predicting IO change (see figure 3.2 below). In a delegation change visualized here for the Fund, the proximate principal is the entity with the closest formal authority to the agent in question. While pressure for change may come from actors (voters, NGOs) several places removed in the delegation chain (“distal principals”), Fund management and staff will most likely ignore these demands and instead focus on signals from their proximate principal: “Because staff members of IOs are not rewarded, or may even be punished if they respond too vigorously to stimuli other than the demands of their proximate principal, they should tend to ignore or discount demands made by interest groups in given member countries.”<sup>178</sup> PA models thus predict little change due to NGO “street heat” or direct lobbying of the Fund. Rather, NGO pressure on states should prove more effective in producing reform in policy direction.

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<sup>178</sup> Nielson and Tierney, “Delegation to International Organizations: Agency Theory and World Bank Environmental Reform,” p.250.

Figure 3.2: Hypothetical Chain of Delegation for IMF



PA modeling is incorporated to clarify the outer structural constraints within which IO policies may diverge from state (or managerial) preferences and which actors carry the greatest leverage over policy choices. Answers to how and why the Fund changes policy direction within semi-autonomous relationship with principals instead draws from sociological organization (SO) theory. SO theory assumes that IOs have their own internal social life, norms, and organizational culture through which external demands from states, NGOs or senior management are refracted and internally processed. It also holds that internal policy culture and subsequent policy choices may sometimes even change without external pressure and develop a path-dependent life of their own potentially at odds with powerful state interests.<sup>179</sup>

Several variables that can shift internal culture and policy choices are identified in the SO literature. Foremost is the role of internal “norm entrepreneurs.” Individuals pushing a new idea will command the greatest influence if they occupy a position within the bureaucracy that: (1) has access to management; (2) can serve as a veto point for policy initiatives; and (3) has access to resources.<sup>180</sup>

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<sup>179</sup> Antje Vetterlein, “Economic Growth, Poverty Reduction and the Role of Social Policies. The Evolution of the World Bank’s Social Development Approach,” *Global Governance* 13, no.4 (2007), pp.513-533 at p.515.

<sup>180</sup> Jeffrey Chwieroth, “Organizational Change ‘From Within’: Exploring the World Bank’s Early Lending Practices,” *Review of International Political Economy* 15, no.4 (2008), pp. 481-505 at p.494.

Staff and management also maneuver through the organizational bureaucracy, promoting new beliefs that can potentially alter the organization's culture and practices.<sup>181</sup> These agents promote particular policy outcomes through three primary avenues.<sup>182</sup> First, they interpret historical experience through the assumptions and worldviews that will support their ideas and actively search for evidence that will reinforce their beliefs. Second, these actors may also engage in small scale experiments to test their assumptions. In the IMF, for example, this dynamics is seen when staff circulate position papers or articles published in *Finance and Development* that explore and test questions concerning appropriate policy response. Third, actors that push for change will also engage strategically in ideological battles to win support for their ideas.<sup>183</sup>

The ultimate success of reforms proposed also is tied to the form and depth of change advocated. When staff interpret new information and events that fail to meet expected outcomes, "they tend to change their beliefs about legitimate means in an ad hoc fashion rather than changing their beliefs about legitimate goals."<sup>184</sup> Shifts in thinking and subsequent policy choice reform are therefore most likely due to "adaptation." Defined as a change in beliefs about desirable means to reach a policy outcome, this is manifested in various forms including "changes in organizational language, structures, symbols, and small modifications of behavior."<sup>185</sup> Adaption differs from more fundamental processes of "learning." Rather than questioning the efficacy of *policy process* to achieve a certain outcome, learning challenges *policy goals*. Given that learning is a deeper process of change that can

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<sup>181</sup> *Ibid.*, p.492.

<sup>182</sup> Jack Levy, "Learning and Foreign Policy: Sweeping a Conceptual Minefield," *International Organization* 48, no. 2 (1994), pp.279-312 at pp.282-283.

<sup>183</sup> Nielson et al., "Bridging the Rationalist-Constructivist Divide: Re-engineering the Culture of the World Bank," p.114.

<sup>184</sup> *Ibid.*, p.54.

<sup>185</sup> Chwioroth, *Capital Ideas*, p.52.

fundamentally challenge organizational culture, SO theorists predict that IO policy shift occurs most frequently through processes of adaption.<sup>186</sup>

Successful reform also hinges in part on the degree of discursive influence individuals hold. Seasoned staff and management considered authorities advocating change encounter less resistance from less senior colleagues. Position in the bureaucracy also matters. Staff situated in leadership positions more easily lobby management, initiate or block potential reforms, and control information.<sup>187</sup> Specific to LIC policy reform at the Fund, we should expect that senior staff found in the Africa, SPR, and Research Departments are key gate-keepers that influence the potential success or failure of reform efforts.

### **PA Modeling, SO Theory and Fund Policy Change**

For purposes of this project, I focus on two levels of delegation (see Figure 3.3 below): State to Fund management (level 1) and management to staff (level 2). At level 1, powerful states represented by the Fund's Executive Board serve as the collective principal. Member states of the Fund delegate authority to the 24 member executive board (EB), which oversees day to day operations of the Fund. As noted in chapter 2, each Executive Director (ED) has different weighted voting power based on quota size of state(s) represented. The U.S., Germany, Britain, Japan, and France each have individual representation on the EB and the largest weighed voting power since 1945. Decisions on the EB are mainly finalized through consensus rather than formal votes and require coalitions built around support of the above shareholders, particularly the United States.<sup>188</sup> Along with the greatest voting

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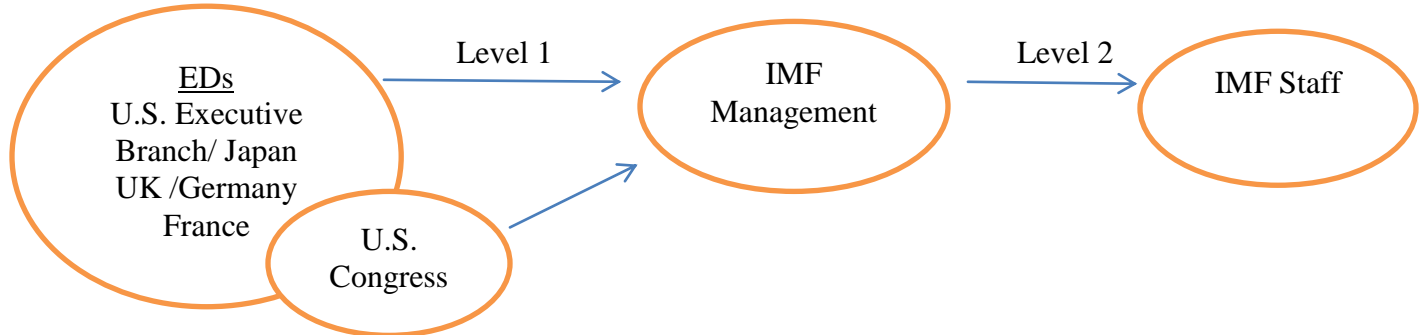
<sup>186</sup> *Ibid.*, p.113.

<sup>187</sup> Chwieroth, "Organizational Change 'From Within': Exploring the World Bank's Early Lending Practices," p.494.

<sup>188</sup> Rule C-10 of the IMF Rules and Regulations states, "the Chairman shall ordinarily ascertain the sense of the meeting, in lieu of a formal vote." As noted by Van Houtven, a "sense of meaning" translates into knowing when there is enough consensus on the EB to approve a policy change if a vote were taken. See Leo Van Houtven, "Governance of the IMF: Decision Making, Institutional Oversight, Transparency, and Accountability," IMF Pamphlet Series No. 53 (Washington, D.C. :IMF, 2002), pp.23-4.

share, the U.S. differs from other powerful states in its presidential government design. The model below therefore includes the U.S. Congress as an additional principal that can contract with Fund management.<sup>189</sup>

Figure 3.3: Principals at Two Levels of Delegation Chain



Congress confirms the ED appointed by the President and must approve any quota increase to the Fund. Congress also must consent to any supplemental lending to the IMF via the General Arrangement of Borrowers (GAB), the New Arrangement of Borrowers (NAB), and sale of IMF gold resources. In addition, Congress passes mandates that direct the Secretary of the Treasury to instruct the U.S. ED to pursue specific policy objectives:

Policy mandates seek to foster or advocate certain policies at the IMF by directing Treasury to instruct the U.S. Executive Director to use his or her “voice,” “vote,” or both, on behalf of the United States at the Executive Board to bring about a policy change at the IMF. For example, the U.S. Executive Director is directed to encourage the IMF to adopt internationally recognized worker rights for borrowing countries. Directed vote mandates are more prescriptive, in that they instruct the United States to “oppose” or “vote against” loans or other IMF assistance to particular countries or categories of countries.<sup>190</sup>

<sup>189</sup>This model is drawn from Nielson and Tierney’s conception of principal-agent relationship between the U.S. and World Bank. The authors also note that divided power between legislative and executive branches also occurs in France during periods of cohabitation. See Nielson and Tierney, “Delegation to International Organizations: Agency Theory and World Bank Environmental Reform,” p.255.

<sup>190</sup> Government Accountability Office, *Treasury Has Sustained its Formal Process to Promote U.S. Policies at the International Monetary Fund*, GAO-06-876R (Washington, D.C: June 29, 2006), pp. 2-3.

As of 2005, the Government Accountability Office has identified 70 legislative mandates passed by Congress since 1945.

As outlined in chapter 2, the Fund's operational culture is characterized by hierarchical and bureaucratic tendencies. The staff is also rooted in a scientific, technocratic worldview that is consistent with analysis found in the broader epistemic and professional economics field. Shifts in LIC policy should not be expected to occur rapidly or be shaped extensively by political pressure from outside the institution. Reform of LIC policy is also more likely if the reform in question resonates or is packaged in way that is congruent with a culture historically supportive of liberal market solutions to development issues (see chapter 4).

Drawing from the PA and SO frameworks, the following hypotheses are derived for explaining LIC policy change:

*H1: If pressure for LIC policy change comes from staff and runs counter to state or management preferences, increased/decreased heterogeneity of principal preferences strengthens/weakens the ability of staff working to shift policy direction.*

*H2: If pressure for LIC policy change comes from state principal demands on the Fund and runs counter to internal staff and management interests, increased/decreased heterogeneity of state preferences weakens/strengthens the ability of management and staff to shift policy direction.*

*H3: LIC policy change only occurs due to proximate principal pressure. Direct NGO or citizen ("leapfrogging") pressure on the Fund will not produce LIC policy change.*

*H4: A strategically situated "norm entrepreneur" is a necessary component of LIC policy change when the change in question challenges the Fund's institutional culture.*

*H5: Framing of policy reform shifts as a need to address policy implementation (adaption), rather than a fundamental challenge to Fund thinking on macroeconomic policy (learning), and increases the change of subsequent implementation of reform in LIC policy choices.*



## **Highly Indebted Poor Country Initiative (HIPC)**

Liberal market policy positions pushed by SAF and ESAF structural conditionality (see chapter 2) sets the stage for examination of the first substantial shift in Fund policy away from a strict Washington Consensus model. Facilitated in part by growing evidence of stagnant growth and rising inequality and poverty across much of the developing world in the 1980s, critics of the IMF and World Bank argued that conditional lending to LICs was a primary cause of unsustainable debt levels and called for substantial multilateral debt relief.

The debate around debt relief first formally emerged in Paris Club<sup>191</sup> negotiations of bilateral debt levels in the 1980s. The general consensus from creditor states at the time was that debt levels of poor states were manageable if correctly addressed. Rather than debt forgiveness, extension of terms of payment or reduction in interest rates was seen as the appropriate response for bilateral agreements. By the mid-1980s, growing debt levels – particularly in sub-Saharan Africa – prompted British officials to propose a framework of bilateral debt relief through the Paris Club. The proposal, introduced by UK Chancellor of the Exchequer Nigel Lawson in 1987, called for Club members to convert bilateral aid loans to grants, increase repayment periods to twenty years, and reduce the rate of interest on outstanding debt by one-third for debtor states in good standing with the Fund.

British lobbying continued through 1987 and 1988 at the Paris Club, the Venice and Toronto G-7 Summits, the Commonwealth Finance of Ministers, and IMF/World Bank Annual meetings. Despite

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<sup>191</sup> The Paris Club is an informal group currently made up of 19 countries (primarily from the OECD) and chaired by the French Treasury. Meeting every six weeks in Paris, it seeks “to find coordinated and sustainable solutions to the payment difficulties experienced by debtor countries.” The IMF plays a prominent role in Paris Club negotiations, as any commitment to rescheduling debt often requires the debtor state in question to have an active Fund program in place and be in good standing with reform efforts. Since 1956, 422 agreements with 88 debtor states have been reached. See <http://www.clubdeparis.org/en/>.

initial broad opposition from other rich states (Germany, Japan, and the U.S.), the G-7 endorsed the “Toronto Terms” in 1988. Through the Paris Club, creditors could choose from three options for dealing with debtor states: long-term rescheduling, lower interest rates, and a partial write down of stock of debt.<sup>192</sup> Inertia toward bilateral debt relief was further enhanced with several U.S. initiatives, including the 1989 Brady plan,<sup>193</sup> and a 1991 reduction of Egyptian debt for its contribution of military forces in the first Gulf War. Further proposals increasing bilateral debt relief pushed by the UK were adopted throughout the early 1990s, culminating in the Lyon Terms agreement at the 1996 G-7 Summit. Under this agreement, highly indebted states in good standing with the Fund and Bank could have up to 80 percent of bilateral debts written off through the Paris Club.<sup>194</sup>

As bilateral debt relief increased through the late 1980s and early 1990s, the percentage of debt owed to multilateral institutions increased substantially.<sup>195</sup> In addition to calls from NGOs (see below), the UK (along with the Netherlands and the Nordic states) formally initiated the notion of Fund and Bank debt relief for LICs at the 1994 spring meetings of the IMF and World Bank. Although broadly resisted by the majority of wealthy states and management at the Fund,<sup>196</sup> growing pressure to examine multilateral debt relief continued. Along with lobbying by the UK and NGOs, newly appointed World Bank President James Wolfensohn was sympathetic to looking at the issue.<sup>197</sup>

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<sup>192</sup> Huw Evans, “Debt Relief for the Poorest Countries: Why Did It Take So Long?,” *Development Policy Review* 17 (1999), pp.276-279 at pp.268-270.

<sup>193</sup> U.S. Treasury Secretary Nicholas Brady argued that debt reduction was necessary for some highly indebted states to regain creditworthiness. The Brady Plan stipulated that commercial banks in the U.S. that reduced principal or interest on debt would receive guarantees of repayment on remaining debt. Along with Japan, the Fund and Bank financed debt guarantees for 17 states (mostly from Latin America) from 1990 to 1997.

<sup>194</sup> Boughton, “Lending to and for the Poor,” p.57.

<sup>195</sup> By 1996, highly indebted poor countries paid nearly half of their debt payments to multilateral creditors.

<sup>196</sup> Both the Fund and World Bank sought to defend their position as “preferred creditors” as the debate on multilateral debt relief heated up. As preferred creditors, loans and interests were paid to the Fund and Bank before commercial banks or states.

<sup>197</sup> See Catherine Weaver, *Hypocrisy Trap: The World Bank and the Poverty of Reform*, p.140. Wolfensohn, appointed in 1995, unveiled a thirty-month, \$250 million reform effort (entitled the “Strategic Compact”) in 1996. As noted by Weaver, “The core objective...was to reestablish the Bank’s preeminent position as the world’s leading development agency by

In February 1995, The Fund and Bank staff presented a joint paper on issues of debt sustainability and concluded that for the majority of LICs “debt service ratios on currently outstanding multilateral debt will be essentially unchanged or lower in the coming three years (1995-1997) and will decline further in most cases over the next decade.”<sup>198</sup> As such “there was no unmanageable hump of debt servicing to multilaterals for the vast majority of heavily indebted poor countries.”<sup>199</sup>

Reaction at the Executive Board was mixed. At a February 24 meeting, critics of the staff report most sympathetic to multilateral debt relief included the EDs from the UK (Evans), Nordic states (Srejber), and those representing LICs (Dlami and Koissey). Evans, for example, concluded “...that the problem is more serious than the Fund staff paper admits. And that the Fund has a role in resolving the problem.”<sup>200</sup> The U.S. (Lissakers) and Canada (Clark) provided more reserved support. Clark argued “that the Fund and Bank cannot be grant agencies. Nevertheless these multilateral credit organizations cannot ignore that their interest charges...divert some productive resources away from the debtor country.”<sup>201</sup> EDs from Germany (Esdar), Japan (Mesaki), France (Autheman), and Italy (Grilli) resisted calls for debt relief. Division of powerful state preferences on the issue of debt relief remained in subsequent EB debates in 1995 and 1996. Most notable was U.S. movement from a mild supporter of the UK position to a strong advocate for debt relief in 1996. ED Lissakers, for example, critiqued an

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instigating a massive transformation in the way the organization goes about its core mission of promoting economic growth and alleviating world poverty.”

<sup>198</sup> IMF, *Issues and Developments in Multilateral Debt and Financing in the Heavily Indebted Countries-Preliminary Considerations*, SM 96/57, 7 February 1995 (IMF Archives), p. 3.

<sup>199</sup> SM 96/57, p.2 as quoted in Bessma Momani, “Internal or External Norm Champions: The IMF and Multilateral Debt Relief,” in *Owning Development: Creating Policy Norms in the IMF and World Bank*, ed. Susan Park and Antje Vetterlein (Cambridge: Cambridge University Press, 2010), pp.29-47 at p.35.

<sup>200</sup> IMF, *Minutes of Executive Board Meeting*, EBM 95/ 12, 24 February 1995 (IMF Archives), p. 8 as quoted by Momani, “Internal or External Norm Champions: The IMF and Multilateral Debt Relief,” p.36.

<sup>201</sup> EBM 95/ 12, p. 14 as quoted by Momani, “Internal or External Norm Champions: The IMF and Multilateral Debt Relief,” p.36.

April 2, 1996 revised staff proposal on multilateral debt relief as biased and too rigid to effectively address debt issues in LICs:

...the proposed framework would not give the Fund sufficient flexibility to assess the needs of individual cases, including those where it might be appropriate to take bolder actions in tandem with other bilateral and multilateral creditors within a shorter time frame to provide effective debt relief and place the country on a path toward higher rates of sustainable growth.<sup>202</sup>

France, Germany, and Japan remained staunchly opposed to the UK and U.S. position and were even critical of staff's reference to poverty issues in the report. Japanese ED Mesaki, for example, stated:

...it would not be appropriate to indicate that...principal donors and multilateral creditors...undertake to implement a set of measures aimed at the achievement of a sustainable debt level consistent with a country's strategy to improve growth prospects and reduce poverty. The Fund's efforts should be aimed at helping countries strengthen their overall macroeconomic framework, not at achieving objectives related to longer-term growth or to social issues.... Therefore, we did not see a need to expand on the prospective role of the Fund in resolving the debt problem of the HIPCs.<sup>203</sup>

Despite this division, there was consensus among wealthy states that any program on debt relief going forward would require strong conditionality requirements and continual staff oversight.<sup>204</sup>

Staff was generally skeptical of any moves toward debt relief. As noted above, an initial paper on the issue of debt sustainability in LICs issued on February 7, 1995 maintained the majority of poor states could manage debt levels. This conclusion was based on assumptions of annual nominal export growth rates of 6 percent and annual nominal 3 percent growth rate of new concessional lending. When challenged by NGOs on these figures, the Executive Board asked staff to revisit the issue. A March 30 revised staff report increased the number of countries that could be adversely affected from 8 to 23 but argued again that multilateral debt was manageable if sufficient concessional lending came

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<sup>202</sup> IMF, *Minutes of Executive Board Meeting*, EBM 96/ 34, 8 April 1996 (IMF Archives), p. 3.

<sup>203</sup> EBM 96/34, p.9.

<sup>204</sup> See EBM 96/34, p.4. U.S. ED Lissakers, while critical of the staff report on most counts, "strongly agreed with the staff that any approach to resolving the debt problems of the HIPCs should be based on strong track records of performance and firm conditionality with respect to policies."

forward.<sup>205</sup> Two further studies requested by the Development Committee and the Board in 1996 focused on individual LIC cases. Staff once again argued that the majority of highly indebted states could pay back multilateral debts. The paper also focused on issues of moral hazard and noted a potential upside to some form of debt relief if the Fund and Bank maintained strong conditionality and oversight of the process:

A potential advantage of refinancing/rescheduling (accompanied by conditionality) relative to explicit up front debt reduction may be that by allowing the Fund and the Bank to constantly monitor policy performances in the indebted countries, it leads to better policies and less moral hazard problems.<sup>206</sup>

In response to an Interim Committee request for some form of debt relief proposal, the staff presented its framework in February 1996. Under a two-step program over a six year period, highly indebted LICs under Fund and Bank surveillance would first be granted up to 90 percent debt relief from Paris Club and commercial creditors. If the LICs met Fund and Bank standards of reform, they then would graduate to phase two where debt owed to the Fund, Bank, and other multilateral institutions would be reduced to sustainable levels.

Along with staff, management was wary of HIPC. Camdessus supported staff positions in regard to debt sustainability and rejected calls for substantive multilateral debt relief:

I would conclude...there does not seem to be at this stage a generalized problem of debt to multilateral institutions...For the Fund, the clear implication is the need to have available resources on ESAF terms for the foreseeable future...there appears to be no need for major changes in the Fund's facilities or in their concessionality for most of the poorest members.<sup>207</sup>

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<sup>205</sup> IMF, *Issues and Developments in Multilateral Debt and Financing in the Heavily Indebted Countries-Further Considerations* (Washington, D.C., IMF, 1995).

<sup>206</sup> IMF, *Analytical Aspects of the Debt Problems of Heavily Indebted Poor Countries*, SM/96/23, 31 January 1996 (IMF Archives), p.40.

<sup>207</sup> IMF, *Concluding Remarks by the Chairman: Issues and Development in Multilateral Debt and Financing for the Heavily Indebted Poor Countries-Preliminary Considerations, Executive Board Meeting 95/19*, BUFF 95/18 (IMF Archives), p. 2.

Due to the split between powerful state preferences on staff HIPC proposals in spring 1996, Camdessus advocated for a proposal put forth by the German (Esdar) and Japanese (Mesaki) EDs that the staff position on HIPCs be considered endorsed by management and not the Executive Board.<sup>208</sup> Despite critiques from the UK and U.S. EDs that the staff proposal was too conservative and “neither economically effective and efficient nor politically sustainable,” the split on the board and Camdessus’ support for Esdar’s proposal allowed the staff framework of debt relief to go to the Interim Committee in April 1996. The HIPC initiative was then endorsed by the Board of Governors and Executive Board in September 1996.

In regard to NGO influence on HIPC adoption, methods included indirect pressure on powerful states and direct lobbying of Fund staff and management. Most prominent in shaping Fund policy change on debt was the European Network on Debt and Development (Eurodad) and Oxfam International. Starting in 1994, Eurodad organized a campaign on multilateral debt forgiveness that targeted the Bank and IMF.<sup>209</sup> By 1996, “over 150 NGOs, NGO networks, academics, debt experts, representatives from the UN, UNCTAD, UNDP, the Non-aligned Movement, the Commonwealth Secretariat and other interested institutions” had joined the campaign.<sup>210</sup> NGO pressure was applied indirectly to powerful state legislatures and finance ministers in several venues. Prior to the July 1995 Halifax G-7 summit, for example, Eurodad heavily lobbied G-7 leadership around issues of multilateral debt relief. In its communiqué, the G-7 acknowledged that the “IMF and World Bank should lead in developing a comprehensive multilateral approach to assist countries with multilateral debt and debt-service ratios

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<sup>208</sup> EBM 96/34, p.5.

<sup>209</sup> Partners in the Eurodad campaign included Oxfam, the British Debt Crises Network, the Debt and Development Coalition Ireland, the Nordic Network on Debt and Development, and the Swiss Coalition. See Schölte, “The IMF and Social Movements,” p.169.

<sup>210</sup> Sasja Bokkerink and Ted van Hees, “Eurodad’s Campaign on Multilateral Debt: The 1996 HIPC Debt Initiative and Beyond,” *Development and Practice* 8, no.3 (1998), pp.323-334 at p.324.

above prudent levels in addressing their debt burdens, through the flexible implementation of existing instruments, and new mechanisms where necessary.”<sup>211</sup>

Relative to direct action, Eurodad was also the primary actor that pressured Fund and Bank EDs and management to review the assumptions of the February 7, 1995 staff report initially downplaying the severity of multilateral debt issues. Eurodad, Oxfam, and the Debt Crises Network also actively lobbied Fund management and staff on debt issues, and participated and demonstrated at the joint annual meetings of the Fund and Bank during this time.<sup>212</sup> Religious organizations were also outside players that actively pushed the Fund to address debt relief issues. Catholic Church leadership, for example, met with Camdessus in London and Washington in 1996, where the MD “was reported to have been deeply affected by the meetings as he came face to face with the hostility of world Catholic leaders toward the institutions he led and its economic policies.”<sup>213</sup>

#### *HIPC Results:*

Returning to the hypotheses introduced above, the evidence in the HIPC case points to the following.

*H1-H2:* The division between two blocs of powerful states (U.S./UK and Germany, Japan, and France) allowed the MD and staff to initially block HIPC reform efforts. While pressure from the U.S. and UK and NGOs ultimately led to adoption of the HIPC, the fact that Germany, Japan, and France resisted these efforts increased the leverage of the MD and staff in shaping the final design of debt relief. Strict conditionality requirements and increased surveillance of LICs as a component of debt relief pushed by the staff, for example, were included in the HIPC. This suggests that powerful state preference heterogeneity increased management and staff power in the shaping of reform efforts.

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<sup>211</sup> G-7, Halifax Communique, available at <http://www.g8.utoronto.ca/summit/1995halifax/communique/index.html>

<sup>212</sup> Thomas Callaghy, “Innovation in the Sovereign Debt Regime: From the Paris Club to Enhanced HIPC,” (Washington D.C.: World Bank, Operations Evaluation Department, 2002), pp.19-20.

<sup>213</sup> Momani, “Internal or External Norm Champions: The IMF and Multilateral Debt Relief,” pp.40-41.

*H3:* NGOs applied pressure both on IMF management and staff and on state principals. PA theory maintains that NGO pressure applied directly to IMF management and staff will not have significant impact on Fund policy change. Effective pressure applied to powerful states, in contrast, is hypothesized to produce a dynamic where the IMF responds to the new demands of its proximate principal. In the HIPC case, NGOs applied pressure both directly on Fund management and staff, and indirectly on powerful states in their support of debt relief. While these efforts helped produce a change in policy direction, the evidence from this case is thus unable to definitively discern to what degree direct or indirect pressure helped spur adoption of the HIPC.

*H4:* Evidence does not point to any individual within the IMF who pushed for the HIPC.

*H5:* IMF management and staff initially resisted debt relief for LICs. As documented above, multiple staff position papers initially downplayed the severity of LIC debt and its impacts. When adopted, the HIPC in its final form was framed in a manner that did not fundamentally challenge Fund thinking. Debt relief, for example, was presented in a manner whereby recipient states would see increased conditionality requirements and Fund surveillance.

### **“Enhanced” Highly Indebted Poor Country Initiative (HIPC II)**

The Fund and World Bank replaced the HIPC with the “enhanced” HIPC (HIPC II) in 1999. HIPC II promised to provide “faster, deeper, and broader debt relief” for LICs and tied debt forgiveness to a series of new poverty reduction initiatives introduced with the PRGF (see below). Dynamics leading to the adoption of HIPC II included broad support from a series of actors, including powerful states, LICs, the Managing Director, staff, and NGOs supportive of the initiative. Both liberal and conservative wings of the U.S. Congress also played an active role in pressuring the Fund to adopt HIPC II. As developed below and further in chapter 4, broad support of a more aggressive stance on debt relief and its relationship to both poverty and development outcomes also points to a broader shift



both within the Fund and the broader policy-making community between 1996 and 1999. This is arguably tied in part to the fallout from the Asian crisis, which significantly challenged Fund competence and Washington Consensus policy prescriptions.

NGOs were perhaps the most important actors pushing the Fund to adopt HIPC II changes in 1999. As articulated by a Fund staff member,

The NGO community, having tasted blood with HIPC, decided to push harder...push further. They said we set the sustainability threshold too high... [and the process of debt relief] is taking too long... And there is not enough linkage between debt relief operations that you are doing and the ultimate objectives of reducing poverty. So they pushed for all of these things as part of a reformed HIPC and the international community eventually bowed to that pressure. You have to hand it to the NGOs, they were extremely effective and in some respects, they got it right.<sup>214</sup>

Jubilee 2000, launched in 1996, was the key NGO pushing for HIPC II. Specific to direct lobbying, Jubilee (along with Oxfam and Eurodad) regularly met with EDs, staff, management, and the Development and Interim Committees between 1996-1999 and pressed their concerns. Jubilee 2000 also organized direct action and lobbying campaigns. By 1999, Jubilee had petitions circulating in over 100 countries and had collected over 17 million signatures demanding debt cancellation.<sup>215</sup> It also was a primary player in organizing highly visible demonstrations at the 1998 Birmingham and 1999 Cologne G-7 Summits.

In the U.S., Jubilee 2000 and other NGOs pushed Congress to pressure the Fund in two primary areas. First, lobbying took place to build support for a symbolic Congressional mandate in 1998, instructing the U.S. ED “to use aggressively his voice and vote to enhance the general effectiveness of the IMF

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<sup>214</sup> Author Interview with Fund staff member from Strategy, Policy, and Review Department, Washington D.C., 14 June 2011.

<sup>215</sup> Joshua William Busby, “Bono Made Jesse Helms Cry: Jubilee 2000, Debt Relief, and Moral Action in International Politics,” *International Studies Quarterly* 51, no. 2 (2007), pp. 247-275 at p. 249. In Birmingham, Jubilee helped organize a human ring of over 50,000 supporters of debt relief. In Cologne, over 35,000 Jubilee 2000 supporters turned out for the G-7/8 meetings.

with respect to...core labor standards, social safety nets...especially the world's poorest, heavily indebted countries.”<sup>216</sup> The Jubilee campaign also built a successful coalition of liberal Democrats and conservative Republicans that eventually secured \$435 million of Congressional funding for Fund debt relief.<sup>217</sup> Pressure was also exerted on Congress in 1998 in regards to the Fund's 11<sup>th</sup> Quota review. While much of the critique came from conservative members focused on the fallout from the Asian financial crisis, hearings in Congress included witnesses critical of Fund programs for the poor.<sup>218</sup> NGO pressure also targeted the Clinton administration and governments in the UK, France, and Germany.

Staff and management thinking around the relationship between debt relief and Fund policy objectives in LICs also shifted during the 1996-1999 time period. Most striking was the rise of internal debates about the efficacy of the Polak model when applied to LICs. As noted by a senior staff member in the African Department:

When I first came here, it was all about closing a balance of payment gap. Every program that you designed had to show that the balance of payments gap closed within a three to five year period. If it didn't show this, out the window it went. Starting with... the HIPC's, we started questioning that. If a country is really developing and is really poor, that can't be true. It has to borrow from abroad. In fact, you have to have a balance of payment gap that opens over time, not one that closes.<sup>219</sup>

The primary role of debt relief therefore no longer was seen by staff as a bridge to allow for an orderly process of correcting balance of payments deficits. Rather, it was one tool to allow LICs to *increase* short-term balance of payment deficits that would allow for long-term poverty reduction and subsequent improved development outcomes.

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<sup>216</sup> Government Accountability Office, *Treasury Has Sustained its Formal Process to Promote U.S. Policies at the International Monetary Fund*, p.9.

<sup>217</sup> Busby, “Bono Made Jesse Helms Cry,” pp.266-268.

<sup>218</sup> See U.S. House of Representatives, Subcommittee on General Oversight and Investigations, “Review of the Operations of the International Monetary Fund,” 21 April 21 1998.

<sup>219</sup> Author interview with Fund staff member from the Africa Department, Washington D.C., 13 June 2011.

NGO pressure and internal staff debates led to a joint IMF-World Bank review of the HIPC in 1998. In April 1999, Camdessus and Wolfensohn outlined their position for modifying the initiative. This included:

1. Debt relief should reinforce the tools of the international community with the wider aim of promoting sustainable development and poverty reduction.
2. Debt relief should strengthen the incentives for debtor countries to adopt strong programs of adjustment and reform.
3. Enhanced debt relief should focus on poorest countries.
4. Debt relief should be irrevocable.
5. Simplification of the HIPC framework.<sup>220</sup>

A joint Fund-Staff paper summarizing critiques and possible options going forward was debated at the EB on April 16. Here four areas were discussed: depth, breadth, and timing of debt relief, and issues of conditionality. Most notable was the shift in position of the Japanese (Yoshimura) and German (Esdar) EDs from three years earlier. While wary of debt forgiveness and a move toward development issues in the HIPC process in 1996, they were now open to deeper and quicker debt forgiveness in 1999 and linking debt issues to poverty. Yoshimura, in endorsing a move toward HIPC reform, argued "...social development and poverty alleviation are among the ultimate targets of HIPC countries, and no one disagrees generally on the need for tighter links among debt relief, poverty reduction, and social policies."<sup>221</sup> The German position was more explicit in calls for deepening debt relief and linkages to poverty and reflected the position of the new Social-Democratic government under the leadership of Gerhard Schröder:

We should aim to speed up the debt relief process, so that HIPCs can benefit from debt reduction as early as possible. The debt relief process should lead to an immediate freeing up of internal budgetary resources for poverty reduction measures by granting debt service relief. We should increase the volume of delivered debt reduction, so that more funds can be released for measures to fight poverty and to promote sustainable development. The debt

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<sup>220</sup> IMF, *Annual Report 1999*, (Washington, D.C. IMF, 1999), p.87.

<sup>221</sup> IMF, *Minutes of the Executive Board Meeting*, EBM 99/43, 16 April 1999. (IMF Archives), p.39.

relief process should be embedded in a development strategy promoting sustainable development and in particular focusing on the reduction of poverty in debtor countries.<sup>222</sup>

This position of speeding up and deepening debt relief was shared by the UK (Pickford) and EDs representing LICs (Barro Chambrier, de Morais), the Nordic states (Lehmussaari), Netherlands and Eastern Europe (Wihnholds), and Canada, Ireland, and the Caribbean (Bernes).<sup>223</sup> The U.S. (Lissakers), while supportive of deepening relief, was cautious on issues of timing:

We believe that the presumption of a six year track record of reforms should be maintained...Providing debt relief outside a framework of macroeconomic stabilization and broader structural reform will not support the type of sustained improvements in growth and poverty alleviation at the heart of this initiative. Stabilization efforts and reform need time to take hold...we do not do these countries any favors by rushing to a completion point.<sup>224</sup>

France (Milleron) was least enthusiastic on deepening and broadening the HIPC framework:

We are also ready to reflect further on tightening the links between debt relief and poverty reduction. We recognize that we do not have specific views on how to proceed at this stage. But, we nevertheless believe that debt cancellation cannot substitute for traditional ODA support, which has the additional advantage of positive externalities. .... Debt relief measures, however generous, can only accompany, not substitute for development policies. France therefore believes that only countries with irreproachable economic and social management as well as governance should benefit from this enhanced exceptional effort by the international financial community.<sup>225</sup>

As with the HIPC process, negotiations around HIPC II saw broad agreement from powerful states and staff on the importance of structural reform, conditionality, and Fund involvement in any new debt relief scheme. This is best captured by EDs from poor LICs who reaffirmed this sentiment pushed by creditor states. ED Chambrier, for example, stated:

While we see merit in de-linking debt relief from ESAF compliance, we understand the concerns expressed on the need for assurances regarding policy performance.... Concerning the use of performance requirements after the completion point, we can endorse the arguments outlined by the staff, given the risk related to the fact that this situation could entail difficult judgments about the delivery of debt relief.<sup>226</sup>

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<sup>222</sup> EBM 99/43, p.55.

<sup>223</sup> *Ibid.*, pp.27-100.

<sup>224</sup> *Ibid.*, pp.59-60.

<sup>225</sup> *Ibid.*, p.48 and p.51.

<sup>226</sup> *Ibid.*, p.53.

Feedback from the 1999 April meeting was forwarded to G-7 leadership for discussion at the Cologne Summit meeting in June. Merging various proposals from the Fund and Bank, the G-7 leaders “recommended relaxing the eligibility criteria to provide speedier and deeper debt relief to more countries.”<sup>227</sup> In September, 1999 HIPC II was approved by the Interim and Development Committees pending funding, and formally adopted by the Fund and Bank Executive Boards in December 1999.

### *HIPC II Results*

*H1-H2:* In contrast to the HIPC, preference heterogeneity of powerful state was low in the HIPC II case. This cohesiveness undermined any attempt by staff and the MD to resist implementation of the reform.

*H3:* Similar to the HIPC, NGOs applied pressure both directly on IMF management and staff and distally on state principals. In this case, staff interviewed more clearly articulated that pressure from NGOs and direct lobbying of staff and management were integral to the implementation of the HIPC II reform. While this analysis is unable to measure the degree to which direct pressure vs. indirect pressure produced policy change, the evidence suggests that direct lobbying efforts that leapfrogged the delegation chain proved effective.

*H4:* As with the HIPC case, there was not a primary individual or set of individuals who pushed for the adoption of the HIPC II internally.

*H5:* Two major shifts in how the HIPC II was framed within the institution are of note. First, the notion that the introduction of the HIPC II would serve a broader agenda for LIC poverty reduction marked a watershed moment for IMF policy direction. Second, the fact that some staff began to reevaluate the appropriateness of the Polak model signaled that the ideas debated went beyond adaption and into the realm of learning as described above.

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<sup>227</sup> IMF *Annual Report 2000*, (Washington, D.C.: IMF, 2000), p.52.

## **Poverty Reduction and Growth Facility (PRGF)**

Unlike the process that led to the HIPC II, replacement of the Fund's decade-old concessionary lending programs (the ESAF) with the Poverty Reduction and Growth Facility (PRGF) in 1999 did not enjoy broad institutional support. Most strident in opposition was the majority of staff wary of moving the Fund too far into issues of development. This became particularly controversial when advocates for the PRGF argued that the new lending facility would include Poverty Reduction Strategy Papers (PRSPs). As introduced in chapter 1, PRSPs included a formal assessment of how specific macroeconomic and social policies should be designed and implemented to reduce poverty. Heading the charge for an overhaul of the ESAF at the time was Managing Director Camdessus and a few select staff members in the Policy, Development and Review (now SPR) and African departments. NGOs also played a role, but less so than in the HIPC and HIPC II cases. Powerful member states were generally supportive while evidence from Executive Board documents shows division among LIC EDs.

As with the HIPC and HIPC II, initial concerns raised about the ESAF were pushed by the NGO community and focused on two areas. First, lending arrangements under the ESAF did not address deeper issues of poverty. Second, conditionality frameworks were not sensitive to specific conditions on the ground for the LIC in question. External and internal reviews of the ESAF completed in 1997 reiterated similar themes. ESAF conditionality had not sufficiently protected the poor; the program had not effectively defined the role of the Fund and Bank in implementing ESAF loans; and attention to linkages between inequality, poverty, and growth were necessary in future Fund lending.<sup>228</sup>

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<sup>228</sup> IMF, *The ESAF at Ten Years: Economic Adjustment and Reform in Low-Income Countries* (Washington, D.C.: IMF, 1997).

Camdessus, nearing retirement, argued before the Executive Board on August 30, 1999 that a new thinking had to emerge in the Fund around policy toward LICs: "...we have made important strides in increasing the attention given to poverty reduction and social sector issues in ESAF programs. It is time to consolidate this progress and formalize some of the reforms envisaged for transforming the ESAF into a new renamed instrument, not least so that it can play the role foreseen for it in the HIPC cases."<sup>229</sup> At the September 13, 1999 EB meeting, Camdessus outlined his case for reform:

The current framework that ties the policies in ESAF-supported programs to poverty reduction is insufficiently comprehensive and lacks the elements needed to ensure the consistency of these policies with the country's social goals and vice versa... To remedy these problems, the ESAF must be made to benefit from an open and comprehensive approach that starts with an understanding of the main obstacles to growth and poverty reduction, and iterates toward a constellation of macroeconomic, structural and social policies sufficient to achieve realistic and monitorable goals for poverty reduction...Hence the proposal-which has the joint support of both Bank and Fund managements-to create a new comprehensive vehicle, the Poverty Reduction Strategy Paper, that is government-led, poverty-focused, based on an open and consultative process, and from which all ESAF and IDA operations should stem.<sup>230</sup>

The proposal was most enthusiastically supported from EDs representing the U.S. (Lissakers), UK (Pickford), France (Milleron), Belgium, Austria, and Eastern Europe ( Kiekens), Italy, Portugal and the Mediterranean (Faini), and the Nordic and Baltic states (Hansen). Lissakers, for example, argued for a comprehensive reform of the ESAF that integrated poverty and social development issues into concessionary lending arrangement:

I fully agree with the Managing Director's statement that the current framework still lacks all of the elements needed to ensure the consistency of ESAF supported policies with the country's social goals and vice versa. We do need a more fully developed integrated strategy...We fully support the establishment of the proposed procedures for PRSPs as a starting point for both the Bank and the Fund operations, with the PRSP replacing the PFP over time.<sup>231</sup>

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<sup>229</sup> IMF, *Minutes of the Executive Board Meeting*, EBM 99/95, 30 August 1999 (IMF Archives), p.32.

<sup>230</sup> IMF, *Minutes of the Executive Board Meeting*, EBM 99/102, 13 September 1999 (IMF Archives), pp.4-5.

<sup>231</sup> *Ibid.*, p.78.

A focus on poverty reduction was also shared by Pickford: “The poverty reduction strategies developed by countries to serve as the basis for Fund and Bank supported programs are clearly the right way forward...it seems clear that the Fund has a key role in poverty reduction.”<sup>232</sup>

EDs representing Japan (Yoshimura) and Holland and the Caucuses (Wijnholds), while generally supportive of ESAF reform, expressed some reservations in regard to the Fund’s traditional mission and a new focus on poverty reduction. For Yoshimura, “the Fund should...deal with social policy issues only insofar as they are necessary to achieve its main purpose, which is to realize macroeconomic stability...sound macroeconomic policies should not be compromised for the sake of social policy concerns.”<sup>233</sup> Wijnholds argued along similar lines, “I do not think it would be expedient to turn the Fund into a multidisciplinary institution. The Fund should do what it does best: offer macroeconomic policy advice. The Fund is not properly equipped to advise on social issues.”<sup>234</sup> For Germany (Esdars), support for reform was framed in maintenance of successful macroeconomic policy: “Effective poverty alleviation requires at first the full commitment of the countries themselves to tackle the roots of poverty, to restructure the economy and to pursue macroeconomic policies that ensure a sustainable high-quality growth process.”<sup>235</sup>

Middle income and poor state ED representatives’ reactions were mixed. Barro Chambier argued that “we should strongly support the MD’s proposal that the PRSP underlining the link [between] debt relief [and] poverty reduction be an integral part of PFPs, or ultimately could replace the existing

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<sup>232</sup>*Ibid.*, pp.25-26.

<sup>233</sup>*Ibid.*, pp.40-41.

<sup>234</sup>*Ibid.*, p.14.

<sup>235</sup>*Ibid.*, p.85.



framework.”<sup>236</sup> Morais was broadly critical of the proposal and instead argued for greater funding of the current ESAF.<sup>237</sup> These concerns were shared by EDs Shalan (Egypt and Arab states) and Kelkar (India, Bangladesh, Bhutan, Sri Lanka), who also remained wary of “mission creep” into poverty areas. For Shalan:

There is no question that the pursuit of poverty reduction, and the promotion of poverty reduction and the promotion of macroeconomic and social policies that support it, should be at the forefront of the economic development agenda at a global level. ...It is important, however, that we approach this subject in a practical manner...While we can appreciate the desire for some in the donor community, and some NGOs, that the Fund take on a more active role in this process. Our contribution, as an institution, toward the goal of poverty reduction, should stem from ensuring macroeconomic stability, thereby providing an optimal environment for sustained growth, while addressing the potential adverse impact of stabilization of the poor.<sup>238</sup>

Another area of concern shared by middle income and poor state EDs was the notion that the PRGF would set specific quantitative targets on social spending levels. Morais worried that “earmarking funds for social sectors would detract us from the multi-dimensional efforts and flexibility that should be embedded in any poverty reduction strategy.”<sup>239</sup> Kelkar was even more specific in his concerns: “In sum, we do not agree to the Fund incorporating structural benchmarks or performance criteria related to social safety nets or social reforms or social issues at large.”<sup>240</sup>

Interviews of LIC staff members also point to broad initial skepticism of the PRSP framework and reforming the ESAF:

We didn’t have any problems getting management to agree with it [the PRSP]. And the shareholders liked it. The [majority of] staff had concerns from various angles. ...a lot of people had problems with the practicality of the PRSP process that required a great deal of coordination. Some people were concerned about branding, putting poverty reduction up there as the sort of headline on our facility. Some people thought it represented mission creep. Some

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<sup>236</sup>*Ibid.*, p.75.

<sup>237</sup>*Ibid.*, p.93.

<sup>238</sup>*Ibid.*, p.19.

<sup>239</sup>*Ibid.*, p.92.

<sup>240</sup>*Ibid.*, p.18.

people thought we were taking too much responsibility as the Fund on an issue that we had little experience.<sup>241</sup>

For Fund staff, the notion that all of a sudden we would be involved in poverty reduction came as a strain at first. Wasn't poverty reduction the job of the World Bank? That was my reaction. This wasn't the way we do things.<sup>242</sup>

Camdessus also challenged the institutional culture of staff through his framing of the reform:

The staff view was that macroeconomic stability was necessary for growth and growth was necessary for poverty reduction...At the same time, Camdessus, in his last days, was pushing very, very hard. He wanted to go one more step. We had said, "First, macroeconomic stability, then growth and poverty reduction." He wanted to close the circle and say that poverty reduction leads to growth. There was a lot of work done trying to show that and he pushed in that direction. The institution was not comfortable doing that.<sup>243</sup>

While the majority of the staff was skeptical of the adoption of PRSPs and reforms of the ESAF, several key staff members were sympathetic to a shift in policy direction:

There were certain IMF staff who were supportive and understood the stakes. Jack Boorman, who was head of Policy, Development, and Review at the time, Hugh Bredenkamp, and Masood Ahmed. But there were often lone voices in the wilderness. It was against a bit the grain and there was a need for a certain number of us to push against the culture that pushed aside and minimized this work.<sup>244</sup>

For these staff members, the main argument toward a more aggressive stand on poverty reduction focused on the fact that despite decreased balance of payment gaps in the 1980s and 1990s, LICs had stagnant growth rates. As with the shift in thinking with adoption of the HIPC II, this also challenged the primary assumptions of the Polak model:

With the Polak model, the assumption is the faster you close the balance of payments gap, the faster you will grow. The old way of thinking in the 1980s and 1990s was to develop a plan that allows a balance of payments gap that lets you go to zero. In that framework, you want to tighten and close the balance of payment gap because that gap is created by bad policy. That was the business of the 1980s and early 1990s. The thought was, if you close all these gaps, all these countries will start growing. But they weren't. And that's where the institution woke up to the fact that development isn't just about macroeconomics. That is where you saw Camdessus saying it is about poverty reduction and growth, it is not about

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<sup>241</sup> Author interview with Fund staff member from the Strategy, Policy, and Review Department, Washington D.C., 14 June 2011.

<sup>242</sup> Author interview with Fund staff member from the Strategy, Policy, and Review Department (Special Advisor to the United Nations), Washington D.C., 20 September 2011.

<sup>243</sup> Author interview with Fund staff member from the Africa Department, Washington D.C., 13 June 2011.

<sup>244</sup> *Ibid.*

structural adjustment anymore. Structural adjustment was closing that gap. Poverty reduction and growth is about opening that gap.<sup>245</sup>

Along with support from a few strategically situated staff members, public pressure also was a variable in adoption of the PRSP and PRGF. As described in the Fund's 2000 Annual Report, "...the persistence of poverty – and mounting public pressure – underscored that more had to be done... In effect, the IMF transformed the ESAF into the PRGF to make poverty reduction a key element of growth oriented, country-owned strategy by combining concessional lending from the IMF in support of appropriate macroeconomic policies with antipoverty assistance from the World Bank and other development agencies."<sup>246</sup> NGOs were also broadly supportive of reforms focused on poverty reduction. Oxfam, for example, "welcomed this new approach as an opportunity to develop economic policies which are genuinely country-owned, and which have poverty reduction as their central aim."<sup>247</sup>

#### *PRGF Results*

*H1-H2:* Preference heterogeneity among powerful states was low in this case and supported the replacement of the ESAF with the PRGF and subsequent PRSPs. The Managing Director, as a primary initiator of this reform, shared preferences with powerful states. Unlike the HIPC case, a coalition of powerful states and the MD allowed the reluctant staff little room to resist or shape the adoption of the PRGF and PRSPs.

*H3:* Unlike the HIPC and HIPC II, NGOs played a more cursory role in the PRGF reform. Raising awareness in regard to the problems of the ESAF in the mid-1990s was their primary contribution to this shift in IMF LIC policy.

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<sup>245</sup> Author interview with Fund staff member from the Africa Department, Washington D.C., 13 June 2011.

<sup>246</sup> IMF, *Annual Report 2000*, pp.49-50.

<sup>247</sup> Oxfam, *Making PRSPs Work: The Role of the Poverty Assessments* (Washington D.C.: Oxfam, 2001), p.4.

*H4:* As demonstrated by the Executive Board minutes and interviews cited above, Managing Director Camdessus was the primary individual who pushed the resistant IMF staff to rethink how it conceptualized the relationship between poverty and growth. Several senior staff members within the influential Strategy, Policy, and Review Department also supported these efforts. These individuals were situated in powerful positions in the institution and thus were able to assert leverage on fellow colleagues.

*H5:* As with the HIPC II, the ideas pushed by advocates of replacement of the ESAF with the PRGF stood well outside the norm of Washington Consensus thinking that was still strongly embedded in the institution in the late 1990s. The evidence from this case suggests that under circumstances where coalitions were among powerful states and the Managing Director, the relative “cognitive dissonance” the reform may produce for resistant staff is unable to block reform.

#### **Extended Credit Facility/ Rapid Credit Facility/ Stand-by Credit Facility (ECF/RCF/SCF)**

In mid-2009, the Fund’s Executive Board scrapped the PRGF-ESF Trust and replaced it with the Poverty Reduction Growth Trust (PRGT).<sup>248</sup> In January 2010, the PRGF was replaced with three new loan facilities that drew from the PRGT. These included the Extended Credit Facility (ECF), Rapid Credit Facility (RCF), and Stand-By Credit Facility (SCF). Adoption of the ECF/RCF/SCF differed from the previous cases as the drivers of the reform primarily came from a coalition that included the Managing Director, staff, and LIC EDs. In regards to powerful states, prior to the onset of the global financial crisis in 2008, only Britain and France were supportive of replacing the PRGF, while the U.S., Germany, and Japan stood in opposition. As the crisis developed in late 2008 and early 2009, opposition from these states dissolved and the new framework was adopted. Unlike in the late 1990s, NGO pressure played no active role in this policy shift.

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<sup>248</sup> Financed primarily by bilateral contributions and revenue raised from a 2009 sell-off of gold reserves, US\$15 billion in funds were raised to fund the PRGT.

The consensus among staff interviewed is that Managing Director Dominique Strauss-Kahn was the key driver in this LIC policy shift:

Strauss-Kahn was a trigger...he created a huge amount energy and a mandate for every part of the Fund to rethink what they were doing. We in the Strategy, Policy, and Review Department were tasked with looking at all our operations and where we needed to refresh them. We revamped conditionality...structural performance criteria were abolished across all facilities. We were also tasked with looking at what we could do to make the low income facilities more tailored and effective for poor countries.<sup>249</sup>

Often times it only takes a spark. You look at Strauss-Kahn. He didn't have, given the world was falling apart, a lot of time devoted to LICs...He would go once or twice to Africa... But he pushed enough and oriented enough so that the rest of us who believed in this work could keep going.<sup>250</sup>

This same sentiment is shared by current and former Executive Board members:

The role of the Managing Director in setting LIC policy is critical. Ultimately it is the Managing Director's expression of interest in LIC issues that moves it onto the Board's agenda. Strauss-Kahn initiated and continued efforts to reshape IMF facilities to be more responsive to African needs.<sup>251</sup>

The Managing Director is critical. Dominique Strauss Kahn wanted to give more fiscal space to meet the need of LICs and less, more targeted conditionality.<sup>252</sup>

Staff also point to the March 2009 "Successful Partnership for Africa's Growth Challenge" held in Dar-es Salaam, Tanzania as a watershed moment for Strauss-Kahn and the Fund's relationship to LICs as Strauss-Kahn formally announced greater commitment to LICs through reforms of the PRGF:

My goal is at least to double the IMF's concessional lending resources. I also want to increase the flexibility of IMF financing. We are exploring better ways to provide short-term financing to members facing immediate financing needs. Raising our access limits, which have become increasingly binding, is under discussion. We are also trying to streamline conditionality, and tailor it better to the circumstances of each individual country. Related to this, we are re-examining our policies on debt limits, to make them more flexible."<sup>253</sup>

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<sup>249</sup> *Ibid.*

<sup>250</sup> Author interview of Fund staff member from the Africa Department, Washington D.C., 13 June 2011.

<sup>251</sup> Author interview of Executive Board Director, Washington, D.C., 26 January 2012.

<sup>252</sup> Author phone interview of Executive Board Director, Washington, D.C., 28 January 2012.

<sup>253</sup> Dominique Strauss-Kahn, "Opening Remarks," Conference on Successful Partnership for Africa's Growth Challenge, Dar-es-Salaam, Tanzania, 10 March 2009, available at <http://www.imf.org/external/np/speeches/2009/031009.htm> .

The Fund staff member responsible for organizing the new framework outlined by Strauss-Kahn highlighted the thinking around the reform focused on flexibility and diversity as follows:

We figured what divides the types of LIC engagement with the Fund are two issues: capacity and financing needs – in particular – the length of financing needs. With capacity, a critical component in the new architecture is the explicit recognition that we need an instrument to provide policy support and financing in the context of a situation where a country cannot implement a full Fund program. And then the other key difference when we come to countries that could implement a full Fund program is how long it will take to achieve a sustainable macroeconomic position. ...So to recognize that LICs are now quite diverse in terms of the time needed between the situation they are in now and a more stable and sustainable macroeconomic position is what distinguishes the instruments.<sup>254</sup>

There was also concern among staff that a title including “poverty” produced a stigma for potential borrowers and that gaps in PRGF LIC policy required a new architecture:

I think there was a need to rebrand [the PRGF] and here the Asia-Pacific Department was influential. It argued, “whatever we do, don’t call it something to do with poverty.” Why? Low Income Countries in Asia and the Middle East didn’t like the stigma of poverty. There also were these near middle income countries and the islands that were eligible to use the PRGF and the poverty name didn’t fit their reality. When you talk about Vanuatu, for example, using the PRGF, it doesn’t resonate because poverty is not as pressing in Vanuatu as it is in Sudan. Then you have states like Georgia and Armenia who are eligible for the PRGF, but the poverty focus doesn’t fit where they are in their development process. There were also other clear gaps as well. There were some countries, for example, who had civil strife and couldn’t get post-conflict assistance because they weren’t officially in a civil war. And the Finance Department was keen to sort out the mess of the financing and wanted to change the structure to one trust rather than many pockets.<sup>255</sup>

Relative to powerful states, there was little initial consensus in regard to replacement of the PRGF with new concessionary facilities prior to the 2008 crisis. From the U.S., there was growing resistance to Fund lending to LICs and a push for a focus on grants facilitated mainly by the World Bank following adoption of the Policy Support Instrument (PSI) and Multilateral Debt Relief Initiative (MDRI)<sup>256</sup> in 2005:

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<sup>254</sup> Author interview of Fund staff member from Strategy, Policy and Review Department, Washington D.C., 14 June 2011.

<sup>255</sup> Author interview of Fund staff member from Africa Department, Washington D.C., 21 September, 2011.

<sup>256</sup> In 2005, the G-8 proposed that the IMF, IDA and African Development Fund cancel 100 percent of the debt claims of states that had reached the HIPC completion points. Under the “Multilateral Debt Relief Initiative” (MDRI), the Fund formed two trusts (MRDI-I and MDRI-II) to pay off the full stock of debt owed to the IMF for loans disbursed prior to 2005. States with per-capita income of \$380 a year or less a year receive debt relief financed by the Fund’s own resources through the MDRI-I. LICs with per capita income above \$380 receive funds from bilateral creditors administered by the

The U.S. position was let's give debt relief and not give them any more loans. They are too poor, their institutions are too underdeveloped. and there is no nerve to collect money for these efforts, so let's go to grants. The IMF should do non-loan arrangements and the Bank should do grants.<sup>257</sup>

Germany, although supportive publically of the PRGF, often argued behind the scenes against greater institutional shift away from a strict focus on monetary issues and maintenance of strict conditionality: “In the end, Germany always goes along with the reforms but along the way they challenge us to not weaken conditionality and not to finance excessively.”<sup>258</sup>

Support for PRGF reform prior to 2008 came primarily from the British and French: “The Brits and the French position was, ‘We did bad lending in the past. Let’s clear out the space so there can be new borrowing for better projects.’”<sup>259</sup> The British and the French also pushed for long term engagement with LICs and were supportive of PRGF reform:

The British and the French have more of a tolerance- even perhaps a desire- to see the Fund engaged on a continuous basis in LICs because they think that having us there with financing creates positive momentums for reforms and prevents things from going too badly. The U.S. would like our engagement to be episodic.<sup>260</sup>

According to staff interviews, low income states were receptive to overhaul of the PRGF and continued engagement of the Fund in their policy direction. Specifically, finance ministers of LICs welcomed greater engagement and input into a new Fund architecture:

The finance ministers of the LICs do like interaction with the Fund because they like in some sense the expertise but also the leverage we bring. Having the perspective of sound public financial management they see as very important to push reform and have budgets that make sense...It is really through our program support that we can help build macroeconomic management capacity and this is very much appreciated by finance ministers and central banks in LICs.<sup>261</sup>

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Fund through the MDRI-II. As of 2010, \$3.4 billion in debt relief was granted to 32 LICs who had reached HIPC completion points

<sup>257</sup> Author interview of Fund staff member from Research Department, Washington D.C., 13 June 2011.

<sup>258</sup> Author interview of Fund staff member from Strategy, Policy, and Review Department, Washington D.C., 14 June 2011.

<sup>259</sup> Author interview of Fund staff member from Africa Department, Washington D.C., 13 June 2011.

<sup>260</sup> *Ibid.*

<sup>261</sup> Author interview of Fund staff member from Strategy, Policy, and Review Department, Washington D.C, 14 June 2011.

Divisions among powerful states in regard to PRGF reform quickly evaporated as the 2008 crisis unfolded and the pressure Strauss-Kahn exerted on the Executive Board after the Tanzania conference:

One other key element in getting the deal done was the dynamics created by the crisis. I think it is fair to say that our shareholders (states) are often strongly divided on LIC policy and we needed consensus on this one, mainly because we wanted to create a new trust. I think the crises got us over the finish line as every Executive Board member came on board in 2009.<sup>262</sup>

No evidence of direct lobbying for PRGF replacement was found from the traditional NGO community focused on the Fund. Staff interviewed also downplayed the impact of NGOs on adoption of the 2010 reforms:

NGOs are much less influential now than in the late 1990s because they much less to complain about. It is uncomfortable for them as we go through this crisis that we have all these countercyclical programs and protection of social spending that are pervasive in our LIC programs...Some NGOs continue to drum up the same type of issues that they did in the late 1990s, but these arguments are not gaining much traction.<sup>263</sup>

An Executive Board member representing LICs reiterated this position. While NGOs were the key actor that pushed the IMF to address issues of debt sustainability a decade prior, they had little input into the 2010 reforms and have little impact on current LIC policy choices at the Fund:

First, let me recognize the role that NGOs played in debt relief and the adoption of the HIPC... There reforms occurred in large part due to the constant pressure from NGOs. Now, debt relief is out of the way and there is much less that NGOs can engage with. The debt issue was something tangible. The only link you can make now is with inflation policy where NGOs generally push for higher inflation targets. There is not much left that is tangible and human that an NGO can get engaged with at the Fund. We do consult with them but in a limited fashion. Once a year during the annual meetings, along with the Executive Director's from the World Bank, we host a civil society forum. We engage, we have cordial meetings, and nobody complains.<sup>264</sup>

### *ECF/RCF/SCF Results*

*H1-H2:* Prior to the 2008 crisis, there was growing division between powerful states in regard to IMF involvement in LICs. France and the UK advocated for a continuation of PRGF concessionary lending

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<sup>262</sup> *Ibid.*

<sup>263</sup> Author interview of Fund staff member from Strategy, Policy, and Review Department, Washington D.C., 14 June 2011.

<sup>264</sup> Author interview of Executive Board Director, Washington D.C., 26 January 2012.



and a focus on poverty issues and were sympathetic to more flexible conditionality requirements. The U.S. instead advocated for phasing out IMF LIC lending programs. Germany was worried with loosening conditionality requirements and was increasingly concerned that too much focus on development issues was pushing the Fund away from monetary and fiscal issues. This lack of cohesive vision among powerful state principals in the mid-2000s allowed Strauss Kahn room to initiate overhaul of the PRGF. Once the crisis hit, all-powerful states rallied around the ECF/RCF/SCF initiative pushed by Strauss Kahn and LIC staff and the framework was quickly adopted.

*H3:* As noted above, NGOs were not involved in efforts to reform the PRGF.

*H4:* Managing Director Strauss Kahn was the primary internal advocate for the reform of the PRGF. Several senior members of the African department and SPR also argued for a more flexible approach to LIC concessionary lending. In addition, Fund chief economist Oliver Blanchard called for a rethinking of how the Fund approaches monetary and fiscal policy response. Following the 2008 crisis, Strauss Kahn and Blanchard advocated for countercyclical policy response as a component of the flexibility of the new LIC concessionary lending program. In this context, it can be argued that these individuals took up the role of internal norm entrepreneurs in this policy change.

*H5:* Advocates for replacement of the PRGF with the ECF/RCF/SCF initially highlighted that the new framework would be both more flexible in dealing with LICs and also respond more nimbly to the diverse realities of LICs. Prior to the 2008 crisis, the reform was not spun as policy shift that would fundamentally challenge IMF thinking.

## **Conclusions**

Comparison across these cases uncovers the following patterns (see Table 3.1 below). First, two tiers of actors were identified in LIC outcomes. What I call “primary actors” included the Managing Director, powerful states, and staff. “Secondary actors” included LICs, NGOs, and the U.S. Congress.

In all the cases examined, LIC reform occurred either with a coalition formed between at least one primary and one secondary actor as seen in the HIPC or at least two primary actors as seen with the HIPC II, PRGF, and ECF/RCF/SCF. While preliminary, evidence from these cases suggests that future LIC policy change should occur under the following two scenarios. First, if there is broad support among three primary actors for reform, policy shift should occur. Second, at a minimum, some form of coalition between two primary actors (MD-staff, MD-powerful states, powerful states-staff) or primary actor and secondary appears necessary to produce significant policy change. As such, evidence from these cases also suggests that a primary actor “can’t go it alone.” Without the support of other primary actors, staff, powerful states, and management must have backing from a secondary actor to initiate reform successfully. In the HIPC case, for example, the U.S. and UK formed a successful coalition with NGOs against the preferences of the Managing Director, staff, and other powerful states.

Table 3.1: Coalitions of IMF LIC Reform (1996-2010)

Reform	In opposition	In support
HIPC	-Powerful states (France/Germany/Japan) -Managing Director -Staff	-Powerful states (U.S./UK) -NGOs
HIPC II		-Powerful states -Managing Director -Staff -NGOs -LICs
PRGF	-Staff -Majority of LICs	-Powerful states -Managing Director -Select senior staff in SPR -Select LICs
ECF/RCF/SCF	-Powerful states (U.S./Germany/Japan)	-Powerful states (UK/ France) -Managing Director -Staff -LICs

As predicted by PA models, increased division among powerful state principals provided openings for management and staff to initiate, resist, or shape LIC policy. This was most salient when staff and the

Managing Director shared preferences. In the HIPC case, divergence of state preferences around a conservative plan of debt forgiveness supported by staff and Camdessus allowed the proposal to go forward for adoption. Splits among powerful states in regard to overhaul of the PRGF framework prior to the 2008 crisis also gave Strauss-Kahn and the staff room to initiate a new framework for LICs. If preference heterogeneity between powerful states on the Executive Board is high in future scenarios, we should expect management and staff to enjoy the same degree of leverage to initiate or block reform efforts. Evidence from these cases also points to the importance of the Managing Director and senior staff in the Strategy, Policy, and Review department in lobbying for change. In the PRGF case, for example, Managing Director Camdessus and the leader of SPR highlighted the connection between poverty reduction and long-term growth to a broader audience of Fund staff highly sceptical of this position. In the ECF/RCF/SCF case, the leadership of Managing Director Strauss-Kahn was a key variable that ultimately produced this reform.

In regard to delegation chains and the impact of pressure applied distally to principals, evidence from the HIPC and HIPC II cases is inconclusive. According to staff interviews, NGO direct pressure was essential and effective in the reforms of the late 1990s (HIPC, HIPC II, and PRGF). Internal IMF documents also note the impact of NGO efforts that leapfrog delegation chains and apply pressure directly to Fund staff and management. NGOs, however, also concurrently lobbied states to reform the Fund. Disaggregating the impact of direct and indirect lobbying on Fund policy choices requires further study before any conclusions can be drawn. More conclusively, evidence from the HIPC case demonstrates greater success of direct lobbying when the NGO has at least one primary actor supporting their position. SO theory hypothesizes that the manner in which a new policy reform is framed should impact its potential success or failure. In the HIPC and ECF/RCF/SCF cases, the

argument presented by those who pushed for reform did not challenge the status quo of what was considered appropriate Fund policy. In the HIPC II and PRGF, those who championed reform did so in a way that more fundamentally countered IMF thinking. While this is a small number of cases, the contradictory evidence suggests that the framing of a reform effort matters less in the ultimate success or failure of its adoption than other variables highlighted above.

## Chapter 4 - Crises of Legitimacy: Constructivist Explanations of LIC Change

As established in chapter 3, the evidence derived from the study of four cases of LIC policy change suggests that coalition formation is a key mechanism necessary for the IMF to implement formal policy shift. As predicted by PA models, increased division among powerful state principals provided openings for management and staff to initiate, resist, or shape LIC policy. This was most salient when staff and the Managing Director shared preferences. This evidence supports a broader notion also consistent with PA models that policy changes occur due to shifting degrees of control of more powerful actors over less powerful actors. This implicitly supports the notion put forth by PA theorists that less powerful actors (agents) enjoy some degree of autonomy relative to their principals. Given the evidence in chapter 3, one notion that can be dismissed is the idea that any one powerful state, even the U.S., can on a consistent basis determine LIC policy choices in the institution. As highlighted by constructivist scholar Jeffrey Chwieroth, another important contribution of PA inspired studies of the Fund, and also supported by the evidence in this project, is that the impetus for change can be driven by agents rather than principals.<sup>265</sup>

Despite these contributions, Chwieroth and constructivist IO scholars argue that one key weakness of rationalist theory is that it is ontologically ill equipped to examine the belief systems of staff and how changes in belief systems impact change. As noted by Chwieroth, “if you want to know to understand how IOs work and evolve, they we must attend not only to member states’ interests but also to beliefs that prevail within IOs and the internal processes and debates shaping these beliefs.”<sup>266</sup> Chwieroth falls in line with a series of other constructivist IO scholars who frame their inquiry not as fundamental challenge to rationalist theory, but one that engages with a different component of reality that

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<sup>265</sup> Chwieroth, *Capital Ideas*, p.9.

<sup>266</sup> *Ibid.*, p.10.

influences policy outcomes. Relative to our purposes for this project, while PA models can tell us that some form of coalition appears necessary for change to occur, they don't elucidate if, how, or why shifts in thinking among those actors might support or undermine the formation of those coalitions or other processes that produce reform.

In chapter 4, I model a study of LIC IMF change on methods used by Chwieroth and several other “conventional” constructivist scholars, including Susan Park, Antje Vetterlein, Bessma Momani, and Manuella Moschella.<sup>267</sup> Chapter 4 first outlines how contemporary constructivist theory explains IMF change. This is followed by an exploration of how the Fund has come to accept particular ideas of what constitutes appropriate macroeconomic and development policy in the post-Washington Consensus period and how these changing ideas impacted IMF LIC reform. This is first accomplished by tracing how five prominent mainstream frameworks of economic theory have influenced the economics profession and Fund management and staff. These economic frameworks include Keynesianism, the neoclassical synthesis, monetarism, new classical economics, and New Keynesianism.

Applied to the study of the post-Washington Consensus period, a constructivist framework finds that the Asian crisis in the late 1990s and the 2008 global financial crisis catalyzed shifts in thinking in the economics profession and policy elites that impacted change in two key areas of Fund LIC policy. The

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<sup>267</sup> As outlined by Jeffrey Checkel, there is an epistemological division between “conventional” and “interpretive” constructivists. Conventional IR constructivists including Alexander Wendt, John Ruggie, Peter Katzenstein, and Martha Finnemore are epistemological positivists. While the world is socially constructed, observers can systematically study this subjective reality and uncover causal patterns. Interpretive constructivists, including Ted Hopf and Thomas Bankoff, reject positivist assumptions about how best to study a socially constructed world. Rather than focus on how norms and idea causes change in the international system, interpretive constructivists instead study how particular identities and norms are formed in the first instance. Checkel describes this as answering “how possible” questions. See Jeffrey Checkel, “Constructivism and EU Politics,” in *Handbook of European Union Politics*, eds. Knud Erik Jørgenson, Mark A. Pollack, and Ben Rosamond (London: Sage Publications, 2007), pp.57-67 at p.58.

2008 crisis sparked a Keynesian-inspired shift within the economics profession and Fund that challenged nearly three decades of neoclassical consensus concerning appropriate monetary and fiscal policy response. Specific to LIC policy, this shift ushered in a new acceptance of countercyclical and flexible monetary and fiscal policy that helped bring about the replacement of the PRGF with the ECF/RCF/SCF in 2010.

Fallout from the Asian crisis led to a reevaluation of the role of the state in its relation to market efficiency, growth, and development. As seen in the Fund's adoption of the PRGF in 1999 and current ECF/RCF/SCF framework, support of targeted state intervention to enhance market efficiency, improve institutional capacity, and invest in human capital is now a fundamental component of IMF strategies to reduce poverty and support growth in LICs. Despite this shift, several components of neoclassical ideology remain firmly entrenched in how the Fund thinks about development. In LIC initiatives, this is expressed through a mantra that consistently and explicitly grounds the IMF's focus on poverty reduction since the 1999 reforms as a "pro-growth" strategy staunchly opposed to policy deemed distortive to markets. While the state is to be used to enhance market efficiency, improve institutional capacity, and invest in human capital, LICs are advised to avoid protectionism, over or undervalued exchange rates, subsidies, redistributive tax arrangements, and large scale entitlement programs.

### **Theorizing IO Change: A Constructivist Framework**

At its ontological foundation, constructivists frame the world as one being driven by the "logic of appropriateness." Humans, as inherently social beings, form collectively held ideas of the world.<sup>268</sup>

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<sup>268</sup>James March and Johan Olsen, in contrast to rationalist ontological assumptions, argue that humans are driven by a 'logic of appropriateness' in decision making. Individuals, as social beings, frame their decisions within the context of identity and legitimacy rather than cost-benefit analyses of utility maximization. See James March and Johan Olsen, *Rediscovering Institutions: The Organizational Basis of Politics* (New York: The Free Press, 1989).

These collectively held understandings form the primary structure within which humans and subsequent state behavior and the international system is embedded. Despite the inherent intersubjectivity of the world, this variant of constructivism argues a positivist framework can systematically identify how changing patterns of identity formation and shifts in norms and ideas explain social and political change.

Constructivists frame their study of change as one that recognizes exogenous, systematic factors but also is consciously and primarily focused on internal, institutionally specific agency and variables of the IO understudy that can catalyze or resist reform.<sup>269</sup> The agency of IO actors also is constituted and influenced by institution specific organizational culture. As outlined by Barnett and Finnemore,

...IOs..are established to accomplish certain tasks. To do this, they develop general consensus around their understandings of their core mission and the functions of their organization; goals to be pursued; basic means to pursue these goals, and some way to measure results. Thus organizations create a shared discourse, symbols, and values for their staff. These shared elements, in turn, generate a group identity for the organization and structure interactions among those within it.<sup>270</sup>

Maintenance and reproduction of organizational culture and identity is not a passive process. Staff members internalize particular frames of reference and also socialize new employees to adopt particular norms and routines within the bureaucracy. Organizational culture therefore is deeply embedded and serves as the frame of reference through which events and signals from the external and internal environment are cognitively processed.

Established organizational culture and subsequent policy direction is not predicted to change quickly or easily in bureaucracies. As noted by Momani, several studies that draw from organizational theory

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<sup>269</sup> *Ibid.*, “Exogenous variables recognized that can stimulate change in IOs recognized by organizational theory include: structural changes in the international system, crises and disasters causing shocks to ripple in international organizations, competition between and among international organizations vying for additional jurisdictional turf; changes in international norms and values, and changes in attitudes and policies of key international members.”

<sup>270</sup> Barnett and Finnemore, *Rules for the World*, p. 19.



conclude individuals in bureaucracies have a default position that resists change: “Organizational theorists contend that individuals resist change because they fear the unknown, have selective attention to and retention of new information, prefer habit and routine, need the security of the known, and feel threatened by change.”<sup>271</sup> Resistance to change manifests itself at the organizational level “because there is a lack of trust, differing perceptions and goals, social disruption with change, a limitation of resources to devote to change, and most importantly change requires a change in the organizational culture.”<sup>272</sup> Despite inertia against radical or swift reform efforts, constructivists highlight that IOs are also never static entities. Vetterlein notes four prominent features of IOs that make them subject to change over time. These include shifting relationships with powerful state principals; the fact that the institution’s original institutional mission evolves due to changing realities in the international system; modifications in formal organizational structure; and less observable alterations of informal organizational culture.<sup>273</sup>

### **Constructivist Theory and IMF Policy Change**

Park and Vetterlein present a framework for studying Fund reform through the concept of “norm cycle.” Norms, defined as “shared expectations about appropriate behavior held by a collectivity of actors,” are not simply static entities that these institutions either adopt or reject. Rather, policy norms are reflexive and represent shifting processes of collective understandings of how the world works by various actors both within and outside the IO. As such, a policy norm “emerges not from thin air but

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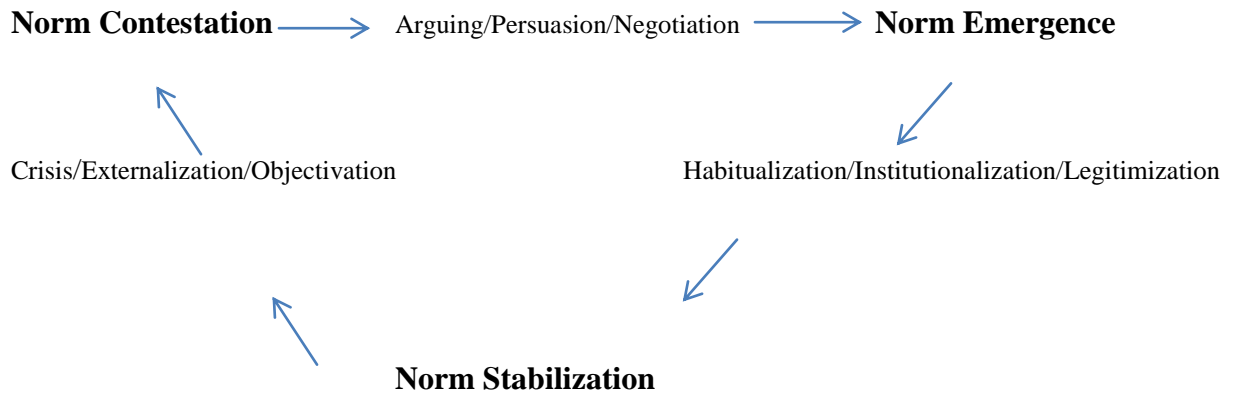
<sup>271</sup> Momani, “Limits of Streamlining Fund Conditionality: The International Monetary Fund’s Organizational Culture,” p.147.

<sup>272</sup> *Ibid.*

<sup>273</sup> Antje Vetterlein, “Lacking Ownership: The IMF and its Engagement with Social Development as a Policy Norm,” p.98.

always out a specific context of an already existing norm which may be contested or inflexible in a changing context.”<sup>274</sup>

Figure 4.1: Norm Cycle.



Three points in the life of a norm cycle are identified by Park and Vetterlein: norm emergence, norm stabilization, and norm contestation (see Figure 4.1 above).<sup>275</sup> A norm gains traction and stabilizes only if it first is granted legitimacy. The degree of legitimacy granted to a new norm and subsequent policy direction is predicted by examining three constitutive components. The norm has “formal validity” if it has been integrated into “the IO’s constitution or Articles of Agreement, its operational strategy, and/or is included in Fund ...loan contracts.”<sup>276</sup> More informally, a norm has “social recognition” when it is accepted by actors as the right thing to do. At the policy level, a norm has “cultural validity” when expressed in programs at the local level. Once accepted as legitimate, patterns of behavior around the norm emerge and are reproduced through policy creation and become

<sup>274</sup> Park and Vetterlein, “Owning Development,” p.19.

<sup>275</sup> *Ibid.*, p.20.

<sup>276</sup> *Ibid.*, p.6.

institutionalized in the organizational culture.<sup>277</sup> I draw from this framework and hypothesize that economic ideas also follow a similar pattern of emergence, stabilization, and contestation.

Specific to the IMF, Moschella identifies three constituencies that legitimize development norms, economic ideas, and policy choices in the institution.<sup>278</sup> The first constituency consists of member states. While the Fund exhibits a high degree of autonomy in its daily operations, as an intergovernmental organization, it ultimately must have significant support from member states. A norm or economic idea that fundamentally challenges the position and interests of powerful states is not expected. The second constituency involves academic economists and the broader economics profession. Many beliefs shared by IMF staff originate in the economics field that is trained and generally concerned with maximizing welfare and efficiency above other objectives. Chwioroth also notes that Fund staff have leverage in their support or resistance to new policy norms due to the fact that they are socially recognized as authorities and experts in the field of economics. Staff thus exhibit productive power as they construct meaning and shape and define what policy choices are legitimate and realistically possible to pursue.<sup>279</sup>

Studies of epistemic communities demonstrate that there are also networks of knowledge-based experts who “share knowledge about the causation...of phenomena in an area for which they have a reputation for competence” and produce “a common set of normative beliefs about what action will benefit human welfare” in the policy domain in question.<sup>280</sup> Like-minded experts can influence what is considered legitimate in policy direction through a process of administrative recruitment that favors

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<sup>277</sup> *Ibid.*, p.22.

<sup>278</sup> Manuella Moschella, *Governing Risk: The IMF and Global Financial Crises*, p.26.

<sup>279</sup> Chwioroth, *Capital Ideas*, pp. 41-43.

<sup>280</sup> Peter Haas, “Policy Knowledge: Epistemic Communities,” in *International Encyclopedia of the Social and Behavioral Sciences*, vol. 17, ed. Neil Smelser and Paul Bates (Amsterdam: Elsevier Science, 2001), pp. 11578-11586 at p. 11579 as cited in Chwioroth, *Capital Ideas*, p.43.

individuals that share their ideological positions. This process is similar to what organizational sociologists Paul DiMaggio and Walter Powell describe as “normative isomorphism.” Processes of professionalization produce formal and informal networks that weed out individuals who stand outside the boundaries of appropriate thinking. Individuals who find positions within professional bureaucracies will generally share the ideas and norms of the mainstream.<sup>281</sup>

Along with member states and the economic profession, private market actors also play a part in granting emerging norms and subsequent policy directives legitimacy at the Fund. Moschella notes that “it is widely recognized that market actors endorse IMF activities when they acknowledge that the Fund’s financial assistance to a member country is of help in restoring the conditions for fruitful investment.”<sup>282</sup> In this gatekeeper role, the IMF provides an informal guarantee that member-states will not pursue policy choices that seriously challenge or undermine the interests of private investors. Moschella also points to evidence where private market actors have undermined Fund policy directives. The lack of private support for the IMF sponsored Special Data Dissemination Standard (SDDS) initiative, for example, limited the success of the process of international data standardization.<sup>283</sup>

Leonard Seabrooke also contends that the post Washington Consensus period has witnessed an expansion of what he terms the IMF’s “social constituency of legitimation.” Fallout from the controversy over structural adjustment lending in the 1980s and the Asian crisis has produced a significant “legitimacy gap” for the Fund. In response, the IMF is now focused on gaining support from the public in member states. The Fund’s decade-old practice of increased transparency and

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<sup>281</sup> Paul DiMaggio and Walter Powell, “The Iron Cage Revisited: Institutional Isomorphism and Collective Rationality in Organizational Fields,” *American Sociological Review*, 48, no. 2 (1983), pp.147-160 at p.152.

<sup>282</sup> Moschella, *Governing Risk: The IMF and Global Financial Crises*, p.27.

<sup>283</sup> *Ibid.*

participation in PRSPs, for instance, are interpreted as an expression of growing sensitivity to the concerns of civil society.<sup>284</sup>

While the process of internalizing norms and ideas into individual and collective identity produces some form of stability concerning how the organization thinks, they are never fully static or uncontested. The effort of internal norm entrepreneurs and external systematic shifts produce new experiences and interpretations that challenge organizational culture, policy practices, and even more fundamental challenges to legitimacy. Park and Vetterlien identify three triggers that undermine legitimacy. First, ideological space for reform is opened when there is broad based agreement among elites that a particular economic or policy program fails. Second, similar to findings from organizational theory, an unexpected external shock can challenge taken for granted assumptions. Third, “mass condemnation” occurring in conjunction with acknowledgement of past policy failure and an external shock can facilitate the acceptance of new ideas and approaches. Once a policy position norm or idea comes under question in this scenario, staff, management, NGOs, and/or states use mechanisms of persuasion, arguing, shaming, and negotiation to push for reform. Moschella offers an additional predictive framework for Fund policy shift based on the aforementioned social constituencies of legitimation. Given the importance of social acceptance of particular norms and ideas in the production and maintenance of policy directives, we can expect change to occur when gaps open between “the institutionalization of specific economic ideas in the Fund’s policies” and “the acceptance of these policies by the actors of its social constituencies of legitimation.”<sup>285</sup>

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<sup>284</sup> Leonard Seabrooke, “Legitimacy Gaps in the World Economy: Explaining the Sources of the IMF’s Legitimacy Crisis,” *International Politics* 44 (2007), pp.250-268 at pp.257-261.

<sup>285</sup> Moschella, *Governing Risk: The IMF and Global Financial Crises*, p.27.

## Paradigmatic Ideas of Development

Contemporary constructivist studies of the Fund focus on two interrelated levels of ideas that shape its institutional culture and subsequent policy choices. The first level is that of paradigmatic economic ideas. These ideas are embedded in theoretical debates about economics and set “cognitive background assumptions” and the interpretive framework for the workings of the economy and shape what is considered sound policy advice.<sup>286</sup> Within the boundaries of paradigmatic thinking sit various schools and trends in economic thinking that gain and lose legitimacy over time.

Specific to paradigmatic ideas, a focus on shifts in thinking in the economics profession and its relationship with Fund LIC policy reform requires that we first step back and recognize in broad terms what constitutes the ideological parameters of acceptable policy choices and debate in mainstream development economics. Wilfred David, in his study of Fund thinking, identifies five prominent principles broadly shared among the staff and the larger mainstream economics community.<sup>287</sup> The first is a belief that growth and national income generation are only possible when there is substantial and sustained capital investment and a skilled workforce. Development strategies for poor societies therefore encourage policies and institutional reform that primarily facilitates rapid resource mobilization and investments in human capital. A second principle is that material gain is maximized only if there is rational and efficient allocation of scarce resources. Alternative choices made irrationally or without complete information will produce long term increases in scarcity and a subsequent decrease in growth and living standards. In order to make rational decisions in the

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<sup>286</sup> John Campbell, “Institutional Analysis and the Role of Ideas in Political Economy,” *Theory and Society* 27, no. 3 (1998), pp. 377-409 at p.386.

<sup>287</sup> Wilfred David, *The IMF Policy Paradigm: The Macroeconomics of Stabilization, Structural Adjustment, and Economic Development*, pp 7-11.

allocation of scarce resources, prices thus should equal real costs in all markets. Market information should also be easily accessible and transparent.

A third principle is that the best mechanism to establish efficient allocation of scarce resources is through market mechanisms. While not perfect, well-functioning and transparent markets minimize conflict and ultimately are the best mechanism for growth and relatively equitable distribution of resources. Building on this theme, the fourth principle extends a preference for free markets to the international arena. A liberal international environment underwritten by the rules of free trade and comparative advantage will produce the most favorable conditions for development. The fifth principle frames development as a rational process that is ultimately tackled through technocratic adjustment of incentives and/or institutions that improve market performance. As summarized by David, “The ruling paradigm of the economics of development rests on the classical-neoclassical view of the world in which change is gradual, marginal, non-disruptive, equilibrating, and largely painless. Incentives are the bedrock of economic growth. Once initiated, growth becomes automatic and all-pervasive, spreading among nations and trickling down among classes so that everybody benefits from the process.”<sup>288</sup>

These principles express themselves broadly throughout the Fund’s formal mandates. As outlined in the IMF’s Articles of Agreement, orderly global trade and exchange are the most effective tools to support international equilibrium and development. In Article 1(iii), Article (v), and Article (vi), the Fund is directed “to promote exchange rate stability,” “maintain orderly exchange arrangements,” and provide member states “with the opportunity to correct maladjustments in their balance of payments

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<sup>288</sup> Jeffery Nugent and Pan Yotopolous, “What has Orthodox Development Economics Learned from Recent Experience Legitimacy,” *World Development* 7 (1979), pp.541-54 at p.542 as cited by David, *The IMF Policy Paradigm: The Macroeconomics of Stabilization, Structural Adjustment, and Economic Development*, p.10.

without resorting to measures destructive of national or international prosperity.” The Articles also stress that the IMF promote a liberal market international economic order – and in so doing – produce successful development outcomes. This is articulated most clearly in Article 1(ii) where the Fund is 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.”

Adherence to an orderly, cooperative, and transparent market system thus sets the broad intellectual and ideological “goal-posts” of mainstream development economics. Within these boundaries, however, sits a diversity of policy debates related to two distinct policy areas where the Fund is actively involved: (1) monetary and fiscal policy to stabilize short term balance of payment disequilibria; and (2) structural reform that improves economic efficiency and stimulates growth and development. Drawing from a constructivist framework, the following hypotheses are derived for explaining post-Washington Consensus LIC policy change through a focus on these two policy areas:

*H1: Policy reform initiatives that draw from ideas and norms that question market based solutions for LICs are unexpected.*

*H2 : A crisis of legitimacy that challenges taken for granted” macroeconomic and development ideas and/or norms is necessary for substantive LIC policy change.*

*H3: Chances of LIC policy change are greatest when economic ideas or norms institutionalized within the Fund are questioned by broader epistemic community of development economists.*

### **Economic Ideas and “Appropriate” Macroeconomic Policies**

Constructivist studies of Fund change maintain that the primary constituency of legitimation is the economics profession. As outlined by Chwioroth, “Cycles, trends, and shifts in economic theory shape the content of [staff] expertise by helping to determine what constitutes an economic problem and how such problems are best solved. When the staff members approach their tasks, they necessarily come to



rely on the content of their training to develop specialized knowledge and to form judgments about policy.”<sup>289</sup> Capturing how these trends manifest and shape the IMF’s normative culture, policy direction, and periods of change is achieved by methodologically “drilling down” into what Ben Clift and Jim Tomlinson describe as the “political sociology of policy instruments” approach.<sup>290</sup> I first trace how five prominent economic schools of thought have shaped internal IMF debates concerning monetary and fiscal policy and how this has manifested itself in influencing post Washington Consensus LIC policy reform. These include Keynesianism, the neoclassical synthesis, monetarism, new classical economics, and New Keynesianism (see Table 4.1 below).

Evidence from interviews, internal staff documents, and LIC lending arrangements shows that ideas drawn from monetarism, new classical economics, and New Keynesianism produced a highly stable framework of what constituted appropriate macroeconomic policy from the 1982 Mexican debt crisis to the global financial crisis of 2008. Since this time, evidence points to greater influence of more traditional Keynesianism in Fund and LIC policy response. Along with calls for more flexible inflation targets, a policy of active, countercyclical fiscal response has emerged in LIC policy directives. To give context to these ideas, I start first with an overview of traditional Keynesianism.

### *Keynesianism as a Response to Classical Orthodoxy*

Keynesian economics developed as a direct critique to classical economic orthodoxy that predominated in the nineteenth and early twentieth century. Classical orthodoxy is based on five assumptions: (1) markets are perfectly competitive; (2) economic actors are fully informed of market dynamics; (3) economic actors are rational utility optimizers who make efficient use of information; (4) in open markets, an equilibrium price is established that reflects when the quantity of the product

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<sup>289</sup> Chwieroth, *Capital Ideas*, p.60.

<sup>290</sup> Ben Clift and Jim Tomlinson, “When Rules Started to Rule: The IMF, Neo-liberal Economic Ideas, and Economic Policy Change in Britain,” *Review of International Political Economy*, 18, no.1 (2011), pp. 1-24 at pp.4-5.

Table 4.1 Five Economic Schools of Thought

School of Thought	Major Themes?	Appropriate Policy Response?	When most influential in IMF?
Keynesianism	<ul style="list-style-type: none"> <li>-Critique of “self-correcting” logic of classical economics</li> <li>-Market failures due to inadequate levels of investment/consumption and self-reinforcing, subjective conceptions about the future</li> </ul>	<ul style="list-style-type: none"> <li>-Expansionary monetary policy in moderate recessions</li> <li>-Aggressive fiscal policy during more severe crises</li> <li>-Public investment</li> <li>-Redistribution</li> <li>-Capital controls</li> </ul>	<p>1945- early 1960s</p> <p>2008-present</p>
Neoclassical Synthesis	<ul style="list-style-type: none"> <li>-Merges aspects of Keynesianism and classical theory</li> <li>-Markets not self-correcting in short term but generally correcting in long term</li> </ul>	<ul style="list-style-type: none"> <li>-Targeted and short term monetary and fiscal intervention to counter recessionary periods.</li> <li>-Permanent government intervention discouraged</li> <li>-Capital control liberalization</li> </ul>	1960s-late 1970s
Monetarism	<ul style="list-style-type: none"> <li>-Money supply is primary variable that drives economic outcomes</li> <li>-Money supply neutral in long term and non-neutral in short term</li> <li>-Free of government intervention, markets are self-correcting in long term</li> </ul>	<ul style="list-style-type: none"> <li>-Limit money supply to match underlying fundamentals</li> <li>-Avoid expansionary monetary and fiscal policy</li> <li>-Avoid market distortion in labor markets</li> <li>-Capital control liberalization</li> </ul>	Late 1960s-late 1980s
New Classical Economics	<ul style="list-style-type: none"> <li>-Micro-level processes explain macro level outcomes</li> <li>-Critique of monetarist assumptions of short –term market inefficiency.</li> <li>-Free of government intervention, “real time” adjustments by utility maximizing actors guarantees efficient markets in short <i>and</i> long term</li> </ul>	<ul style="list-style-type: none"> <li>-Avoid expansionary monetary and fiscal policy.</li> <li>-Monetary policy as tool to combat inflation</li> </ul>	Late 1970s-2008
New Keynesianism	<ul style="list-style-type: none"> <li>-Micro-level processes explain macro level outcomes including involuntary unemployment</li> <li>- Critique of New Classical Economics’ assumption of perfect markets. Imperfect markets are rule, not exception.</li> <li>-Market not efficient in short term due to menu costs, efficiency wages, etc.</li> </ul>	<ul style="list-style-type: none"> <li>-Monetary and fiscal policy as instruments to correct market failure. More effective if used in short term.</li> <li>- Inflation targeting as primary policy goal of central banks.</li> <li>-Targeted policy to reduce market imperfections</li> </ul>	Mid 1980s-2008

demanded is just equal to the quantity of product supplied at that price;<sup>291</sup> and (5) given the above conditions, an economy will self-adjust to clear markets of excess supply or demand,<sup>292</sup> allows for “Pareto-efficient” welfare improving outcomes,<sup>293</sup> and will always trend toward its natural level of real GDP<sup>294</sup> and full employment.

Specific to conceptualizations of full employment and its relationship to free markets, the classical school is rooted in ideas initially developed by nineteenth century economists John Stuart Mill and Jean Baptiste Say. They begin with the notion that the only reason people produce is to consume. If the desire to consume drives the effort of production, it is impossible to have conditions of overproduction in free market systems due to lack of demand. Or as stated in Say’s Law, production (supply) and selling of one product therefore can be thought of as demand for another product of equal value.<sup>295</sup> If supply creates its own demand, a key mechanism that must be in place to guard against misplaced production is free market price and wage flexibility. Under open market conditions, the price mechanism will correct short term misdirected production as owners will either drop prices or shift production to other profitable enterprises. Free labor markets also allow wages to fall or rise in accordance to the value of production. In this scenario, any unemployment in the economy is either

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<sup>291</sup> If a price of a product is above the equilibrium price, supply exceeds demand. This produces downward pressure on prices to the equilibrium price. In contrast, if prices of a product stand below the equilibrium price, demand exceeds supply. This results in upward pressure on wages to the equilibrium price.

<sup>292</sup> James Caporaso and David Levine, *Theories of Political Economy* (Cambridge: Cambridge University Press, 1992), p. 100.

<sup>293</sup> *Ibid.*, pp. 82-83. Under free market conditions, individuals are able to buy and sell at prices that produce maximum mutual benefit. As such, the aggregate effect of individuals acting in pursuit of maximization of private satisfaction in a free market allows for ‘win-win’ Pareto optimal outcomes.

<sup>294</sup> The natural level or real GDP is the level of GDP when resources in an economy are fully employed.

<sup>295</sup> Mark Blaug, “Say’s Law of Markets: What Did It Mean and Why Should We Care?,” *Eastern Economic Journal* 23, no. 2 (1997), pp. 231-235.

voluntary (e.g. – workers unwilling to take wages below market value) or “frictional” due to short term imperfections in the labor market.<sup>296</sup>

This approach also highlights the role that savings and investment have in maintenance of natural levels of real GDP. A certain percentage of income is saved rather than spent. An increase in savings reduces the demand for consumption of goods and services. In response, suppliers reduce production of consumption goods and services, employment falls, and the short term equilibrium level of real GDP falls below its natural level. While this appears to contradict Say’s Law, the classical argument counters that savings can be conceptualized as a source of spending for investment. Under normal circumstances, investment spending fills the gap of lowered consumption spending and the natural level of GDP is maintained.<sup>297</sup> Classical theorists also argue that free markets self-correct when the demand for investment falls below the supply available via saved income. In this scenario, flexible interest rates are the mechanism that adjusts saving and investment. In periods of excessive saving, for example, downward pressure is exerted on interest rates.<sup>298</sup> As interest rates fall, savings decrease and subsequent investment levels increase. Investment levels also increase as high rates of saving represents decreased demand and prices for consumer goods. As consumer goods industries become less profitable, resources shift toward investment industries that are in higher demand. Investment, for classical theorists, thus increases precisely when consumption decreases and moves the economy back to its equilibrium real GDP.<sup>299</sup>

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<sup>296</sup> Robert Skidelsky, *Keynes* (Oxford: Oxford University Press, 1996), pp. 77-78.

<sup>297</sup> Dudley Dillard, *The Economics of John Maynard Keynes: The Theory of a Monetary Economy* (Englewood Cliffs, New Jersey: Prentice-Hall, 1948), p.19.

<sup>298</sup> *Ibid.* At equilibrium, the amount of saving and investment are equal at interest rate  $i$ . If aggregate savings increases at interest rate  $i$ , real GDP falls below equilibrium level as the supply of money for investment exceeds demand for investment. This excess of supply of money for investment put downward pressure on interest rates.

<sup>299</sup> *Ibid.*, p. 20.

In his seminal *The General Theory of Employment, Interest, and Money*, Keynes leveled a broad based critique of the logic of market self-correction championed by classical theorists.<sup>300</sup> A key argument pushed by neoclassical economists in the interwar period was that increased wage inflexibility due to the rise of the labor movement undermined recovery and full employment.<sup>301</sup> Keynes maintained that even if wages, interest rates, and commodity prices are perfectly flexible and adjusted accordingly downward during periods of economic contraction, there is no guarantee that an economy will self-correct. In fact, as seen during the Depression era, an economy can reach equilibrium levels well below full economic capacity. This radical break from the self-correcting classical logic focused on three primary interrelated themes: money and its relationship to uncertainty; investment levels, effective demand, and employment; and the variable of human subjectivity in driving business cycles.

Classical and neoclassical understanding of money maintains that it serves only as a medium of exchange.<sup>302</sup> Keynes instead highlighted that money plays an additional role around the storage and maintenance of wealth as follows. Saved income can be lent for interest, invested in a capital asset, or held in liquid form. Individuals, particularly when they are uncertain about the future profitability of capital investment or return on interest rates, hoard money in liquid form. Given that the holding of excess savings in liquid form produces no income, money thus serves the function of wealth maintenance.<sup>303</sup> The fact that individuals choose to invest or not invest surplus income in productive

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<sup>300</sup> John Maynard Keynes, *The General Theory of Employment, Interest and Money* (New York: Harcourt, Brace and Company, 1936).

<sup>301</sup> Most influential in this regard was Cambridge University economist Arthur Cecil Pigou. In his influential *The Economics of Welfare*, Pigou argued that various policies emerging from the increased power of labor in the post WW I period increased voluntary unemployment and undermined economic recovery. See Robert Skidelsky, *John Maynard Keynes: The Economist as Savior, 1920-1937* (New York: Penguin Press, 1992), p. 597.

<sup>302</sup> This conception of money started with Adam Smith and was reinforced by the works of J.B. Say, David Ricardo, and John Stuart Mill. See Dudley Dillard, "The Barter Illusion in Classical and Neoclassical Economics," *Eastern Economic Journal* 14, no.4 (1988), pp.299-318 at pp. 299-311.

<sup>303</sup> Or, as summarized by Skidelsky, "People saved money not to *do* something with it, but because they felt anxious about the future." Skidelsky, *John Maynard Keynes: The Economist as Savior, 1920-1937*, p.595.

activity thus undermines the classical argument and Say's Law in two primary areas. First, individuals make choices to keep or not keep income in liquid form based on expectations about the future. For Keynes, these expectations about the future are primarily based on the subjective and often volatile "conventional wisdom" of the day. Mass psychology, rather than "rational actors responding to a rational world," thus is a key variable that determines if and when individuals will invest or hoard.<sup>304</sup> Second, when hoarding occurs, this liquid savings is not a component of demand but rather subtracts from it. Supply does not *de facto* create its own demand.<sup>305</sup>

Maintenance of demand in the economy through consumption is also undermined by high inequality. The wealthy minority has more income than they need for consumption. The poor majority, in contrast, consumes little due to low income levels.<sup>306</sup> Given this reality, Keynes highlighted the fundamental role that investment plays relative to production of income and maintenance of effective demand and employment. Investment not only supports demand in the future, it is essential for the maintenance of current levels of consumption.<sup>307</sup> Keynes thus focused on factors that undermine investment and subsequent full employment. As introduced above, a certain percentage of excess income is hoarded. Keynes argued that the rate of interest is best understood as the price paid to those who part with liquid savings.<sup>308</sup> The greater the desire to hoard (what Keynes termed the "liquidity

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<sup>304</sup> Keynes highlighted how dynamics of mass psychology in regard to expectations about the future produces high levels of instability in capitalist economies. He argued that classical theory ignored "the concealed factors of utter doubt, precariousness, hope and fear" that drive individual decisions. Dillard, *The Economics of John Maynard Keynes: The Theory of a Monetary Economy*, p.9.

<sup>305</sup> Skidelsky, *Keynes*, p. 79; Caporaso and Levine, *Theories of Political Economy*, p. 105.

<sup>306</sup> Dillard, *The Economics of John Maynard Keynes: The Theory of a Monetary Economy*, p.7.

<sup>307</sup> Caporaso and Levine also highlight the multiplier effect that investment and consumption produces as follows: "Revenues determine spending, which determines demand, which depletes inventories and thus stimulates production, which in turn generates revenues... Since the purchase of commodities generates incomes, and since incomes stimulate their recipients to purchase commodities, and initial addition to demand will multiply into a series of additions to demand. Since growth in demand will also stimulate investment in working capital to renew inventories; this investment will stimulate demand and revenues, which will multiple again into a series of expenditures." Caporaso and Levine, *Theories of Political Economy*, pp. 106-108.

<sup>308</sup> Classical theory, in contrast, argues that interest rates are the reward for delayed consumption.

preference”), the higher the interest rate must be to induce those with liquidity to part with cash.<sup>309</sup> Those with liquid assets will only invest these resources if the expected future profits from this investment are greater than the reward given by current interest rates.<sup>310</sup> Several dynamics thus can produce a downward spiral of economic retraction that can lead to economic recession or depression. If there is little confidence in future profitability, interest rate levels, even at very low levels, will exceed future expected earnings and investment decreases. Lower investment translates into reduced demand, higher unemployment, and reduced profits. Fear of still worse future conditions increases the incentive to hoard income in liquid form. This produces continued downward expectations on future profits and the downward cycle begins anew.<sup>311</sup>

Breaking this cycle thus requires several potential interventions from government to stimulate investment and aggregate demand. In moderate periods of economic contraction, an increase in money supply can lower interest rates sufficiently to catalyze investment. In more severe periods of economic contraction, monetary policy that reduces interest rates may not be sufficient. During these “liquidity traps,” Keynes maintained that government spending and investment were critical to jumpstart the economy back toward full productive capacity and full employment.<sup>312</sup> Along with short term monetary and fiscal policy response to economic contraction, Keynes identified a series of additional measures that reduced instability and unemployment over the long term. These include a steep

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<sup>309</sup> Dillard, *The Economics of John Maynard Keynes: The Theory of a Monetary Economy*, pp. 6-7.

<sup>310</sup> “Investment... is governed by the future expected return on investment goods discounted at the current rate of interest. Aggregate investment will be pushed to the point where the expected net yield... equals... the income which could be obtained from lending money rather than buying capital assets.” Skidelsky, *John Maynard Keynes: The Economist as Savior, 1920-1937*, pp.499-500.

<sup>311</sup> Dillard, *The Economics of John Maynard Keynes: The Theory of a Monetary Economy*, pp..6-7.,pp, 11-12; Skidelsky, *Keynes*, pp.78-86.

<sup>312</sup> On liquidity traps and the need for government spending to stimulate investment and a return to growth, see Hyman Minsky, *John Maynard Keynes* (New York: Columbia University Press, 1975), pp. 37-38; Paul Krugman, *Peddling Prosperity: Economic Sense and the Nonsense in the Age of Diminished Expectations* (New York: W.W. Norton & Company), pp. 31-32; and Caporaso and Levine, *Theories of Political Economy*, pp. 121-122.

progressive income tax, greater public investment and government coordination of private investment, and regulations to reduce speculative activities.<sup>313</sup>

Keynesianism emerged as the dominant economic theory in the 1930s until the mid-1950s and provided the intellectual foundation for those sympathetic to policies of countercyclical government intervention and highly regulated financial and international capital markets.<sup>314</sup> As the prominent framework that shaped the creation of the IMF, Keynesian theory also was prominently featured in early Fund policy.<sup>315</sup> This was most strongly expressed in initial support of capital controls. Along with reducing international volatility in the Bretton Woods framework, capital controls gave states the ability to implement countercyclical monetary and fiscal measures to support full employment policies. Keynesian-inspired ideas are also expressed in the Fund's framework of demand management in relation to balance-of-payment disequilibria. Components of the Polak model (see chapter 2), for example, are rooted in Keynesian assumptions that balance of payment crisis reflects imbalances of aggregate demand and supply and that multiple policy levers including monetary and fiscal intervention should be used to restore equilibrium.<sup>316</sup>

Contemporary critics of the IMF including Joseph Stiglitz argue that the institution moved away from its Keynesian roots mainly following the 1982 Mexican debt crisis until the 2008 global financial

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<sup>313</sup> Dillard, *The Economics of John Maynard Keynes: The Theory of a Monetary Economy*, pp.326-334.

<sup>314</sup> Jacqueline Best, "Hollowing Out Keynesian Norms: How the Search for a Technical Fix Undermined the Bretton Woods Regime," *Review of International Studies* 30, no. 3 (2004), pp.383-404 at p.389.

<sup>315</sup> James Boughton, "The IMF and the Force of History, The Ten Events and Ten Ideas that Have Shaped the Institution," IMF Working Paper WP/04/75 (Washington, D.C.: IMF, 2004), pp.13-14.

<sup>316</sup> Clift and Tommilson, "When Rules Started to Rule: The IMF, Neo-liberal Economic Ideas, and Economic Policy Change in Britain," p.11. Clift and Tommilson also note that while the Polak model contributed to the revival of monetary analysis in macroeconomics, Polak argued that his model was a "Keynesian inspired IMF version" that stood in contrast to a monetarist, "Chicago School revolutionary" approach. See Jacques Polak, "The Two Monetary Approaches to the Balance of Payments: Keynesian and Johnsonian," IMF Working Paper WP/01/100 (Washington D.C.: IMF, 2001), pp. 3-5.



crisis. For Stiglitz, the Fund was guilty of adopting “the pre-Keynesian position of fiscal austerity in the face of a downturn... which almost always entail contractionary policies leading to recessions or worse” during this time.<sup>317</sup> Several staff members interviewed for this project, in contrast, argued that Keynesianism has always remained at the center of the Fund’s normative culture, even during the Washington Consensus era:

Public perceptions have sometimes put the IMF in an ideological corner. I don’t think we had a dramatically different view [during the 1980s and 1990s]. You have to remember that we have always been a Keynesian institution. We are an institution of fiscal activists.<sup>318</sup>

Other staff members and Executive Directors noted that the post-2008 period witnessed a return to greater acceptance of Keynesian thinking in the economics profession and the institution:

In terms of institutional thinking, I think we started out as a Keynesian institution in the 1940s and 1950s and then moved quite a lot to the Chicago school, free market side of things and now it’s a little more middle of the road.<sup>319</sup>

I explore this possible return to Keynes in further detail below with a look at post-2008 shifts in LIC policy on inflation and fiscal and monetary counter-cyclical intervention.

### *The Neoclassical Synthesis*

The diversity of opinions among current IMF LIC staff in regard to when and how Keynesian thinking has influenced the Fund is partially explained by the emergence of the neoclassical synthesis. As outlined by Chwieroth, the main economics debate in the late 1950s and 1960s was not between Keynesians and the emerging monetarist school, but rather an internal Keynesian divide. One group, consisting primarily of economists based at Cambridge University, sought to preserve and build on a strict interpretation of Keynesian themes.<sup>320</sup> These self-described “post-Keynesians” argued for

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<sup>317</sup> Joseph Stiglitz, *Globalization and its Discontents* (New York: W.W. Norton, 2002), p.38 as cited in Boughton, “The IMF and the Force of History: Ten Events and Ten Ideas that Have Shaped the Institution,” p.14.

<sup>318</sup> Author interview with senior advisor in the African Department, Washington D.C., 19 September, 2011.

<sup>319</sup> Author interview of Fund staff member from Asia and Pacific Department, Washington D.C., 26 September 2011.

<sup>320</sup> Several prominent American economists including John Kenneth Galbraith also were tied to the post-Keynesians.

maintenance and expansion of capital control and a robust policy of countercyclical full employment policies.<sup>321</sup> Several American economists, including Paul Samuelson and James Tobin (also known as “neo-Keynesians”), instead argued for a rethinking of Keynes within a neoclassical framework.<sup>322</sup>

Samuelson et al. pushed for a “neoclassical synthesis” that combined aspects of Keynesian and classical theory and emerged as the dominant economic school of thought until the late 1970s. Proponents of the synthesis rejected neoclassical assumptions that economies self-correct and argued like Keynes that counter-cyclical government intervention is necessary to stimulate recessed economies to their full productive capacity. Neoclassical synthesists, however, diverged from Keynesianism in several key areas. While Keynesianism maintained that markets are inherently unstable and driven by irrational and inefficient use of information, neoclassical synthesists differentiated between short-term and long-term market dynamics. In the long term, markets are considered efficient and equilibrating. Long-term efficiency, however, is undermined by short-term market errors (e.g., asymmetric information, price stickiness). At the Fund, this translated into an emphasis on targeted, short-term fiscal and monetary response rather than a focus on a more permanent regime of government intervention.<sup>323</sup> The neoclassical synthesis and Fund policy also distanced itself from Keynes’ support of capital controls. Drawing back to neoclassical assumptions, both long and short term speculative capital flows were not considered destabilizing, but rather natural equilibrating factors in an open trading system.

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<sup>321</sup> Chwiero, *Capital Ideas*, p.74.

<sup>322</sup> Neoclassical synthesists played a prominent role in the Kennedy and Johnson presidential administrations. Both Samuelson and Tobin, for example, were members of Kennedy’s Council of Economic Advisors (CEA). See Best, “Hollowing Out Keynesian Norms: How the Search for a Technical Fix Undermined the Bretton Woods Regime,” p.394.

<sup>323</sup> Chwiero, *Capital Ideas*, p.76.

In what Jacqueline Best describes as the “hollowing out” of Keynesianism, the dismissal of Keynes’ focus on inter-subjective dynamics driving market behavior reframed macroeconomic issues as essentially technical, short-term issues that could be modeled and ultimately corrected.<sup>324</sup> The ascendancy of this interpretation of macroeconomics helped reinforce a technocratic, economic norm at the Fund that remains firmly embedded in the institution (see chapter 2). Based on interview with staff, this form of Keynesianism with a neoclassical and technocratic bent is arguably what many Fund staff who consider themselves Keynesians self-identify. Fiscal intervention that “works” in the short run is the primary concern rather than a focus on developing policy that accepts long-term instability and irrationality of modern capitalist economies.

### *Monetarism*

The neoclassical synthesis focus on demand management emerged as the dominant mainstream macroeconomic paradigm in the 1960s and early 1970s. Its most direct challenge came from the emerging popularity of monetarist theory in the 1970s and 1980s. Developed by economists associated with the University of Chicago including Milton Friedman, monetarists root their analysis in four primary assumptions.<sup>325</sup> First, as with neoclassical orthodoxy, markets free of distortion are efficient and equilibrating. Second, the amount of money in an economy is the primary variable driving total spending and overall level of economic activity and output. Expansion of money supply is reflected in increased economic activity, inflation, and inflationary expectations. Third, a stable and non-inflationary economy free of government intervention will tend toward full employment. Fourth, while

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<sup>324</sup> As articulated by James Tobin, “In the realms of macro-economics, at least, problems were coming to be treated as technical rather than ideological.” See James Tobin, *The New Economics One Decade Older* (Princeton, NJ: Princeton University Press, 1974), p.5 as cited by Best, “Hollowing Out Keynesian Norms: How the Search for a Technical Fix Undermined the Bretton Woods Regime,” p.383.

<sup>325</sup> Influential monetarist works include Milton Friedman, ed. *Studies in the Quantity Theory of Money* (Chicago, IL: University of Chicago Press, 1956); Milton Friedman, “The Role of Monetary Policy,” *American Economic Review* 58 (1968), pp.1-17; Milton Friedman and Anna J. Schwartz, *A Monetary History of the United States* (Princeton, N.J.: Princeton University Press, 1963) ; and Edmund Phelps, “Phillips Curves, Expectations of Inflation and Optimal Unemployment Over Time,” *Economica*, 34 (1967), pp.254-281.

long-term increases in money supply consistent with productive capacity of a society are stabilizing, short-term changes in money supply are destabilizing. Monetary stimulus unrelated to underlying fundamentals, for example, produces inflation with no guarantee of increased employment. Attempts to reduce inflation through a short-term decrease in money supply also are problematic due to what monetarists describe as “adaptive expectations.” Economic output and employment are reduced but high wages and prices remain due to lag time “between changes in fundamentals and the market’s perception of these changes.”<sup>326</sup>

Based on these assumptions, monetarist theory strongly contrasted with the neoclassical synthesis in several areas. First, countercyclical fiscal policy is at best inconsequential to growth and often detrimental as it crowds out private investment. Second, attempts to restore full employment through fiscal or monetary policy or to manage unemployment through wage intervention are counterproductive. Monetarists argue there is a natural rate of unemployment consistent with a society’s productive capacity and that government intervention to stimulate growth results in inflation with possibly little effect on increasing employment. Intervention in labor markets also produces wage distortions that unnecessarily maintain or increase unemployment above their natural levels. Third, given that short-term monetary intervention is problematic, discretionary monetary policy is to be avoided. Authorities should instead use fixed, rigid rules that support a gradual expansion of money supply in line with underlying productive capacity.<sup>327</sup>

Fund historian James Boughton asserts that monetarism “had less impact on the IMF than on the economics profession at large, and its influence was felt primarily in efforts made to examine and

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<sup>326</sup> Chwieroth, *Capital Ideas*, p.73.

<sup>327</sup> Clift and Tomlinson, “When Rules Started to Rule: The IMF, Neo-liberal Economic Ideas, and Economic Policy Change in Britain,” p.6.

ultimately reject it.”<sup>328</sup> Rather, it was the emergence of new classical economics (see below) that “had the biggest post-Keynesian impact on the IMF.”<sup>329</sup> This is arguably overstated as several prominent policy positions consistent with monetarism have shaped policy directives of the Fund. Most evident is the logic and general conclusion associated with components of the Polak model. While Polak explicitly differentiates his monetary approach to the balance of payments model as a “Keynesian inspired IMF version” from that of a competing “Chicago School revolutionary approach,” the main policy recommendations are the same: Creation of domestic credit leads to loss of foreign reserves of an equal amount.<sup>330</sup> As such, states with balance-of-payment deficits are advised to reduce domestic consumption.<sup>331</sup>

Another prominent impact of monetarism in IMF thinking was its stance on capital controls in the 1980s and 1990s. Monetarists frame aversion to capital controls as misguided, arguing that capital flow volatility is a symptom of speculators and investors responding rationally to underlying policy and institutional weakness. Capital movement thus is a corrective mechanism rather than a variable in and of itself that causes economic turmoil. This argument was expressed most forcefully by IMF Managing Director Michel Camdessus and First Deputy Managing Director Stanley Fischer in the late 1990s as they unsuccessfully lobbied for the Fund Executive Board to amend its Articles of Agreement to include jurisdiction over capital controls.<sup>332</sup> While the fallout from the Asian crisis

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<sup>328</sup> Boughton, “The IMF and the Force of History, The Ten Events and Ten Ideas that Have Shaped the Institution,” p.14.

<sup>329</sup> *Ibid.*, p.17.

<sup>330</sup> Both models assume fixed exchange rates. The creation of domestic credit puts downward pressure on the exchange rate. In order to maintain the fixed or pegged exchange rate, the central bank must use its foreign reserves to repurchase its excess currency on the foreign exchange market. See Michael Connolly, *International Business Finance* (London: Routledge, 2007), p.33.

<sup>331</sup> Polak’s main argument differentiating the two approaches is the Chicago School’s rejection of short term use of monetary policy to correct balance of payment deficits. See Jacques Polak, “The Two Monetary Approaches to the Balance of Payments: Keynesian and Johnsonian,” IMF Working Paper WP/01/100 (Washington D.C.: IMF, 2001), pp. 3-5.

<sup>332</sup> Stanley Fischer, “Capital Account Liberalization and the Role of the IMF,” *Conference on Development of Securities*, Inter-American Development Bank, Washington D.C. (28 October 1997).

cooled IMF efforts to pursue an integration of capital account liberalization into its formal mandate, two interconnected monetarist-inspired themes remain influential in Fund debates. First is the notion that the primary role of monetary policy is sustaining price stability rather than focusing on issues of full employment. Second, given the political pressure for short term inflationary stimulus, the most effective institutional arrangement to promote price stability is an arrangement where central banks are independent and follow fixed rules rather than ad hoc discretion when instituting monetary policy.<sup>333</sup>

### *New Classical Economics*

As with monetarism, new classical economics gained popularity in the 1970s as Keynesian-inspired models failed to provide a logical explanation of patterns of stagflation afflicting many major economies during this time. New classical economics, like monetarism, dismisses Keynesian assumptions of inefficient markets and roots its thinking in classical conceptions of prices, markets, and natural rates of unemployment.<sup>334</sup> Free of intervention, prices and wage levels clear markets (balance supply and demand) efficiently. New classical economics, however, diverges from monetarism in its conception of individual adaptability to changing market conditions. Monetarists maintain that markets clear in the long run but short-term inefficiencies in markets exist due to adaptive expectations and the relative inflexibility of prices and wages to adjust quickly to shifts in money supply. These short-term dynamics impact aggregate demand, employment levels, and economic output.<sup>335</sup> New classical theory rejects the notion that markets and prices only clear over medium and long time horizons. Rather, rational, utility maximizing individuals and firms constantly adjust to changing market conditions to maximize profit and/or utility. The aggregate effect of

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<sup>333</sup> Stanley Fischer, "Maintaining Price Stability," *Finance and Development* 33, no.4 (1996), pp.34-37 at p.35.

<sup>334</sup> New classicalism, for example, maintains that Keynesian aggregate-level macroeconomic models fail to account for individuals and firms' behavior in "formulating expectations for a future that is substantially different from the past." Mark Willis, "Rational Expectations as a Counterrevolution," in *The Crisis of Economic Theory*, ed. Daniel Bell and Irving Kristol (New York: Basic Books, 1981), pp.81-96 at pp. 87-88.

<sup>335</sup> If an economy sees a decrease in money supply, for example, consumption and aggregate demand fall. As prices and wages are generally inflexible, they fail to quickly respond to reduced demand. This results in a drop in production and increased unemployment.

individuals and firms acting rationally and in “real time” guarantees that prices accurately reflect underlying fundamentals and quickly balance supply and demand.

Individuals and firms also develop what John Muth initially described as “rational expectations” of future market direction.<sup>336</sup> Rational economic actors learn to predict changes in government policies and also how to react to these changes to maximize profits and utility. Through this process, new classical theorists argue that individuals and firms will also offset government policy aims, preventing them from having a real effect on aggregated demand and economic output.<sup>337</sup> This translates into an aversion of “activist” fiscal or monetary intervention:

Activist policies must be curbed, first, because a growing body of evidence...suggests that existing models cannot succeed in offsetting the normal fluctuations in output, employment, or other aggregates. Second, activist policies must be curbed because most of their effects are uncertain...Third, activist policies must be curbed because even if we know what their results would be, we wouldn't know whether they were desirable or not.<sup>338</sup>

Neoclassicalists instead advocate that governments focus on issues of market stability and intervene primarily in areas that improve overall efficiency.

Specific to the Fund and LICs, a focus on efficiency and stability rather than activist intervention was a key component of structural adjustment lending under the SAF and ESAF frameworks in the 1980s and 1990s. Merging aspects of new classical and monetarist thinking, reduction in government spending was seen as the most effective macroeconomic tool to stimulate growth by reversing low

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<sup>336</sup>John Muth, “Rational Expectations and the Theory of Price Movements,” *Econometrica* 29, no.3 (1961), pp.315-323.

<sup>337</sup> *Ibid.*, New classical theorists present the following scenario during a period government monetary expansion designed to increase output and employment . In anticipation of inflation, consumers will spend on goods and services before prices rise. Firms, for their part, will raise prices. Unemployed individuals will adjust to inflationary expectations and hold out for higher wages. Government expansionary policy thus produces (1) immediate increases in nominal demand and lower supply that results in no change in aggregate output or unemployment levels and (2) higher price levels.

<sup>338</sup> Willis, “Rational Expectations as a Counterrevolution,” p.94.

rates of private investment and high inflation found in the majority of poor states during this period.<sup>339</sup> Fiscal austerity via cuts in government employment and caps on salaries and transfers was also pushed to reduce overall consumption and produce so-called “demand compression” to help reverse balance of payment deficits.<sup>340</sup> While conditionality frameworks under the PRGF and ECF/SCF/RCF moved away from the notion that fiscal austerity and private investment guarantees growth, components of new classical and monetarist themes remain. In a 2008 staff paper outlining the role of Fund in LICs, for example, “prudent fiscal policy” entails a “fiscal stance” that helps “ensure macroeconomic stability and debt sustainability, and avoids crowding out.”<sup>341</sup>

### *New Keynesianism*

New Keynesianism first emerged in the early 1980s as a reaction to monetarist and new classical critiques of Keynesian inspired theory. As outlined by Bruce Greenwald and Joseph Stiglitz, New Keynesians share with traditional Keynesians three general propositions: “1. During some periods – often extended – an excess supply of labor exists at prevailing level of real wages. 2. The aggregate level of economic activity fluctuates markedly... These fluctuations are greater in magnitude and different in pattern from any that might be accounted for by short-run changes in technology, tastes, or demography. 3. Money matters, at least most of the time, although monetary policy may be ineffective in some periods (like the Great Depression).”<sup>342</sup> While in disagreement with new classical and

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<sup>339</sup> The argument for this strategy was presented as follows. First, high levels of government spending pushes up interest rates and lowers private borrowing and investment. Second, government spending is primarily in the form of short-term transfers (e.g. salaries, welfare payments, subsidies, and grants) that increase aggregate money supply. An increase in money supply out of proportion with underlying productive capacity produces inflation that undermines investor confidence. Fiscal austerity reverses these trends. Reduced government spending enables interest rates to fall and reduces inflation. As private borrowing costs and inflation fall, private investor activity and business confidence increases and growth returns.

<sup>340</sup> John Rapley, *Understanding Development: Theory and Practice in the Third World* (London: Lynne Rienner, 2007), p. 81.

<sup>341</sup> IMF, “The Role of the Fund in Low-Income Countries,” 13 June 2008, p. 11, available at <http://www.imf.org/external/np/pp/eng/2008/061308.pdf>.

<sup>342</sup> Bruce Greenwald and Joseph Stiglitz, “New and Old Keynesians,” *Journal of Economic Perspectives*, 7, no.1 (1993), pp.23-44 at p.23. Robert Gordon, in a similar manner, describes New Keynesianism as follows: “The essential feature of Keynesian macroeconomics is the absence of continuous market clearing. Thus a Keynesian model is by definition a



monetarist assumptions concerning market self-correction, New Keynesians concede that the new classical focus on microeconomic principles to explain macroeconomic outcomes is an important advancement. New Keynesians thus adopt the micro-foundational focus of new classical economics but differ in their assumptions about the nature of markets. While new classical models see market distortion as the exception rather than the rule, New Keynesians highlight that imperfect information and other distorting externalities are a “given” in market transactions.<sup>343</sup> The cumulative effect of individuals rationally responding to imperfect market conditions produces aggregate market failure, particularly in the short run.<sup>344</sup>

New Keynesians highlight several dynamics that produce price and wage rigidities during periods of economic downturn that undermine market clearing. Specific to prices, the concepts of “menu costs” and “price staggering” explain why reduced demand during economic downturn does not necessarily result in lower prices. Menu costs refer to the cost of changing prices. Prices do not adjust quickly or continuously as it costs firms resources to implement a new price.<sup>345</sup> Price staggering also occurs as firms are conscious of their prices relative to other firms and don’t want to be the first to decrease their prices.<sup>346</sup> In regard to explanations of involuntary unemployment, the concept of “efficiency wages”

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nonmarket-clearing model, one in which prices fail to adjust rapidly enough to clear markets within some relatively short period of time...The task of New Keynesian economics is to explain why changes in the aggregate price level are sticky.” Robert Gordon, “What is New Keynesian Economics?,” *Journal of Economic Literature* 28 (1990), pp.1115-1171 at pp. 1116 and 1135 as cited by Guido Zimmerman, “Optimal Monetary Policy: A New Keynesian View,” *The Quarterly Journal of Austrian Economics* 6, no.4 (2003), pp. 61-72 at p. 62.

<sup>343</sup> David Romer, “The New Keynesian Synthesis,” *Journal of Economic Perspectives* 7, no.1 (1993), pp.5-22.

<sup>344</sup> “...new classical economists base their theories on simple (we would say simplistic) models of markets that employ perfect information, perfect competition, the absence of transaction costs, and the presence of a complete set of markets...In contrast, modern Keynesians have identified real world “imperfections” as the source of the problem: leaving them out is the model is like leaving Hamlet out of the play.” Greenwald and Stiglitz “New and Old Keynesians,” p.23-24.

<sup>345</sup> The concept of menu costs was first developed by N. Gregory Mankiw. See N. Gregory Mankiw, “Small Menu Costs and Large Business Cycles: A Macroeconomic Model of Monopoly,” *Quarterly Journal of Economics* 100, no.2 (1985), pp. 529-537.

<sup>346</sup> Guillermo Calvo, “Staggered Prices in a Utility-Maximizing Framework,” *Journal of Monetary Economics* 12, no.3 (1983),pp.383-398; John Taylor, “Aggregate Dynamics and Staggered Contracts,” *Journal of Political Economy* 88, no.1 (1980), pp. 1-23.

highlights why wages may remain high despite high unemployment. Firms pay above market average wages as high wages make workers more productive, produce less turnover, and attract more qualified and dedicated employees. In the aggregate, the choice of individual firms to pay above equilibrium wages to their high value workers reinforces involuntary unemployment.<sup>347</sup>

In regard to macroeconomic policy response, New Keynesians are generally conservative in their application of expansionary monetary and fiscal policy.<sup>348</sup> Influential New Keynesians including N. Gregory Mankiw, for example, are strong supporters of inflation targeting and present their policy positions primarily as a response to demand shocks (e.g., government spending).<sup>349</sup> In the short run, central bank manipulation of interest rates is to be used to counter inflationary pressure caused by demand shocks. Given that prices and wages are sticky, however, there will be periods of involuntary unemployment following a necessary reduction in money supply. The best solution therefore is to proactively avoid imbalances caused by introducing excessive aggregate demand into the economy.<sup>350</sup> This framing of monetary policy became the norm in the 1990s through broad acceptance within central banks and the Fund of the so called “Taylor Rule.” Introduced by New Keynesian economist John Taylor in 1992, it stipulated that central banks “lean against the wind” by systematically responding to increased inflation “with a more-than-proportional increase” in nominal interest rates.<sup>351</sup>

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<sup>347</sup>Carl Shapiro and Joseph Stiglitz, “Equilibrium Unemployment as a Worker Discipline Device,” *The American Economic Review* 74, no.3 (1984), pp.433-444.

<sup>348</sup> A prominent exception to the rule here is Stiglitz who advocates a more traditional Keynesian position.

<sup>349</sup> Inflation targeting involves central banks setting low rates of inflation and then abiding by them. New Zealand was the first country to adopt inflation targeting in 1989. As of 2010, 26 countries used inflation targeting. See Scott Rodger “Inflation Targeting Turns 20,” *Finance and Development* 47, no.1 (2010), pp. 46-49.

<sup>350</sup> Zimmerman, “Optimal Monetary Policy: A New Keynesian View,” at p.62; Daniela Gabor, “The International Monetary Fund and its New Economics,” *Development and Change* 41, no.5 (2010), pp.805-830 at p.807.

<sup>351</sup> Prakash Loungani, “Quest for Rules,” *Finance and Development* 45, no.1 (2008), pp.6-9 at p.8.

## **The 2008 (legitimacy) Crisis and a Return to Keynes?**

A combination of monetarist, new classical, and New Keynesian theory (also referred to as “the New Consensus”) was reflected in Fund macroeconomic positions from the 1982 Mexican debt crisis to the 2008 global financial crisis. Inflation management was the primary goal of monetary policy along with a dismissal of countercyclical fiscal policy. Trust in the stability and long term efficiency of markets also factored into aversion to government intervention into labor and financial markets. Relative low volatility, low unemployment, and low inflation in most industrialized states from the 1980s to 2008 were attributed to these policy directives. Described as “The Great Moderation,” proponents of the New Consensus including then Federal Reserve governor Ben Bernanke argued that financial liberalization and “improved macroeconomic performance, particularly monetary policy” were primarily responsible for nearly three decades of steady growth and low inflation in industrialized states.<sup>352</sup> Olivier Blanchard, for his part, declared in August 2008 that an intellectual consensus had formed around appropriate monetary, fiscal, and regulatory response, concluding that the “state of macro was good.”<sup>353</sup>

As introduced above, constructivists focused on the IMF argue that a “crisis of legitimacy” can facilitate ideational change and policy reform. The 2008 global financial crisis proved to be such an event as components of three decades of macroeconomic policy consensus were called into question. Dominique Strauss-Kahn, in a 2011 speech delivered at an IMF sponsored forum on “Macro and Growth Policies in the Wake of the Crisis,” captured this sentiment in his opening remarks:

The last few years have not only been a crisis for the global economy, but also a crisis for economics. The Great Moderation led too many of us to underestimate macroeconomic

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<sup>352</sup> Ben Bernanke, “The Great Moderation,” Eastern Economic Association, Washington, D.C., 20 February 2004, available at <http://www.federalreserve.gov/boarddocs/speeches/2004/20040220/default.htm> (accessed 8 April 2012).

<sup>353</sup> Olivier Blanchard, “The State of Macro,” Working Paper 14259, NBER Working Paper Series August 2008, p.1, available at [http://www.nber.org/papers/w14259.pdf?new\\_window=1](http://www.nber.org/papers/w14259.pdf?new_window=1).

risks...the recent experience has raised profound questions about the pre-crisis consensus on macroeconomic policies.<sup>354</sup>

Blanchard, in an apparent mea culpa, shared a similar notion that the relative stability in advanced economies prior to the 2008 crisis had “lulled economists and policymakers into a false sense of security” and that the “Great Recession” required “a reassessment of what we know about how to conduct macroeconomic policy.”<sup>355</sup> As outlined below in analysis of shifts in monetary and fiscal policy, the post-2008 period is characterized in part by the growing influence of more orthodox aspects of Keynesian theory.

### *Monetary Policy*

In regard to monetary policy, Blanchard outlined the pre-2008 consensus thinking in these terms:

Stable and low inflation was presented as the primary, if not exclusive, mandate of central banks. This was the result of coincidence between the reputational needs of central bankers to focus on inflation...and the intellectual support for inflation targeting by the New Keynesian model....There was an increasing consensus that inflation should not only be stable, but very low (most central banks chose a target around 2 percent).<sup>356</sup>

Blanchard also noted that despite some debate among economists that exceedingly low target inflation rates could replicate dynamics of deflationary spirals seen during the Great Depression, these concerns were largely dismissed prior to the 2008 crisis: “The liquidity traps in the Great Depression, combining significant deflation, and low nominal rates, were seen as belonging to history, a reflection of policy errors that could now be avoided.”<sup>357</sup> Blanchard argued that there is now recognition that inflation targets were too low in the pre-2008 era and led to “costly” consequences:

When the crisis started in earnest in 2008, and aggregated demand collapsed, most central banks quickly decreased their policy rate to close to zero. Had they been able

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<sup>354</sup> Dominique Strauss-Kahn, “Opening Remarks: Macro and Growth Policies in the Wake of the Crisis,” Washington, D.C., 7 March 2011, available at <http://www.imf.org/external/np/speeches/2011/030711.htm> (accessed 10 April 2012).

<sup>355</sup> Jeremy Clift, “Interview with Olivier Blanchard: IMF Explores Contours of Future Macroeconomic Policy,” *IMF Survey Online*, 12 February 2010, available at <http://www.imf.org/external/pubs/ft/survey/so/2010/int021210a.htm> (accessed 1 June 2012).

<sup>356</sup> IMF, “Rethinking Macroeconomic Policy,” pp.3-4.

<sup>357</sup> *Ibid.*, p.4

to, they would have decreased the rate further: estimates...suggest another 3 to 5 percent for the United States. But the zero nominal interest rate bound prevented them from doing so...it is clear that the zero nominal interest rate bound has proven costly. Higher average inflation, and thus higher nominal interest rates to start with, would have made it possible to cut interest rates more, thereby probably reducing the drop in output and the deterioration of fiscal position.<sup>358</sup>

Specific to LICs policy, the debate on appropriate inflation levels prior to the 2008 crisis appeared more sensitive to the effects of exceedingly low inflation targets on growth rates and monetary flexibility. In a 2005 staff paper, discussion around appropriate inflation rates recognized that “the desirability of single digit inflation had been questioned” and that no consensus around the appropriate inflation rates for LICs had been clearly established. In their ultimate conclusion that LIC policy rates should be targeted between 5 and 10 percent, Fund staff argued that LICs needed room for short term expansionary intervention due to the high risks of exogenous shocks to their economies, but also warned against inflation levels above 10 percent:

On balance, the above considerations support the use of single-digit inflation targets.... However, pushing inflation too low, say below 5 percent, may entail a loss of output and seigniorage revenue, suggesting a need for caution in setting very low inflation targets in low-income countries. As these countries tend to be subject to larger output volatility and more pronounced price shocks, program design should take these economic attributes properly into account. In particular, inflation targets should be set so as to help avoid risks of an unintended contractionary policy stance.<sup>359</sup>

If discussion prior to the crisis called for higher inflation rates, the 2008 crisis resulted in LIC staff more forcefully pushing flexible monetary response. As seen in Figure 4.2 below, target rate inflation levels of LICs negotiated with the Fund have increased under the new ECF/RCF/SCF framework. 20 of 34 LIC lending arrangements negotiated in 2010-2011 have inflation targets above 5 percent as

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<sup>358</sup> *Ibid.*, p.8.

<sup>359</sup> IMF, “Monetary and Fiscal Policy Design Issues in Low Income Countries,” 8 August 2005, p.19., available at <http://www.imf.org/external/np/pp/eng/2005/080805m.pdf> (accessed 1 June 2012).

compared to 10 of 32 under PRGF lending from 2003-2007. 5 LICs also have inflation targets between 10 and 20 percent under the new lending arrangements.<sup>360</sup>

Figure 4.2 Target LIC Inflation Rates (1995-2011)  
(Number of LICs)

	3% below	3.1%-5%	5.1-10%	10.1-20%
1995-1999 (ESAF)	15	13	14	5
2003-2007 ("late" PRGF)	12	10	9	1
2010-2011 (ECF/RCF/SCF)	7	7	15	5

Source: Goldsbrough et al (2007); Martin and Watts (2012)

Staff debates on how LICs should deal with the aftermath of the 2008 crisis maintain that most LICs were conservative in their monetary response and argue that in future downturns a "more active monetary easing" is advisable:

In the 2009 downturn, LICs did not fully exploit the scope of monetary easing...while LICs did lower nominal policy rates, they did so by less than the decline in inflation would have allowed, resulting in sharply higher real policy rates at the peak of the crisis. In the event of another global downturn and softening of commodity prices, more active monetary easing may be appropriate in LICs with moderate inflation.<sup>361</sup>

<sup>360</sup> Data compiled for Table David 15 is from Goldsbrough, Ehui Adover, and Ben Elberger, "Inflation Targets in IMF-Supported Programs," Center for Global Development (March 2007). pp. 5-8 and Matthew Martin and Richard Watts, "Enhancing the IMF's Focus on Growth and Poverty Reduction in Low-Income Countries," Development Finance International (April 2012), pp. 25-26.

<sup>361</sup> IMF, "Managing Global Growth Risks and Commodity Price Shocks-Vulnerabilities and Policy Challenges for Low Income Countries," 21 September 2011, p.26., available at <http://www.imf.org/external/np/pp/eng/2011/092111.pdf> (accessed 4 May 2012).

Staff from the Africa Department also argue for Keynesian-inspired monetary policy that reflects inflation levels and adjusts accordingly: “As inflation falls, monetary policy should be eased...On the other hand, countries still experiencing excessive inflation many need to tighten monetary policy.”<sup>362</sup>

### *Fiscal Policy*

New Consensus thinking, drawing from monetarist, new classical, and New Keynesian theory, dismissed countercyclical fiscal policy as an appropriate macroeconomic policy tool. As noted by Blanchard, “In the 1960s and 1970s, fiscal and monetary policy had roughly equal billing...In the past two decades, however, fiscal policy took a backseat to monetary policy.”<sup>363</sup> For New Keynesians, aversion to countercyclical fiscal response was coined in terms of rational expectations of individual economic agents. Individuals aware of plans of increased government spending financed through taxes or bonds understand that such activity negatively impacts future income. As such, they rationally chose to decrease consumption to save for future higher taxation. The subsequent drop in consumption therefore offsets attempts by government authorities to stimulate aggregate demand.<sup>364</sup> Monetarists and new classicalists also portrayed countercyclical fiscal response as irresponsible, as deficit spending undermined macroeconomic stability through increased inflationary pressure.

Since the 2008 crisis, countercyclical fiscal policy has been reestablished as an appropriate component of macroeconomic response in the Fund. Strauss-Kahn fired the first shot at the New Consensus in early November 2008. The crisis, he argued, was “...what economists call a Keynesian recession” and required coordinated international fiscal expansion to stimulate demand and “avoid a global

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<sup>362</sup> IMF, *Impact of the Global Financial Crisis on Sub-Saharan Africa*, (Washington, D.C.: IMF, 2009), p.7, available at [http://www.isdbforum.org/Subjects/Causes-Impact\\_of\\_the\\_Financial\\_Crisis/Impact\\_Global\\_Financial\\_Crisis\\_Sub-Saharan\\_Africa.pdf](http://www.isdbforum.org/Subjects/Causes-Impact_of_the_Financial_Crisis/Impact_Global_Financial_Crisis_Sub-Saharan_Africa.pdf). (accessed 1 June 2012)

<sup>363</sup> IMF, “Rethinking Macroeconomic Policy,” p.5.

<sup>364</sup> Gabor, “The International Monetary Fund and its New Economics,” p.816.

depression.”<sup>365</sup> At a November 2008 emergency G-20 summit meeting, Strauss-Kahn welcomed the fact that G-20 leaders emphasized “fiscal stimulus, which I believe is now essential to restore global growth.”<sup>366</sup> Fund staff papers during the first year of the crisis reiterated similar themes. A joint staff paper from the Research and Finance Departments in December 2008 urgently argued for a “timely, large, lasting, diversified, contingent, collective, and sustainable” fiscal policy stimulus to increase aggregate global demand.<sup>367</sup> In perhaps the most dramatic shift in policy recommendations since the early 1980s, the paper warned against pro-cyclical balanced budget requirements and called for a strong public sector involvement to help stimulate demand:

First, ... governments should make sure that existing programs are not cut for lack of resources. In particular, central governments or sub-national governments that are facing balanced budget rules may be forced to suspend various spending programs. Measures should be taken to counteract the procyclicality build in these rules.... Second, spending programs, from repair and maintenance, to investment projects delayed, interrupted or rejected for lack of funding or macroeconomic considerations, can be (re)started quickly. A few high profile programs, with good long-run justification and strong externalities, (for example, for environmental purposes) can also help, directly and through expectations. Given the higher degree of risk facing firms at the current juncture, the state could also take a larger share in private-public partnerships for valuable projects that would otherwise be suspended for lack of private capital.<sup>368</sup>

Acceptance of Keynesian themes of countercyclical intervention has also been seen in the Fund’s support of “automatic fiscal stabilizers” in the post-2008 era. As outlined by Blanchard et al., the impact of future recessions could be ameliorated if automatic targeted tax rebates and income transfers

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<sup>365</sup> Dominique Strauss-Kahn, “Staving off a Global Depression,” *The Guardian* 3 November 2008, available at <http://www.guardian.co.uk/commentisfree/2008/nov/03/marketturmoil-banks>.

<sup>366</sup> IMF, “IMF Managing Director Dominique Strauss-Kahn Calls G-20 Action Plan Significant Step toward Stronger International Cooperation,” IMF Press Release No. 08/286 15 November 2008, available at <http://www.imf.org/external/np/sec/pr/2008/pr08286.htm>. (accessed 1 June 2012)

<sup>367</sup> Antonio Spilimbergo, Steve Symansky, Olivier Blanchard, and Carlo Cottarelli, “Fiscal Policy for the Crisis,” IMF Staff Position Note SPN/080/01 29 December 2008, available at <http://www.imf.org/external/pubs/ft/spn/2008/spn0801.pdf>. (accessed 1 June 2012).

<sup>368</sup> *Ibid.*



to “low-income or liquidity-constrained households” were implemented once employment levels fell below a threshold level.<sup>369</sup>

As with monetary policy, staff involved with LIC policy diverged somewhat from the broader institutional and professional consensus on fiscal policy prior to the 2008 crisis. Starting with the PRGF, fiscal policy advice centered on issues of debt sustainability, strategic financing, and appropriate public expenditure to support the Millennium Development Goals (MDGs).<sup>370</sup> Staff argued that fiscal policy ultimately should work to lower budget deficits and public debt levels to manageable levels, as doing so would increase levels of private investment and subsequent growth. Specific to LICs, however, a history of unsustainable debt levels produced dynamics that undercut the ability of these states to pursue prudent fiscal policy choices. Staff argued for a two tiered strategy. LICs should work toward a tighter fiscal stance while multilateral institutions and bilateral donors should concurrently maintain or increase concessionary lending and debt forgiveness to produce policy space for pursuing MDG initiatives.

Following the broader institutional trend following the 2008 crisis, countercyclical fiscal policy reentered the policy tool-kit for LICs. A series of staff papers focused on the crisis and LIC response, for example, highlighted the importance of countercyclical fiscal intervention during the crisis and rebuilding “policy buffers” going forward in preparation for future economic recession:

Growth was supported by a countercyclical policy response—a first for LICs in contrast to past crises when the fiscal stance was tightened. Most LICs let their fiscal automatic stabilizers operate, and the median income in real primary spending was higher than in the previous five years... Empirical analysis suggests that the response allows vital spending to

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<sup>369</sup>IMF, “Rethinking Macroeconomic Policy,” pp 15-16.

<sup>370</sup> Author interview with former Deputy Director the African Department, Washington D.C., 13 June, 2011..

be preserved, in particular on social sectors and infrastructure, and helped mitigate the negative impact of the global crisis on economic growth and the poor.<sup>371</sup>

Fund staff involved with LICs also maintained that targeted income transfer plans “to the poorest often result in a larger stimulus to aggregate demand, given their higher propensity to consume” and argued for targeted public works programs and income transfer as a component of fiscal stimulus.<sup>372</sup>

When asked what drove the IMF to support more Keynesian fiscal and monetary policy choices in the new ECF/RCF/SCF framework, answers from LIC staff generally came to the conclusion that the macroeconomic position of LICs leading into the 2008 crisis was the most influential variable shaping why LIC staff supported a countercyclical position:

Many countries had built up quite significant policy space because debt had been reduced, inflation had come down, because deficits across the board were relatively small. All of these things put together allowed countries some room and they used it. I don't think there has been some sort of deep ideological change.<sup>373</sup>

In 2008, many LICs were in much more favorable position than they would have been ten years prior. Due to their good macroeconomic performance, they had built up policy buffers that they were able to then use. It was that change that made it very clear to observers outside the Fund that countercyclical policies have a role.<sup>374</sup>

This was a new policy direction but the new direction was driven by the conditions in low income countries. It was at some level pragmatic advice that worked because countries actually had the reserves and policy space to actually do the stimulus. I would not pin the Fund's position too much on any internal change in culture and thinking but perhaps more of an evolution also of the countries that we work in.<sup>375</sup>

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<sup>371</sup> IMF, “Emerging from the Global Crisis: Macroeconomic Challenges Facing Low-Income Countries,” 5 October 2010, p.4, available at <http://www.imf.org/external/np/pp/eng/2010/100510.pdf>.

<sup>372</sup> IMF, *The Implications of the Global Financial Crisis for Low-Income Countries* (Washington, D.C.: IMF, 2009), p.31, available at <http://www.imf.org/external/pubs/ft/books/2009/globalfin/globalfin.pdf>.

<sup>373</sup> Author interview with senior advisor in the Africa Department, 19 September, 2011. International Monetary Fund, Washington D.C.

<sup>374</sup> Author interview with Assistant Director of Research Department, 13 June, 2001, International Monetary Fund, Washington D.C.

<sup>375</sup> Author interview with Division Chief of Strategy, Policy, and Review Department, 14 June, 2011. International Monetary Fund, Washington D.C.

Staff explanations as to why the Fund shifted in a more Keynesian direction thus did not reflect this as representative of a broader crisis of legitimacy.

### **Structural Reform and Market Efficiency**

Unlike fiscal and monetary shifts seen after 2008, evidence points to little significant challenge to norms that champion improved market efficiency as the primary goal of structural reform. Since the 1982 debt crisis and through the Asian crisis of the late 1990s and the 2008 global financial crisis, IMF policy has consistently supported market-determined exchange rates, trade liberalization, and aversion to government-induced price intervention as the most prudent course of action for growth and development. Specific to LICs, policy focused on poverty reduction that first emerged under the PRGF and continued with the ECF/RCF/SCF framework explicitly argues for removal of market distortive policies as a prime tool to meet poverty reduction targets in LICs.

Normative frames wary of market distortion have their roots in debates in the 1950s and 1960s. During this time period, IMF policy advocating limited state intervention and trade integration contrasted sharply with those sympathetic to the then popular strategy of ISI. As outlined in chapter 2, proponents of ISI argued poor states could only develop if they abandoned liberal economic models dependent on export of primary commodities. ISI instead advocated for internal industrialization through a series of state interventions that ostensibly reduced dependence on exports and kick-started the economy into producing manufactured goods for domestic consumption. While those critical of ISI stood outside the mainstream in the 1950s and 1960s, faltering growth rates in the 1970s across much of Latin America,

Africa, and the Middle East and the fallout from the 1982 Mexican debt crisis reshaped the development debate on terms more in line with the Fund's position.<sup>376</sup>

Most notable in this respect was a series of influential publications in the 1970s supported by the Organization for Cooperation and Economic Development (OECD),<sup>377</sup> the National Bureau of Economic Research (NBER),<sup>378</sup> and the Brookings Institution<sup>379</sup> that focused on various deleterious effects of market distortions caused by ISI policies. Following the 1982 crisis, two edited volumes from the Institute of International Economics focused on Latin America reinforced similar themes.<sup>380</sup> Bela Balassa et al.'s *Toward Economic Growth in Latin America* (1986) underscored how inefficiency and corruption due to state intervention in Latin America had produced economic stagnation and dependency on global capital markets to finance deficits.<sup>381</sup> John Williamson's *Latin American Adjustment: How Much Has Happened?* (1990) outlined a growing "Washington Consensus" within the IMF, World Bank, D.C. -based think tanks and the U.S. government concerning appropriate policy to reform indebted ISI states.<sup>382</sup> These critiques of ISI served as the ideological foundation for aversion to state intervention in development outcomes that remain strongly embedded in Fund thinking and policy choices. I explore in more detail below how this has manifested itself in three

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<sup>376</sup> Harold James, "Bretton Woods and the Debate about Development," pp.40-45.

<sup>377</sup> Ian Little, Tibor Scitovsky and Maurice Scott, *Industry and Trade in Some Developing Countries* (London: Oxford University Press, 1970) ; Edward Shaw, *Financing Deepening in Economic Development* (London : Oxford University Press, 1973).

<sup>378</sup> Jagdish Bhagwati, *Anatomy and Consequences of Exchange Control Regimes* (Cambridge MA: Ballinger Press, 1978); Anne Krueger, *Foreign Trade Regimes and Economic Development: Liberalization Attempts and Consequences* Cambridge MA: Ballinger Press, 1978).

<sup>379</sup> Ronald McKinnon, *Money and Capital in Economic Development* (Washington, D.C.: Brookings Institution, 1973).

<sup>380</sup> The Washington D.C. based Peterson Institute for International Economics (formerly the Institute for International Economics) was founded in 1981 and remains among the most influential think-tanks concerning international economic policy.

<sup>381</sup> Bela Balassa, Gerardo Beuno, Pedro-Pablo Kuczynski, and Mario Henrique Simonsen, *Toward Renewed Economic Growth in Latin America* (Washington, D.C.: Institute for International Economics, 1986).

<sup>382</sup> John Williamson, *Latin American Adjustment: How Much Has Happened?* (Washington, D.C.: Institute for International Economics, 1990).

policy areas applied to LICs: market determined exchange rates, support of trade liberalization, and aversion to government-induced price distortion.

### *Exchange Rates*

A primary purpose of the IMF, outlined in Article I (iii) of the Articles of Agreement, is “to promote exchange stability, to maintain orderly exchange arrangements among members, and to avoid competitive exchange depreciation.” Fund thinking concerning the relationship between exchange rates, growth, and development in poor states is summarized as follows. Drawing from monetarist inspired theory, an assumption is first made that aggregate money supply is relatively stable, that individuals have access to goods and money balances, and that the demand for goods and money is positively correlated with income. A temporary disequilibrium between current money holding and long run demand for money produces a movement in international reserves. High demand for money due to economic expansion and/or deficit spending, for example, generates a trade surplus, as that economy imports money through increased exports to increase its money supply. Conversely, excess supply of money gives rise to a trade deficit as the country reduces supply of money through a rise in imports. Under open market conditions, exchange rate fluctuations reflecting case specific macroeconomic fundamentals are to be expected and states generally should not act to artificially create overvalued or undervalued currency values.<sup>383</sup>

Due in part to the history of ISI, the primary concern of Fund staff over the past three decades is that developing states may return to a pattern of state intervention that overvalues exchange rates. LICs, particularly in Sub-Saharan Africa, also demonstrated more willingness than many other developing states in the post-ISI era to intervene in currency markets to maintain inflated exchange rates during

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<sup>383</sup> David, *The IMF Policy Paradigm*, p.88.

the 1980s and 1990s.<sup>384</sup> The argument against artificial overvaluation of currency focuses on the following themes: (1) Overvaluation represents a tax on exports and subsidization of imports. Discrimination against exporters lowers their ability to compete in foreign markets, lowers foreign exchange receipts, and subsequently undermines a state's ability to obtain imports; (2) Limited foreign reserves may also become rationed and inefficiently allocated by the state; (3) Overvaluation puts pressure on import-competing industries. As seen under ISI, these interests will lobby for protectionist measures that further distort markets; (4) Overvaluation stokes possibilities of capital flight, particularly when currency comes under speculative attack; and (5) Defending an overvalued currency through tight monetary policy can produce economic recession.<sup>385</sup>

Exchange rate stability in LICs is also particularly vulnerable to the effects of large and sporadic inflows and outflows of foreign currency into their economies. Sharp upsurges in income come from four areas: discovery and export of a natural resource, a price spike in international markets of a primary export commodity, foreign direct aid, and short term foreign direct investment. Often described by development economists as symptoms of "Dutch disease," large inflows of foreign currency place upward pressure on exchange rates and render traditional export sectors less competitive in international markets.<sup>386</sup> Inflow of money also increases domestic demand for goods and services and can produce a production shift away from export sectors to the domestic non-trading goods sectors. For Fund staff, the general consensus is that a shift in production away from traditional export sectors that "generate learning by doing" undermines a country's human capital potential and

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<sup>384</sup> See Ibrahim Elbadawi, Linda Kaltani, and Raimundo Soto "Aid, Real Exchange Rate Misalignment and Economic Performance in Sub-Saharan Africa," *World Development* 40: 4 (2012), pp.681-700. The authors highlight that in the three decades following the 1982 Debt crisis, the median African country maintained higher exchange rate values than other developing states.

<sup>385</sup> Howard Shatz and David Tarr, "Exchange Rate Overvaluation and Trade Protection: Lessons from Experience" World Bank Working Paper WPS 2289 (Washington, D.C.: World Bank, 2000), pp.6-7.

<sup>386</sup> Mwanza Nkusu, "Aid and Dutch Disease in Low Income Countries: Informed Diagnoses for Prudent Prognoses" IMF Working Paper WP/04/49 (Washington, D.C.: IMF, 2004), pp.3-8.

subsequently undermines long term growth and development. Some form of government intervention to devalue currency in the short term may be advisable to limit the effects of Dutch disease.<sup>387</sup>

While there is broad agreement among development economists on the negative impact of overvalued exchange rates, there is growing concern among Fund staff with strategies that move in the opposite direction and deliberately undervalue exchange rates. Most pertinent in current internal Fund debates around this issue are the contributions of Harvard economist Dani Rodrik. Rodrik, in a 2008 study focused on growth rates in developing countries from 1950-2004, presents evidence that growth rates were higher in developing states that deliberately undervalued their currency. Rodrik asserts that this is due to institutional factors and market failures unique to developing states that disproportionately impact traded goods sectors. Rather than the more difficult task of reforming markets and institutions that would invite investing in tradable sectors, devaluation serves as a “second best” policy for poor states. While the most prudent solution would be “deep” institutional and market reform, Rodrik concludes that a more practical course for poor states is to abandon the devaluation scheme and directly subsidize export sectors and allow exchange rates and wages to adjust to equilibrate the current account balance.<sup>388</sup>

Current Fund staff working with LICs are wary of strategies of devaluation or direct subsidies to export sectors. When asked about Rodrik’s conclusions, for example, a senior staff member in SPR responded as follows:

Fund advice to countries is, broadly speaking, to try and keep the real effective exchange rates aligned with fundamentals. There are two reasons why we would not advocate an

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<sup>387</sup>Christine Ebrahim-zadeh, “Dutch Disease: Too Much Wealth Managed Unwisely,” *Finance and Development* 40, no. 1 (2003), pp. 50-51.

<sup>388</sup> Dani Rodrik, “The Real Exchange Rate and Economic Growth: Theory and Evidence,” *Brookings Papers on Economic Activity* (Washington, D.C.: The Brookings Institute, Fall 2008), pp. 365-412.

active strategy of underevaluation: (1) the beggar-thy-neighbor problem (it is, after all one of the Fund's reason d'être to discourage such policies); and (2) attempts to sustain such a strategy for an extended period (which policy makers would be tempted to do) would give rise to other distortions-notably high /rising inflation-that would be harmful to growth.<sup>389</sup>

Exchange rate policy recommendations for LICs thus remain broadly in line with the Washington Consensus view developed three decades ago. While overvaluation is the major concern with developing states, under-valuation can also be detrimental to growth potential. Exchange rates should reflect underlying fundamentals and be competitive enough to promote export growth, but should not be deliberately undervalued due to subsequent inflationary pressure and underinvestment in domestic sectors.<sup>390</sup>

### *Trade controls*

As with exchange rate policy, contemporary thinking that shapes how Fund staff approach trade restrictions in LICs has roots in critiques of the ISI model that emerged in 1970s and 1980s. Among economists, the debate around the appropriateness of trade protectionism was challenged most forcibly by contributions of Anne Krueger, Jhagdish Bhagwadi, and T.N. Srinivasan. Krueger's seminal "The Political Economy of the Rent-Seeking Society" in *American Economics Review* modeled the adverse economic effects on growth that occur when actors compete for import licenses. Krueger argued that import licenses and other non-tariff trade restrictions create substantial economic rents due to the fact that they legally grant monopolistic control of market share to favored, politically connected actors. She highlighted that we should expect hard fought competition for these rents ("competitive rent seeking") that misallocate resources in the formal economy and incur a subsequent welfare cost *additional* to that caused by tariff restrictions alone. The high cost of winning market share via rents also incentivizes actors to turn to informal and/or illegal activities (e.g., bribery, smuggling, black

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<sup>389</sup> Author email interview of Fund staff member from Strategy, Policy, and Review Department, 29 June 2012.

<sup>390</sup> Andrew Berg and Yanliang Miao, "The Real Exchange Rate and Growth Revisited: The Washington Consensus Strikes Back," IMF Working Paper WP/10/58 (Washington, D.C.: IMF, 2010), p. 3.



markets) that can further undermine growth and development goals.<sup>391</sup> Bhagwati and Srinivasan generalized Krueger's argument to explore further how various market distortive policies create what the authors described as "Directly Unproductive, Profit-seeking" activities.<sup>392</sup>

The battle against rent-seeking was also tied to the concept of "efficiency prices." Efficiency prices are considered those that result in profit maximization per unit of input use and are deemed to exist under conditions where domestic markets are able to freely interact with international markets. State intervention into markets undermines appropriate prices and subsequent efficient allocation of resources.<sup>393</sup> Trade liberalization for poor states was thus considered the primary tool to counter distortive effects and spur growth and development<sup>394</sup> and was heavily integrated into the rationale for IMF (and World Bank) structural adjustment lending in the 1980s and 1990s.<sup>395</sup> Krueger, who went on to serve as the World Bank's Chief Economist (1982-1986), First Managing Deputy Director of the IMF (2001-2003; 2005-2006), and interim Managing Director of the IMF in 2004, reflected on this "radical" shift toward a free trade model in her 1997 presidential address to the American Economic Association:

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<sup>391</sup> Anne O. Krueger, "The Political Economy of the Rent-Seeking Society," *American Economic Review* 64, no. 3 (1974), pp.291-323. Monopolies and their opportunity costs on welfare outcomes were initially modeled by Gordon Tullock (Gordon Tullock, "The Welfare Costs of Tariffs, Monopolies, and Theft," *Western Economic Journal* 5, no. 3 (1967), pp.224-232). Krueger, however, was the first to coin the term "rent seeking."

<sup>392</sup> Jagdish Bhagwati and T.N Srinivasan, "Revenue Seeking: A Generalization of the Theory of Tariffs," *Journal of Political Economy* 88, no. 6 (1980), pp.1069-1087.

<sup>393</sup> David, *The IMF Policy Paradigm*, p.64.

<sup>394</sup> For a sample of the economic literature supportive of this position in the 1990s, see David Dollar, "Outward-Oriented Developing Economies Really Do Grow More Rapidly: Evidence from 95 LDCs, 1976-85," *Economic Development and Cultural Change* 40, no. 3 (1992), pp.523-544; Jeffery Sachs and Andrew Warner, "Economic Reform and the Process of Global Integration," *Brookings Papers on Economic Activity* (Washington, D.C.: The Brookings Institute, 1995), pp. 1-118; Sebastian Edwards, "Trade Orientation, Distortions, and Growth in Developing Countries," *Journal of Development Economics* 39, no. 1 (1992), pp.31-57; and Jeffrey Frankel and David Romer, "Does Trade Cause Growth?," *American Economic Review* 89, no. 3 (1999), pp.379-399.

<sup>395</sup> See IEO, *IMF Involvement in International Trade Issues* (Washington, D.C.: IMF, 2009), p.9. The average number of trade policy conditions per arrangement peaked in 1998 at 2.3 and fell steadily after 2000. The average number of conditions dropped below one in 2002 and below half by 2007.

Ideas with regard to trade policy and economic development are among those that have changed radically. Then and now, it was recognized that trade policy was central to overall policies of economic development. But in the early days, there was a broad consensus that trade policy for development should be based on “import substitution”...The contrast with views today is striking. It is now widely accepted that growth prospects for developing countries are greatly enhanced through an outer-oriented trade regime and fairly uniform incentives for production across exporting and import-competing goods...It is generally believed that import substitution as a minimum outlived its usefulness and that liberalization of trade and payments is crucial for both industrialization and economic development...And, while there are still some disagreements over particular aspects of trade policy both among academic researchers and policy makers, the current consensus represents a distinct advance over the old one, in terms both of knowledge and of the prospects it offers for rapid economic growth.<sup>396</sup>

IMF publications, policy documents, and interviews with staff suggest the “consensus” described by Krueger remains firmly ingrained in the institution’s thinking. A 2009 IEO report focused on IMF involvement in trade issues from 1995-2007, for example, observed that “... the IMF’s position on trade policy reflected a rather broad consensus in the academic and public policy literature on the merits of liberal trade regimes.”<sup>397</sup> The same report notes that Fund staff draw from arguments in the literature that protectionist measures as representative of “second best approaches” to market failures are often unrelated to trade. Rather than support the second best solution, Fund policies should instead target correction (“first best solutions”) of the market failure itself.<sup>398</sup> This same ideological support of free trade is found in Fund policy debates following the 2008 crisis. A 2010 article in *Finance and Development* authored by two economists from SPR outlines current trends in protectionism since the crisis and highlights three areas that the Fund should address to support free trade in the near future: (1) enhanced monitoring of trade policy that supports discriminatory policies; (2) guard against

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<sup>396</sup> Anne O. Krueger, “Trade Policy and Economic Development: How We Learn,” *American Economic Review* 87, no.1 (1997), pp.1-22 at pp. 1-2.

<sup>397</sup> IEO, *IMF Involvement in International Trade Issues*, p.8.

<sup>398</sup> *Ibid.*

“murky” protectionist policies (e.g., public procurement, product standards, and custom procedures) and (3) support effort to conclude the current stalled WTO Doha Round.<sup>399</sup>

Specific to staff working with LICs, Fund position papers on how best poor states can maintain growth and development in post-2008 crisis environment draw heavily from an argument focused on the merits of free trade:

Trade is an engine of development and can contribute strongly to reducing poverty...Perhaps the most important step that the international community can take to support LDCs- and, indeed, of all LICs-is to conclude the WTO Doha Round...To benefit strongly from better trade opportunities, the LDCs would need to tackle aggressively their own high tariff and nontariff barriers to trade...On tariffs, a reasonable goal within a few years is for a maximum 25 percent rate and a simple average below 15 percent. Nontariff barriers, such as non-critical road blocks and checkpoints, and overly burdensome custom practices, significantly slow trade and should be removed.<sup>400</sup>

The aforementioned 2009 IEO report does note that despite an ideological position strongly supportive of trade liberalization, the past two decades have witnessed a swing in the conditionality requirements in LIC lending arrangements that focus on trade liberalization. From the mid-1980s until 2000, the general trend was active and growing involvement in trade policy issues in SAF and ESAF programs. From 2000 forward, trade issues have been less central in Fund LIC lending arrangements. Reasons behind this shift are explored further in chapter 5.

### *Price Distortions*

Government intervention in market prices consists of two broad forms (see Figure 4.3 below). “Fixed” pricing includes setting producer prices, ceilings on consumer prices, freezing of wholesale and retail

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<sup>399</sup> Christern Hern and Brad McDonald, “Avoiding Protectionism,” *Finance and Development* 47:1 (2010), pp. 20-23 at p.23.

<sup>400</sup> IMF, *Reaching the MDGs. Macroeconomic Prospects and Challenges in Low-Income Countries* (Washington, D.C : IMF, 2010) pp. 15-16.

price margins, and commodity price support. “Input” pricing involves subsidies and use of taxes to discourage consumption of particular products.

Figure 4.3 Price Intervention Typology

<p><u>Fixed Pricing</u></p> <p>    Producer Prices</p> <p>    Consumer Prices</p> <p>    Price Margins</p> <p>    Commodity Prices</p>	<p><u>Common Features</u></p> <p>State purchases export at maximum prices and sells on international market at higher price.</p> <p>Retail price ceiling</p> <p>Wholesale/retail margins set by law.</p> <p>State purchases select commodities at guaranteed minimum</p>
<p><u>Input Pricing</u></p> <p>    Price Subsidies</p> <p>    Taxes/Disincentive Pricing</p>	<p>Subsidies used to support domestic production of commodities, support urban populations and/or encourage use of specific inputs</p> <p>Artificially inflated prices on inputs and/or outputs to discourage consumption</p>

(Source: David, *The IMF Policy Paradigm*, 1985, p.70.)

Most salient to LIC government intervention in market distortion are issues related to the agricultural sector. ISI inspired policies in the 1960s and 1970s heavily penalized agricultural sectors through various price interventions. Most common was the practice of fixing low producer prices to agricultural products. In this scenario, marketing boards of parastatal agencies with monopoly control purchased from agricultural producers at artificially low rates and then sold at open (world market) prices. Along with this “tax” on agricultural producers, price controls on basic foodstuffs were also a common practice during this period. For critics of this model, the narrative is that these policies ultimately produced a subsidization of urban elites at the expense of the rural and urban poor:

The general conclusion is that the rural and agricultural sectors have been taxed in favor of a relatively high-cost, high-wage, import substituting, and domestically oriented manufacturing sector. The overall result has been a squeezing of the poor and powerless, and a general nurturing of a domestic industrial and bureaucratic class earning excessive monopoly rents.<sup>401</sup>

Within this context, Fund and World Bank co-sponsored studies of price distortion in the agricultural sector are grounded in the following set of arguments. First, as seen under ISI inspired policy, government intervention into agricultural markets via export taxes, tariffs, or price subsidies worsens outcomes for the most vulnerable. Food protectionism increases domestic food prices, which impact poor consumers disproportionately as they spend more of their income on food than the well off. Government intervention into agricultural markets also does not help the rural poor who don't own farmland and have to pay higher food prices and those who do own land but don't produce for commercial markets.<sup>402</sup> Second, protectionism undermines innovation, supports inefficient processes, and diverts resources away from rural education, infrastructure development, and technical assistance.<sup>403</sup> Third, while protected agricultural markets might see short term price stability, the overall cost of market distortion is increased instability in prices in world markets. Both in the medium and long term, a better strategy is to liberalize agricultural markets.<sup>404</sup>

Along with concerns surrounding agricultural price distortions, the Fund's position has consistently argued against a broad range of subsidies used in LICs. Along with food subsidies described above, subsidies on energy use and transportation remain a prominent concern. A 2010 staff paper focused on

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<sup>401</sup> David, *The IMF Policy Paradigm*, p.76.

<sup>402</sup> Kym Anderson and William Masters, "Sub-Saharan and North Africa," in *Distortions to Agricultural Incentives: A Global Perspective, 1955-2007*, ed. Kym Anderson (Washington D.C.: The World Bank and Palgrave MacMillan (2009), pp. 323-357 at p.354.

<sup>403</sup> John Nash and Donald Mitchell, "How Freer Trade Can Help Feed the Poor: An Agenda for Easing Hunger Worldwide by Reducing Trade Protectionism," *Finance and Development* 42:, no.1 (2005), pp.37-37 at p.35.

<sup>404</sup> IMF and World Bank, "Market Access for Developing Country Exports-Selected Issues," 26 September 2002, p.33, available at <http://www.imf.org/external/np/pdr/ma/2002/eng/092602.pdf>.

the increase in energy subsidies in Africa since the 2008 crisis argues that while well intended, price subsidies are generally costly and inefficient in allocation and disproportionately benefit the wealthy.<sup>405</sup> The Fund's response to the global price spikes in agricultural and oil prices in 2007-8 provides further evidence into how strongly embedded norms wary of market distortive effects remain in the institution. Masood Ahmed, current Director of the Middle East and Central Asia Department and heavily involved in LIC policy is a lead spokesperson for the Fund's position on subsidies.<sup>406</sup> In a 2008 article in *Finance and Development*, Ahmed argued for targeted, short-term subsidies to help the poor rather than long-term state intervention as the most appropriate response to global price spikes. There is also a focus on "achieving market-led solutions in the longer run" rather than long term, untargeted subsidies that will undermine producers and contribute to inflationary pressure.<sup>407</sup>

The Fund's April 2011 regional outlook on Sub-Saharan Africa argued along similar lines. Food price controls should be avoided as they "exacerbate scarcity" and "amount to ad hoc taxation of those that produce, distribute retail items." The same goes for fuel subsidies. "Country studies show that fuel subsidies are almost invariably badly targeted" and as such tend to be "highly regressive" and "very costly fiscally" as they "encourage excessive consumption, and are difficult to phase out because of vested interests."<sup>408</sup> Several recent Fund loan agreements with LICs demonstrate that the Fund's normative position on subsidies is being heeded by member states. Mozambique, for example, reported that it will gradually phase out fuel subsidies in 2012 and replace food and transport subsidies

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<sup>405</sup> David Coady, Robert Gillingham, Rolando Ossowski, John Piotrowski, Shamsuddin Tareq, and Justin Tyson, "Petroleum Product Subsidies: Costly, Inequitable, and Rising," IMF Staff Position Note SPN/10/05, 25 February 2010, p. 12, available at <http://www.imf.org/external/pubs/ft/spn/2010/spn1005.pdf>.

<sup>406</sup> Ahmed was mainly responsible for creating the PRSP framework at the World Bank and was hired by the IMF in 2000. In an interview with Antje Vetterlein in 2004, Ahmed expressed that he was responsible for persuading the Executive Board to change the name of the ESAF to PRGF. Ahmed served as Deputy Director of SPR from 2000-2003.

<sup>407</sup> Masood Ahmed, "The Next Frontier: Low-Income Countries Gain Ground in a Globalized World but they Face Major Challenges," *Finance and Development* 45:, no.3, pp.9-14 at pp.10-11.

<sup>408</sup> IMF, *Regional Economic Outlook: Sub-Saharan Africa, Recovery and New Risks* (IMF, Washington, D.C., 2011), p.17, available at <http://www.imf.org/external/pubs/ft/reo/2011/afr/eng/sreo0411.pdf>.

with more “targeted schemes,” including a voucher scheme covering low income workers, students, and the elderly.<sup>409</sup> Senegal followed a similar model in 2008 as it eliminated subsidies on food staples, vegetable oil, and butane gas.<sup>410</sup>

Evidence thus points to a highly stable norm of free market thinking in the Fund that emphasizes the distortive effects of rent seeking. This notion has expressed itself consistently as seen in LIC policy directives on exchange rates, trade, and subsidies since the demise of ISI in the early 1980s. This is best captured by a senior staff member in the Research Department who argued that the Fund “has remained fairly Washington Consensus oriented all the way through” his three decade tenure.<sup>411</sup>

## Conclusions

*H1: Policy reform initiatives that draw from ideas and norms that question market-based solutions for LICs is unexpected.*

*H2 : A crisis of legitimacy that challenges taken for granted macroeconomic and development ideas and/or norms is necessary for substantive LIC policy change.*

*H3: Chances of LIC policy change are greatest when economic ideas or norms institutionalized within the Fund are questioned by broader epistemic community of development economists.*

Returning to the hypotheses above, I draw the following conclusions. First, despite policy shifts catalyzed in part by the Asian crisis of the late 1990s and the 2008 financial crisis, LIC reform measures have remained within the boundaries of paradigmatic conceptions of market based development established and reinforced for over five decades in mainstream economics. Second, while LIC policy since the late 1990s promotes limited state intervention and “pro-poor” policies, these

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<sup>409</sup> IMF, “Republic of Mozambique: Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding,” 20 May 2011, p. 7, available at <http://www.imf.org/external/np/loi/2011/moz/052011.pdf>.

<sup>410</sup> IMF, “Senegal: Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding,” 22 June 2012, p.7, available at <http://www.imf.org/external/np/loi/2012/sen/062212.pdf>.

<sup>411</sup> Author interview with senior staff member of Research Department, Washington D.C., 11 June 2011.

directives are conceptualized and enacted through a script that diverges little from a framework wary of market distortive protectionist and redistributive policy directives. This sentiment is best captured by a staff member from the African Department, who describes the PRSPs as follows:

Policies have become more generous, but the basic principles have not changed... When you boil it down, the core targets were there in 1986 and they are still there today. The core quantitative conditionality requirements have not changed. Think of it as a new cereal package. Clearly it looks different on the outside, and there is a bit of difference in what is inside, but it is still cereal.<sup>412</sup>

In this sense, it is easy for Fund critics to argue that little has changed in the institution and among its social constituencies of legitimation in the post-Washington Consensus era.

Analysis derived from constructivist process tracing of ideas, however, points to a more complicated story. While monetarist, new classical, and New Keynesian arguments wary of market distortive policy choices remain firmly entrenched in LIC lending arrangements, a shift in thinking has occurred in monetary and fiscal policy debates. As seen with the response by Strauss-Kahn and Blanchard to the 2008 crisis, policy elites can reach a tipping point where they fundamentally question components of past policy direction and show willingness for self-critique and reform. Evidence thus points to the economics profession and Fund management and staff as entities that seek legitimacy in their policy choices. Specific to LIC policy, rejection of the New Consensus framework of monetary and fiscal policy popular from 1982 to 2008 has been replaced by more Keynesian ideas supportive of activist, countercyclical response. Returning to the model of norm cycle presented by Park and Vetterlein, the notion of activist and countercyclical monetary and fiscal policy has achieved stability within the Fund. We can expect future LIC policy initiatives in the short and medium term to include traditional Keynesian macroeconomic themes.

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<sup>412</sup> Author interview of Fund staff member from Africa Department, Washington D.C., 21 September, 2011.



This chapter also highlights that more precise insight into current Fund reform is best achieved by conceptually treating themes of monetary and fiscal policy to stabilize short term balance of payment disequilibria as separate at some level from policies choices focused on structural reform and market efficiency. Evidence from this chapter demonstrates that we can expect more flexibility and change with the former as most policy choices along the spectrum of Keynesianism to monetarism still falls within broad paradigmatic themes of mainstream development economics. Alternative development proposals for LICs that challenge consensus around what is deemed market distortive should not be expected unless broader and deeper challenges or crisis in capitalism occur that subsequently challenge deep held beliefs in market efficiency. I address some of these concerns in chapter 5 through introduction of critical, historical structural engagement with IMF LIC policy reform.

## **Chapter 5 Inclusive Neoliberalism: Historical Structural Explanations of LIC Reform**

Mainstream theoretical approaches applied to the study of LIC policy in the post Washington Consensus period provide several new insights into what drives reform in this institution. From chapter 3, evidence derived through the use of PA models suggests that while the actors may change, a coalition consisting of at least one primary actor is necessary for policy reform. From chapter 4, constructivist analysis focused on the role of economic ideas and norm shifts and their relationship to contemporary IMF LIC policy reform highlights that Fund thinking and subsequent policy reform is influenced by external crises and policy failures. However, some ideas that frame policy choices are more sacrosanct than others. While conceptions of what is considered appropriate monetary and fiscal response have shifted in the post Washington Consensus period and have facilitated LIC policy reform, ideational frameworks skeptical of market distortion remain firmly entrenched in IMF thinking.

In chapter 5, I shift gears from current mainstream theory and examine Fund LIC policy reform in the post Washington Consensus through the lens of a historical-structural framework developed initially by Robert W. Cox and adopted by several generations of neo-Gramscian IPE scholars. I first summarize how Cox differentiates what he describes as a “critical” approach from “problem-solving” studies of politics. I then outline the concept of historical structure and Gramscian concepts of hegemony, state-society complex, and historic bloc, and explore how a historical structural framework engages with the study of contemporary international politics. Specific to the IMF, I then apply Cox’s methodology to trace the historical structural foundations of the institution and how its role has changed in relationship to LICs and the broader world order in three distinct periods: the hegemonic era of Bretton Woods, the non-hegemonic Washington Consensus era of globalist supremacy, and the

current era characterized by attempts of the globalist bloc to reassert a consensual framework of inclusive neoliberalism. This provides the context to assess two primary hypotheses put forth by several neo-Gramscian scholars focused on post Washington Consensus reform. First, the social upheaval and crises born out of the Washington Consensus period threatened to undermine the legitimacy of market driven development. In order to facilitate long term support for IMF and World Bank policy, the Fund has become more sensitive to concerns of weak economic growth, poverty, and increased inequality in LICs. Second, given that the IMF is one component of a broader globalist bloc, neo-Gramscians maintain that post Washington Consensus IMF reforms are a by-product of progressive elements within the globalist bloc to (re)establish a hegemonic world order through a more inclusive form of globalizing capitalism.

### **Cox, Critical Theory, and Historical Structures**

Rationalist and constructivist frameworks employed in chapters 3 and 4 fall into what Cox categorizes as “problem-solving” theory. Problem-solving theory is designed to study and improve outcomes in a particular social and political order. Cox argues that problem-solving approaches “take the world as they find it” and analytically separates the entity under study from deeper power relations and social forces that perpetuate the order within which the phenomena under study are embedded.<sup>413</sup>

Ontologically, this lends itself to an atomistic understanding of the world. Human agents and their behavior are “reduced to their outward phenomenal aspects” and historic entities such as the IMF are conceptualized and studied as independent objects that exist ‘out there’ in a broadly stable (a “continuing present”) social and political order underwritten by general patterns or laws that can be

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<sup>413</sup> Cox, “Social Forces, States, and World Orders: Beyond International Relations Theory,” p.128

elucidated through positivist methodology.<sup>414</sup> Cox highlights two analytical strengths of political analysis rooted in problem-solving theory. It sets clear limits on the potential variables that impact the phenomena under study that allow for precise, targeted examination. Through invoking the *ceteris paribus* assumption, it is also able to identify patterns of causal effect between variables and tease out patterns that can be applied in a predictive capacity to a given social and political order.<sup>415</sup>

Critical theory differs in its understandings and approach in several key respects. It is an openly normative framework whose purpose is to systematically evaluate (“historicize”) power structures and institutional arrangements of an existing world order and analyze the possibilities of alternative futures and how they might come into effect. Given its focus on historical social process, it rejects an essentialist understanding of human nature and the notion that subsequent political and social arrangements (e.g., social relations of production, the state, institutions, and interstate system) have inherent or timeless qualities. Rather, society is conceptualized as consisting of reflexive human agents embedded in historically specific social structures and institutions that simultaneously shape – and are shaped – by their actions. Integral in this reflexivity of human agents is their individualized processes of interpreting the world. While individual human beings are interrelated to historically specific and coherent structural arrangement of ideas and institutions, this does not determine in a mechanical fashion their ways of thinking and acting. This tension between individual agency and

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<sup>414</sup> Cox, “On Thinking About Future World Order,” in *Approaches to World Order*, eds. Robert W Cox and Timothy J. Sinclair (Cambridge: Cambridge University Press, 1996) pp.60-84 at p.63.

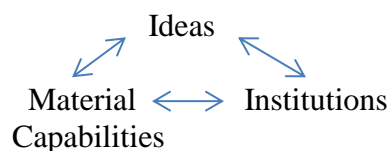
<sup>414</sup>Cox, “Social Forces, States, and World Orders: Beyond International Relations Theory,” p.129.

<sup>415</sup> *Ibid.*

broader structural intersubjective understandings thus serves as a primary source of historical change.<sup>416</sup>

While a dialectic, relational understanding of social structures and human action is inconsistent with positivist ontological and epistemological assumptions, a critical approach is not devoid of predictive capacity. Through systematic analysis of the social structures and power dynamics of a world order, a range of possible alternatives that might emerge are presented.<sup>417</sup> Cox describes this as “utopianism ... constrained by its comprehension of historical processes.”<sup>418</sup> Methodologically, this is accomplished through application of an ideal type that Cox terms a “historical structure.” A historical structure is a simplified representation of time-specific patterns of forces that frame in broad terms the “context of habits, pressures, expectations and constraints within which action takes place” within a given world order.<sup>419</sup> While these forces don’t determine agency and outcomes directly, they impose pressures and constraints: “Individuals and groups may move with the pressure or resist and oppose them, but they cannot ignore them.”<sup>420</sup> Three interrelated forces are identified that make up a historical structure. These include material capabilities, ideas, and institutions (see Figure 5.1 below).

Figure 5.1: Historical Structure



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<sup>416</sup> Robert W Cox, “On Thinking About Future World Order,” in *Approaches to World Order*, ed. Robert W Cox and Timothy J. Sinclair (Cambridge: Cambridge University Press, 1996) pp.60-84 at p.66.

<sup>417</sup> By “structure,” Cox refers to “the product of recurrent patterns of actions and expectations” in the human experience: “Structures exist in language, in the ways we think, in the practices of social and economic and political life. Any particular way of life in time and place, when analyzed will reveal a certain structure.” Cox, “Towards a Post-hegemonic Conceptualization of World Order: Reflections on the Relevancy of Ibn Khaldun,” p.149.

<sup>418</sup> Cox, “Social Forces, States, and World Orders: Beyond International Relations Theory,” p.130.

<sup>419</sup> Cox, *Production, Power and World Order*, p.4.

<sup>420</sup> Cox, “Social Forces, States, and World Orders: Beyond International Relations Theory,” p. 135.

Material capabilities describe power resources of a social order tied to level of technology, financial and military power, and organization capacity. Ideas are divided into two broad categories.

Intersubjective meanings are broad-based and historically derive shared understandings of the world.

Cox stresses the crucial dynamic by which intersubjective understandings take on an objective form that serves as the foundation of historical structures:

Historical structures express the unity of subjective and the objective. A nation, a class, a religion are not real physical objects, yet they give real form to the human situation. They are ideas shared in the subjectivity of innumerable individuals...In being so shared, these ideas constitute the social world of these same individuals. They attain objectivity in the structure that circumscribes human action. These structures are as much a part of the material existence of people as the food they eat and the clothes they wear.<sup>421</sup>

If intersubjective meanings form the objective foundation of historical structures, more contested and varied are “collective images of social order.” Perhaps best described as more openly ideological frameworks of thinking, these ideas engage with “both the nature and the legitimacy of prevailing power relations, the meaning of justice and public goods and so forth.”<sup>422</sup> Cox highlights that tensions found between rival ideologies or between ideologies that challenge broad-based intersubjective understandings can serve as flashpoints of change that may produce alternative material and institutional arrangements and subsequent shifts in the historical structure.<sup>423</sup>

Dynamics surrounding the interplay between ideas and power relations are introduced into the framework of historical structure through discussion of institutions and hegemony. Institutions are operationalized as expressions of ideational and material forces that subsequently reinforce prevailing power relations. Here, Cox adopts Antonio Gramsci’s conception of hegemony to capture the critical

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<sup>421</sup> Cox, *Production, Power and World Order*, p.395.

<sup>422</sup> Cox, “Social Forces, States, and World Orders: Beyond International Relations Theory,” p. 136.

<sup>423</sup> *Ibid.*

role that institutions play in perpetuating a historical structure.<sup>424</sup> Hegemony, as developed further below, is conceptualized as a form of domination where power relations primarily take on a consensual form and subsequently lower coercive aspects of rule.<sup>425</sup> Institutions such as the IMF can serve as critical vectors for the formation and reproduction of hegemony in several respects. First, as institutions are ostensibly designed to serve general interests rather than the interests of ruling groups, they increase the legitimacy of the status quo.<sup>426</sup> Institutions also reinforce the rule of powerful groups through framing how particular issues are understood and managed. This is particularly salient when potentially counter-hegemonic ideas challenge power structures, as institutions can absorb and reframe these ideas in a form that is consistent with hegemonic doctrine.<sup>427</sup> As is the case with material and ideational forces, institutions are not determined in any strict sense by ruling groups. They can “take on their own life” and facilitate opposing tendencies that challenge and transform historical structures and subsequent world orders.<sup>428</sup>

In sum, a critical approach applied to the study of international politics is interested in understanding how the contemporary world order has come to be, and what forces and dynamics potentially may

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<sup>424</sup> Gramsci, leader of the Italian Communist Party from 1921-1927, was imprisoned under Mussolini’s regime from 1929-1935. Cox and neo-Gramscians draw heavily from his writings. See Antonio Gramsci, *Selection from the Prison Notebooks of Antonio Gramsci* edited and translated by Quinton Hoare and Geoffrey Nowell Smith (New York: International Publishers, 1971).

<sup>425</sup> Gramsci, studying late 19<sup>th</sup> and early 20<sup>th</sup> century state form in Western capitalist societies, argued the political power of ruling classes was reinforced primarily through multiple institutions and relationships in civil society rather than on direct control and use of the coercive aspects of the state. Described as hegemony, this form of class rule occurs when consensual forms of power between dominant and subordinate groups, rather than overt or direct coercion of dominant over subordinate groups via the state, are primary. For further discussion of Gramscian conceptions of hegemony, see Walter Adamson, *Hegemony and Revolution: A Study of Antonio Gramsci’s Political and Cultural Theory* (Berkeley, California: University of California Press, 1980), pp.169-179; Cox, “Gramsci, Hegemony and International Relations: An Essay in Methods,” pp.162-168; Paul Thomas *Alien Politics: Marxist State Theory Retrieved* (New York: Routledge, 1994), pp.143-164.

<sup>426</sup> Cox, “Social Forces, States and World Orders: Beyond International Relations Theory,” pp.136-137.

<sup>427</sup> Here, Cox draws from Gramsci’s concept of *transformsimo* that roughly translates into processes of co-option of subaltern groups by those in power. See Cox, “Gramsci, Hegemony and International Relations: An Essay in Method,” pp. 166-167.

<sup>428</sup> Cox, “Social Forces, States and World Orders: Beyond International Relations Theory,” p.137.

transform it. The structural context of a world order is first established through identification of the time-specific interrelated material capabilities, ideas, and institutions that underwrite it. The next step is an application of a historical structural approach that involves clarification in regard to the stability of that order, and what possible amalgamation of contradictions and pressure points therein could lead to its transformation. Specific to the focus on the IMF, application of the historical structural approach will examine how Fund LIC reform in the post Washington Consensus period may be reflective of nascent attempts to rebuild global hegemony in the early 21<sup>st</sup> century around “inclusive neoliberalism.” Employment of Cox’s method first necessitates further clarification as to why a historical structural framework employs a social relational ontology of the state and power how this understanding is then applied to the study of the international system and multilateral institutions.

### **Social Relational Ontology of the State, Power, and Hegemony**

Mainstream problem-solving theories of international relations, including neorealism and neoliberal institutionalism, conceptualize a world system inhabited by states that are: (1) the origin and primary unit of political action; (2) sovereign, rational actors whose unchanging *modus operandi* is to maximize their security in an anarchical world system and; (3) unrelated in form and function to social forces, including those tied to productive processes.<sup>429</sup> Historical structural approaches instead argue for what they describe as a relational understanding of the state. States are not sovereign entities with preset and timeless qualities or the sole site of political activity. They are instead conceptualized as time-specific institutionalized expressions and points of linkage between global and local social forces.<sup>430</sup>

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<sup>429</sup>Cox, “Social Forces, States and World Orders: Beyond International Relations Theory,” pp.138-139; Rupert, “*Producing Hegemony: State/Society Relations and the Politics of Productivity in the United States*,” pp. 431.

<sup>430</sup> Cox, “Social Forces, States and World Orders: Beyond International Relations Theory,” p.141; Rupert, “*Producing Hegemony: State/Society Relations and the Politics of Productivity in the United States*,” pp. 432.



A social relational framing of the state is also inconsistent with mainstream realist and structural Marxist conceptions of state power, multilateral institutions, and hegemony in the international system. In both neorealism and world system theory, for example, state power is reduced to single dimension of dominance based on relative economic position and/or hard power capabilities.<sup>431</sup> For historical structural IR scholars, this approach fetishizes state power as it fails to elucidate social forces and dynamics that ultimately produce the conditions necessary for the state to act. Power instead should be “seen as *emerging* from social processes rather than taken as given in the form of accumulated material capabilities that is as the result of these processes.”<sup>432</sup> If power is derived from social processes, a relational framework also rejects the notion that power can be reduced or conceptually tied only to territorial entities such as the nation-state. Historical structural analysis therefore recognizes the global system as a totality within which power tied to social processes and forces operates at multiple sites of human activity within, above, and below the state.<sup>433</sup>

Cox, drawing from the tradition of historical materialism,<sup>434</sup> argues that a universal component that shapes historical structures includes social forces in the human experience tied to productive

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<sup>431</sup> Rupert, “*Producing Hegemony: State/Society Relations and the Politics of Productivity in the United States*,” pp. 428-430.

<sup>432</sup> Cox, “Social Forces, States and World Orders: Beyond International Relations Theory,” p.141.

<sup>433</sup> Stephen Gill, “Epistemology, Ontology, and the ‘Italian School,’” in *Gramsci, Historical Materialism and International Relations*, ed. Stephen Gill (Cambridge: Cambridge University Press, 1993) pp.21-48 at p.42.

<sup>434</sup> Cox differentiates between two major “currents” of Marxism: historical materialist and structural Marxism: “There is a Marxism that reasons historically and seeks to explain, as well as to promote, changes in social relations; there is also a Marxism... which turn its back on historical knowledge in favor of a more static and abstract conceptualization of the mode of production.” See Cox, “Social Forces, States, and World Orders: Beyond International Relations Theory,” p. 133. Critical IPE scholars including Rupert make similar distinctions between “economistic” forms of Marxism and “Western Marxism.” The former argues a self-contained economic sphere (base) determines human behavior and other “super-structural” factors. The later sees human agents as embedded in –but not determined by– historical structures that they ultimately may “reconstruct...to develop themselves and their social power, and thus to make their own history.” See Rupert, “*Producing Hegemony: State/Society Relations and the Politics of Productivity in the United States*,” p.431.

relations.<sup>435</sup> While an integral component of social structures, Cox and neo-Gramscians stress that productive relations should not be conceived in economistic terms: “Production...is to be understood in the broadest sense. It is not confined to the production of physical goods used or consumed. It covers the production and reproduction of knowledge and of the social relations, morals, and institutions that are the prerequisites of the production of physical goods.”<sup>436</sup> Nor do social forces engendered by productive processes determine in a unilinear direction political outcomes. Rather, Cox maintains that historical comparisons of different modes of social relations of production elucidate how new productive processes generate social forces and power relations and how these forces shape – and are shaped by – particular forms of state and world orders.<sup>437</sup>

Specific to forms of state and its relationship to social forces of production, I return to the relational ontology introduced above and develop further several components of Gramscian theory. Cox describes the state in terms of state-society complexes underwritten by historical blocs. A historic bloc describes the configuration of social forces that serves as the foundation of a particular state form. This is conceptualized in dialectical terms, where interacting and mutually constituted subjective (ideology, political organization, etc.) and objective elements (physical means of production) form a complex of social relations that is expressed in the form and function of the state.<sup>438</sup> By state-society complex, Cox draws from Gramsci’s analysis of the Western capitalist state as constituted by both a coercive

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<sup>435</sup> “Production creates the material basis for all forms of social existence, and the ways in which human efforts are combined in productive processes affect all other aspects of social life, including the polity.” Cox, *Production, Power, and World Order*, p.1.

<sup>436</sup> Robert W. Cox “Production, the State, and Change in World Order,” in *Global Changes and Theoretical Challenges: Approaches to World Politics for the 1990s*, ed. Ernst-Otto Czempiel and James Rosenau (Toronto: Lexington Books, 1989), p. 39 as cited in Andreas Bieler and Adam David Morton, “A Critical Theory Route to Hegemony, World Order, and Historical Change,” *Capital & Class* 82 (2004), pp. 85-113 at p. 89.

<sup>437</sup> Cox, “Social Forces, States and World Orders: Beyond International Relations Theory,” pp.138-139.

<sup>438</sup> Rupert describes an historic bloc as follows: “In understanding Gramsci, it is essential to grasp that a historic bloc is more than a simple alliance of classes or class factions: it encompasses both objective and subjective aspects of a particular social formation uniting in historically specific ways political, cultural, and economic factors into a complex, politically contestable, and dynamic ensemble of social relations.” See Rupert, “Producing Hegemony: State/Society Relations and the Politics of Productivity in the United States,” p.433.

apparatus of government and a highly developed private sphere of civil society (“extended state”) critical to the formation and reproduction of historic blocs and hegemony.<sup>439</sup>

In this context, civil society has within it multiple sites (education, the media, religious institutions, etc.) where ideological frames of common culture are formed that produce a base level of cohesion and stability among the multiple and often contradictory elements of a historic bloc. Intellectuals tied to the dominant class (“organic intellectuals”) also play a prominent role in the production of hegemony in civil society as they “perform the function of developing and sustaining the mental images, technologies, and organizations that bind together the members of a class and of a historic bloc into a common identity.”<sup>440</sup> Under conditions of hegemony, we can expect that ideology, power relations, and prominent institutions are not perceived as representing the interests of a particular class and as such promote “buy in” from subordinate groups. This dynamic will serve to reproduce cohesive rule and reduce challenges that undermine structures of power and interests of the leading class.<sup>441</sup>

If hegemony is established at the national level, Cox contends that this can also expand and operate upward and outward to the global level. Based on analysis of the past two centuries, this involves several components: (1) an emergence of a preeminent state power and its historic bloc that facilitates the expansion of a new social relations of production and the interests of its leading class on a world scale; (2) construction of a world order that is universal in conception and; (3) opportunities for hegemony to operate in globally formed expressions of civil society that support the dominant mode of

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<sup>439</sup> Gramsci defines the state follows: “For it should be noted that the general notion of state includes elements which need to be referred back to the notion of civil society (in the sense that one might say that state=political society + civil society, in other words hegemony protected by the armor of coercion).” See Gramsci, *Selections from the Prison Notebooks*, pp.262-263.

<sup>440</sup> Cox, “Gramsci, Hegemony, and International Relations: An Essay in Methods,” p.168.

<sup>441</sup> *Ibid.*

production and historic bloc.<sup>442</sup> As summarized by Cox, world hegemony is best conceptualized as “a social structure, an economic structure, and a political structure....expressed in universal norms, institutions and mechanisms which lay down general rules of behavior for states and for those forces in civil society that act across national boundaries-rules that support the dominant mode of production.”<sup>443</sup>

While hegemonic periods lower coercive rule and increase stability, they are never uncontested or permanent in character. Shifts in productive relations and subsequent state-society complexes, a breakdown of class coalition formation in a historic bloc, or counter-hegemonic social and political movements can undermine hegemony in historical structures. Non-hegemonic world orders are characterized by a lack of ideological cohesiveness, increased conflict, and more overt use of coercive force by powerful entities. In the capitalist era, Cox identifies the “era of rival imperialisms” (1873-1945) and the current period of globalization (1965-present) as non-hegemonic in character. This stands in contrast to the hegemonic world orders of mid-19<sup>th</sup> century *pax Britannica* and the post-WW II US led Bretton Woods era (1945-1965).<sup>444</sup>

### **Tracing the Historical Structural Foundations of the IMF**

Application of the historical structure method to the study of post Washington Consensus IMF reform involves historical comparisons of power relations and social structures that led to the formation of the institution in 1945 and how the nature of these forces and the Fund have changed over time. In this section, I first summarize prominent dynamics of the 19<sup>th</sup> century *pax Britannica* and the subsequent era of “rival imperialisms” to establish context for the formation of the IMF and roles it played in the

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<sup>442</sup> *Ibid.*, p.171.

<sup>443</sup> *Ibid.*, p.172.

<sup>444</sup> *Ibid.*, pp.170-171.

reproduction of post-World War II historical structures. Specific attention is focused on the rise of a Fordist historic bloc in the United States during the first half of the 20<sup>th</sup> century and how this development provided the foundation for the post-World War II hegemonic era of *pax Americana* supported by multilateral institutions, including the IMF. This provides the necessary context and a comparative anchor to evaluate current hypotheses that IMF LIC reforms in the post-Washington Consensus signal a broader attempt by a dominant transnational historic bloc to rebuild global hegemony around an inclusive neoliberal model.

Cox's point of departure in his study of modern world orders focuses on the first industrial revolution and the emergence of capitalist social relations in Great Britain in the late 18<sup>th</sup> century and early 19<sup>th</sup> century. With the rise of capitalist social relations in Britain, the ascendant bourgeoisie successfully used state power to replace feudal and mercantilist practices (e.g., protectionist measures, guild mandated regulation of production, state granted monopolies and corporations) with laws that promoted conditions for free markets. By the mid-19<sup>th</sup> century, the formation of a hegemonic historic bloc and liberal state form in Britain served as the foundation for an outward expansion and expression of liberal hegemony at the global level.<sup>445</sup> The liberal hegemonic world order of *pax Britannica* was supplanted by a non-hegemonic and conflictual period described by Cox as the "era of rival imperialisms" (1875-1945). Challenges to British power from the rise of Germany and the United States in later half of the 19<sup>th</sup> century and sustained periods of economic crises across Europe and North America from the 1870s to the outbreak of World War I catalyzed competitive imperial

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<sup>445</sup> The elimination of the protectionist Corn Laws in 1846 is given as the historical point of reference for the consolidation of a bourgeois led hegemony. Cox argues an essential component of the historic bloc that produced the hegemonic liberal state was the division of roles between a weakened aristocratic class and the ascendant bourgeoisie. Following the repeal of the Corn Laws, an aristocratic governing class maintained the role of running the state, but now did so in accordance with liberal market principles. It also made limited and targeted concessions to working class demands that facilitated hegemonic rule. These included the Factory Act of 1847 that limited the workday of women and children to ten hours. See Cox, *Production, Power, and World Order*, pp.131-138.

expansion across Africa and Asia. The political and economic fallout of World War I undermined any remaining vestiges of the liberal global economy of the mid-19<sup>th</sup> century. Following multiple attempts to revise the international gold standard in the 1920s, the project was abandoned in 1931. Competitive “beggar they neighbor” currency devaluations to correct balance of payment deficits and stimulate demand combined with a sharp rise of protectionism spurred by the U.S. Smoot-Hawley Tariff of 1930 soon followed. Protectionism and the effects of the Great Depression produced severe drops in global trade and economic outputs that further reinforced the international turmoil and competition leading up to WW II.

A shift away from liberal hegemony and the liberal state form also coincided with radical shifts in productive relations in the late 19<sup>th</sup> and early 20<sup>th</sup> century. The replacement of small-scale capitalism with assembly line factory models of production transformed the nature of work, social relations, and historical structures. Most notable in this respect was the emergence of scientific management (“Taylorism”) of mass-based industrial production initially developed in the United States in late 19<sup>th</sup> century. In this model, the pacing and control of production was removed from skilled workers and replaced with an assembly line model of fragmented, highly specialized tasks performed by low skilled labor.<sup>446</sup> The introduction and eventual consolidation of mass-based production and consumption was underwritten by new social structures, ideology, and practices initially described by Gramsci as “Fordism.”<sup>447</sup>

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<sup>446</sup>On Taylorism, see Rupert, *Producing Hegemony: The Politics of Mass Production and American Global Power*, pp.59-67 and Cox, *Production, Power, and World Order*, p.160.

<sup>447</sup> Gramsci is credited for coining the term “Fordism” in his chapter on “Americanism and Fordism.” See Gramsci, *Selections from the Prison Notebooks*, pp. 279-318.

Gramsci maintained that this production regime was successfully implemented and reproduced in the United States through a combination of coercive and persuasive tactics.<sup>448</sup> Leading industrialists of the early 20<sup>th</sup> century including Henry Ford, for example, employed direct coercive means to undermine unionization yet paid high wages, offered company-based pensions and insurance, and supported an expansion of the state's role in protecting worker well-being.<sup>449</sup> Rupert, in his study of early 20<sup>th</sup> century U.S. state-society relations, also highlights the critical ideological and cultural dimensions that helped create and sustain Fordism. These included a reframing of "the American way" as consistent with the values of employer-employee partnership, industrial and labor efficiency,<sup>450</sup> and mass consumption.<sup>451</sup> Moreover, a focus on maximizing productivity was framed in universalistic terms. Moving beyond just the American reality, all of humankind was to benefit from the productivity and prosperity of the U.S. capitalist model.<sup>452</sup>

Despite such lofty aspirations, the implementation and reproduction of Fordism was not without significant struggle. Through multiple waves of confrontation between a growing trade union movement and powerful American industrialists in the 1920s and 1930s, Fordism evolved to include a critical dynamic of class compromise expressed in the policies and ideology of FDR's New Deal.<sup>453</sup>

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<sup>448</sup> *Ibid.*, pp. 295-297.

<sup>449</sup> For an in depth account of Ford's tactics of coercion and persuasion see Rupert, *Producing Hegemony: The Politics of Mass Production and American Global Power*, pp. 110-138.

<sup>450</sup> The Ford Motor Corporation, for example, established a "Sociological Department" to monitor employees' home lives and set standards of behavior necessary to qualify for maximum pay. This included a focus on sobriety and monogamy. *Ibid.*, pp. 124-126.

<sup>451</sup> Rupert quotes directly from Henry Ford to articulate this point: "...The owner, the employees and the buying public are all one and the same...It is the thought of enlarging buying power by paying high wages and selling at low prices which is behind the prosperity of this country." *Ibid.*, p.65.

<sup>452</sup> *Ibid.*

<sup>453</sup> As documented by Rupert, industrialists successfully cracked down on organized labor following World War I, often with the direct compliance and aid of state power. While the industrial union movement was largely impotent in the 1920s, the crisis of the Great Depression and the 1933 National Industrial Recovery Act and National Labor Relations Act of 1935 sparked unionization and militant strike activity that would last through World War II. Most prominent in leading industrial unionization was the Committee for Industrial Organization (CIO) formed in 1935. The CIO won collective bargaining rights at General Motors (1937), Chrysler (1937), the US Steel Corporation (1937), and Ford (1941). *Ibid.*, pp. 91-95.

Here, a welfare state committed to full employment policies was complemented by moderate unionism supportive in principal to capitalism and loyal to the U.S. government and its policy objectives.<sup>454</sup> As discussed further below, the formation of this hegemonic historic bloc and the productive forces unleashed by Fordism was an integral component of the post-World War II world order of *pax Americana* managed in part by the IMF.

The social relations and state forms born from the assembly line factory model manifested itself differently in Europe than the United States with important ramifications for the trajectory of post-World War II historical structures and multilateralism. The highly productive model that emerged in the United States was not hampered by what Gramsci described as the historical hangover of “parasitic” classes and social forces in Europe.<sup>455</sup> While European industrialists attempted to emulate U.S. factory methods, pushback from powerful non-productive classes undermined full implementation of Taylorism. This shaped state/society relations in two major areas. First, states in Europe became more active intermediaries in the industrialization process as they attempted to balance the interests of large scale industrial capital supportive of “scientific” production methods and reinter classes who stood in opposition. Lower productivity and powerful non-productive classes in Europe also undermined attempts to reproduce the high wage, mass consumption strategy of Fordism that helped moderate the American union movement. Managing the class antagonisms and demands of industrialists, non-productive classes, and a radicalized workers movement in Europe, was manifested in what Cox describes as a corporatist “welfare-nationalist” state form. Invoking nationalist and

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<sup>454</sup> *Ibid.*, pp.150-160.

<sup>455</sup> Gramsci describes different class structures in the US and Europe in the early 20<sup>th</sup> century as follows: In America, “...there do not exist numerous classes with no essential function in the world of production, in other words classes which are purely parasitic. European “tradition”, European “civilization”, is conversely, characterized precisely by the existence of such classes, created by the “richness” and “complexity” of past history.” Gramsci, *Selections from the Prison Notebooks*, p. 281.



militaristic sentiment, these state forms championed protectionism, selectively integrated demands of capital through government managed industrialization, and undermined more radical elements of labor through expansion of welfare provisions. This state form was reinforced by World War I and World War II as governments played an integral role in planning and implementing national strategies of industrial production for war efforts. This translated into strong support of tripartite corporatist models involving government-business-labor coalitions.<sup>456</sup>

### **The IMF as a Mechanism of Hegemony in the Bretton Woods era**

The outward expression of U.S. based Fordist hegemony to an international scale represented the major force that reshaped the post-World War II global order. In this section, I outline the major dynamics of this process with emphasis on the relationship between an ascendant internationalist-Fordist historic bloc, the transformation of the nationalist welfare state to a liberal-Keynesian state form,<sup>457</sup> and how the formation and early IMF played a central role in these efforts. Building on this foundation, I then discuss how neo-Gramscians focused on the Fund theorize its modern role in a contemporary non-hegemonic world order characterized by a transnational restructuring of capitalism, the formation of a globalist historic bloc, and the emergence of the transnational state form.

Neo-Gramscian interpretations of *pax Americana* maintain that this hegemonic world order had its roots in the restructuring of U.S. state-society relations during the Depression years around the Fordist

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<sup>456</sup> Cox, *Production, Power, and World Order*, pp.181-189.

<sup>457</sup> Cox highlights that the state form that predominated during *pax Americana* represented in broad terms compromise and tension between elites focused on liberalizing capitalism and working class support of Keynesian welfare state policies. He describes this state form as “neoliberal.” To avoid confusion with the commonly understood use of the term, I instead use “liberal-Keynesian.”

“politics of productivity.”<sup>458</sup> Here, the New Deal consensus that emerged in the interwar years and World War II was reinforced by a broad-based belief that American industrial capitalism, stripped of its most abusive characteristic by a moderate labor movement, had proven superior in productive capacity both to totalitarian models (e.g., fascism, communism) and capitalist European states. High growth rates through capital-labor consensus, in turn, had produced the social stability and conditions in the U.S. for liberal democracy and individual freedom to flourish.<sup>459</sup> This understanding thus equated problems in politics with inefficiencies in production that could be overcome by conditions that maximized economic growth.<sup>460</sup> The formation of interclass coalitions focused on growth, rather than a focus on redistribution or restructuring of social productive relations through class-based political action, thus became a central tenet for those championing the American capitalist model. As with the formation of Fordist hegemony in the U.S. in the interwar period, the internationalization of Fordism also was articulated as serving a higher universal purpose. As noted by Stephen Gill, its “ideological banners included the concepts of liberty, modernity, affluence, welfare and the ‘end of ideology,’ fused into a concept of ‘the West’ and an anti-communist alliance.”<sup>461</sup>

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<sup>458</sup> A cross section of neo-Gramscian interpretations of the post-World War II era roots their analyses in Rupert’s study of the relationship between U.S. Fordism in the interwar years and the formation of *pax Americana*. Rupert, in developing his argument, draws in part from historians Charles Maier and Michael Hogan when discussing the restructuring of European capitalist states after World War II. See Rupert, *Producing Hegemony: The Politics of Mass Production and American Global Power*, pp.42-53 ; Charles S Maier, “The Politics of Productivity,” in his *In Search of Stability: Explorations in Historical Political Economy* (Cambridge: Cambridge University Press, 1987), pp. 121-152 and Michael Hogan, *The Marshall Plan* (Cambridge: Cambridge University Press, 1987).

<sup>459</sup> Rupert highlights how this rationale was used by American industrial union leadership as it clamped down and/or purged ‘radical’ union members in the late 1940s and early 1950s: “Liberal capitalism was preferable to communism insofar as it allowed “free trade unions” to petition capitalists for redress of grievances, and thus to control abuse. These abuses were not construed as intrinsic to liberal capitalism, but were implied to be the product of idiosyncratic conditions and authoritarian employers...Communism, on the other hand, was inherently flawed and irredeemably opposed to the interests of Americans and workers.” Rupert, *Producing Hegemony: The Politics of Mass Production and American Global Power*, p. 157.

<sup>460</sup> Maier, “The Politics of Productivity,” p.23 as cited by Rupert, *Producing Hegemony: The Politics of Mass Production and American Global Power*, p.44.

<sup>461</sup> Stephen Gill, *Power and Resistance in the New World Order*, pp.58-59.

For the U.S., reconstruction of the post-World War II order along peaceful, prosperous, and non-communist lines thus required at baseline a commitment from its allies to maximize economic productivity and growth through adoption of the Fordist model. An additional critical dynamic that emerged in the U.S. in the interwar period and World War II was the ascendance of an international Fordist historic bloc. This coalition of liberal minded government officials, internationally oriented industrialists and financiers, and the leadership of major industrial unions found common ground in the notion that productivity and subsequent American interests were undermined by the wide-spread protectionism of the interwar years.<sup>462</sup> For this historical bloc, a post-World War II order could only serve American and universal interests if Fordism was combined with an open global economy.

The state form created in the reconstruction of capitalist Europe through the Marshall Plan reflected the vision of the international-Fordist historic bloc. This included the adoption of American business and labor management practices, support and integration of a moderate union movement and centrist political parties, and a commitment to free trade through participation in the nascent Organization for European Economic Cooperation.<sup>463</sup> As highlighted by Cox, the state form that emerged in the late 1940s in capitalist societies also had to manage three established components of the welfare-nationalist state from the previous era at odds with liberal economic ideology. First, states were now active managers of the economy through corporatist arrangements and Keynesian demand management. Second, states selectively intervened to protect vulnerable social groups from market forces. And third, as a component of a half century of state economic management, capital investment was

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<sup>462</sup> Rupert identifies the three major groups making up the neoliberal historic bloc as follows: “(1) Wilsonian liberals, especially in the State Department (2) those fractions of capitalist class which were internationally oriented, especially major banks and technologically advanced corporations engaged in mass production, and (3) the official leadership (and to some extent the mainstream membership) of organized labor in America.” See Rupert, *Producing Hegemony: The Politics of Mass Production and American Global Power*, p.57.

<sup>463</sup> For an overview of how the Marshall Plan was used to restructure European state-society relations along liberal capitalist lines, see Cox, *Production, Power and World Order*, pp. 214-217 and Rupert, *Producing Hegemony: The Politics of Mass Production and American Global Power*, pp.52-53.

concentrated in a powerful oligopolistic sector more open to world markets that coexisted with domestically oriented and smaller competitive sectors of small businesses and the state sector.<sup>464</sup>

With the support of the oligopolistic sector, capitalist states passed laws and supported the creation of institutions including the IMF to facilitate integration into an open world economy. However, these states also had to balance the demands of domestic groups who often were the short term losers in the transition away from more generous welfare state policies and protectionism. This tension manifested itself in the dynamic of “embedded liberalism” discussed in Chapter 2. Transitional and selective exceptions to liberalization were granted to cushion particular domestic sectors while the national economies as a whole were restructured to integrate into an open world market.<sup>465</sup>

It is within this context of the internationalization of Fordism, the rise of an international Fordist historic bloc, and the emergence of a post WW II liberal-Keynesian welfare state form that historical structuralists analyze the early IMF. As outlined in chapter 2, the Fund had clear policy objectives when formed in 1945. It promoted global trade stability and liberalization through the implementation and management of a flexible gold standard and provision of conditional short term lending for states with balance of payments deficits.<sup>466</sup> Historical structural understandings of the IMF add several more layers to this analysis. The IMF at its inception reflected in large part the interests and belief system of the U.S. led international historic bloc. This bloc stood increasingly at odds with more left leaning proponents of Keynesian state capitalist models that prioritized full employment policies and protectionism over open market policies.<sup>467</sup> Member states with balance of payment deficits that

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<sup>464</sup> Cox, *Production, Power, and World Order*, p.220.

<sup>465</sup> *Ibid.*

<sup>466</sup> As discussed in chapter 2, a fixed exchange rate and independent monetary and fiscal policy requires a commitment to capital controls.

<sup>467</sup> Keynes, as chief negotiator for Britain at Bretton Woods, attempted to reconcile these differences through his proposed International Clearing Union (ICU). Under the ICU plan, states with balance of payments surpluses or deficits would be

borrowed from the IMF, for instance, were disincentivized from pursuing full employment policies due to loan conditionality that prioritized currency stability and a return to payments equilibrium.

Fund policy concurrently reflected the tensions found in emerging liberal-Keynesian welfare state forms between forces that lobbied for a maximization of liberalization and the historical hangover of class compromise forged in the interwar years. While the IMF prioritized a commitment to balance of payment equilibrium over full employment, its conditional lending program allowed for a softer landing of internal adjustment than was seen during the 19<sup>th</sup> century classic gold standard.<sup>468</sup> In addition, the IMF's support of capital controls during the Bretton Woods era allowed individual states to pursue independent monetary and fiscal policy decisions. This gave national politicians room to appease domestic constituents who had grown accustomed to the full-employment policies of the interwar years. During *pax Americana*, the Fund also did not push industrialized states to abandon corporatist arrangements or mixed market economies. These policies facilitated the popular buy in to the new hegemonic project of international Fordism in advanced capitalist states.

The policy choices advocated by IMF in regard to LICs during the Bretton Woods era also can be traced to the social forces and contradictory elements of international-Fordist hegemony. As introduced in chapter 2, much of the developing world during this time embraced ISI policies. While Fund policy makers were opposed to the heavy state intervention and protectionism of ISI, IMF conditionality requirements for poor states did not require internal structural reforms to liberalize their

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incentivized to return to equilibrium. Under this plan, conditionality would not be tied to borrowing and states with balance of payments deficits could pursue full employment policies.

<sup>468</sup> As discussed in chapter 2, under the classic gold standard, a state with balance of payment deficits was to implement rapid deflationary monetary and fiscal policy. Under the modified gold standard of the Bretton Woods, resources from IMF loans would allow states with deficits to adjust more slowly and systematically to return to balance of payment equilibrium. Resources from Fund loans also could be selectively targeted to help vulnerable groups in period of adjustment.

economies during this time period. Fund policy therefore reflected a position of compromise between the policy objectives and ideology of a U.S. led international historic bloc and elites in ISI states. For the former, tepid support of state capitalist – but anti-communist regimes – was a necessary compromise given the realities of Cold War politics. The integral role of generally anti-communist unions in the corporatist model of ISI also was congruent with the model of Fordist class coalitions seen in wealthy capitalist states. Rather than force structural reforms to dismantle ISI through the leverage of conditionality requirement as was done in the 1980s and 1990s, the IMF instead pushed its anti-statist agenda through technical assistance programs such as the IMF Institute. Cox argues that this less coercive dynamic of winning hearts and minds of elites in peripheral states to reflect the interests and belief systems of dominant social and economic forces is a critical component of how international organizations, including the Fund, reproduce hegemony.<sup>469</sup>

### **The IMF, Globalization, and the Politics of Supremacy**

If the IMF played a central role in – and was reflective of – the formation and reproduction of a hegemonic world order during the Bretton Woods era, neo-Gramscians maintain that the Fund also played a critical role in the shift away from U.S. led international Fordism starting in the late 1960s. Here, historical structural analysis of the contemporary world order and its relationship to the IMF and its LIC policy choices focuses on four interrelated themes: the introduction and acceleration of globalized production following the crisis of Fordism in the 1970s; the rise of an American led globalist historic bloc dominated by an emerging transnational capitalist class unable to secure global hegemony; a restructuring of the liberal-Keynesian welfare state form to a transnational, neoliberal

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<sup>469</sup> Cox, “Gramsci, Hegemony and International Relations: An Essay in Method,” pp. 172-173.

state form; and counter-tendencies that have emerged that challenge what Stephen Gill describes as the “politics of supremacy” employed by the globalist historic bloc.<sup>470</sup> I develop these themes below.

For two decades following WW II, the Fordist model produced historically unprecedented rates of growth, labor productivity, low unemployment, increased living standards, and redistribution in developed capitalist economies.<sup>471</sup> By the late 1960s and early 1970s, Fordism and the hegemonic Bretton Woods order began to falter. Drops in productivity and consumption in wealthy capitalist states, combined with the spikes in oil prices due to Middle East conflict, produced both high unemployment and inflation. Profit rates also fell sharply through the 1970s, as did exchange rate stability when the Bretton Woods modified gold standard was abandoned in 1973.<sup>472</sup> Marxist and neoGramscian scholars point to this “crisis of capitalism” as the catalyst that sparked a new epoch characterized by a movement away from nationally organized capitalism and Keynesian state forms toward a world characterized by the emergence of globalized capitalist production and transnational, neoliberal state-forms.<sup>473</sup>

A key variable in the restructuring of capitalism and state forms is the emergence of what Robinson, Kees van der Pijl, and Leslie Sklair describe as the “transnational capitalist class” (the TCC).<sup>474</sup> The

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<sup>470</sup> Stephen Gill, “Globalization, Market Civilization, and Disciplinary Neo-Liberalism,” *Millennium: Journal of International Studies* 24, no. 3 (1995), pp.411-431.

<sup>471</sup> Andrew Glyn *Capitalism Unleashed: Finance, Globalization and Welfare*, (Oxford: Oxford University Press, 2006), p.1.

<sup>472</sup> *Ibid.*, pp.2-8.

<sup>473</sup> Robinson describes this process in more detail as follows: “The post-World War II expansion- the so called “golden age” of nation-state capitalism-entered into crisis in the 1970s, precipitating a period of restructuring and transformation. Capital responded...by “going global.” This allowed it to break free of the constraints that had been imposed on profit maximization by working and popular classes and by national government in the preceding epoch of Keynesian capitalism.” Robinson, *A Theory of Global Capitalism: Production, Class, and State in a Transnational World*, pp. 148-149.

<sup>474</sup> For further discussion of transnational capitalist class formation, see Kees van der Pijl, *Transnational Classes and International Relations* (London: Routledge, 1998) and Leslie Sklair, *The Transnational Capitalist Class* (Oxford: Basil Blackwell, 2002).

TCC, made up of the owners and managers of transnational corporations and transnational financial institutions, has become the “owners of the major productive resources of the world” and as such “imposes the general direction of production worldwide and conditions the social, political, and cultural characteristics of capitalist society worldwide.”<sup>475</sup> The TCC also serves as the dominant class in an emerging globalist historical bloc described by Robinson as follows:

At the center of the globalist bloc is the TCC...and also includes the elites and bureaucratic staffs of the supranational organizations agencies such as the International Monetary Fund, the World Bank, and the WTO. The historic bloc also brings together major forces in the dominant political parties, media conglomerates, and technocratic elites and state managers in both North and South, along with select organic intellectual and charismatic figures who provide ideological legitimacy and technical solutions...Below this transnational elite is a small, shrinking layer of middle classes who exercise very little real power but who, pacified by mass consumption, form a fragile buffer between the transnational elite and the world’s poor majority.<sup>476</sup>

Since the 1970s, this bloc has supported a two dimensional strategy to restructure social and economic systems to support global capitalist production. The first dimension involves worldwide market liberalization and the formation of legal and regulatory structures to support globalized production and trade (e.g., the formation of the World Trade Organization in 1995). The second involves the internal restructuring and integration of national economies into the liberalized global economy.<sup>477</sup> As documented by multiple studies of the IMF and World Bank, the Bretton Woods institutions were central players in this process in LICs, particularly after the 1982 Mexican debt crisis.<sup>478</sup> Robinson, for example, highlights that the IMF and World Bank implemented over 566 structural adjustment

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<sup>475</sup> Robinson, *A Theory of Global Capitalism: Production, Class, and State in a Transnational World*, pp.47-48.

<sup>476</sup> *Ibid.*, pp.75-76.

<sup>477</sup> *Ibid.*, pp.77-78.

<sup>478</sup> Woods, *The Globalizers: The IMF, the World Bank, and their Borrowers*, pp.141-178; Richard Peet, *Unholy Trinity: The IMF, World Bank, and WTO* (Johannesburg: WITS University Press, 2003), pp.74-110; Duncan Green, *Silent Revolution: The Rise of Market Economics in Latin America* (London: Cassell, 1995), pp.60-89.



programs in over seventy countries from 1979-1992 focused primarily on dismantling state heavy and protectionist strategies of ISI.<sup>479</sup>

The restructuring of the national economies through the efforts of the IMF, World Bank, and other members of the globalist bloc also is interrelated to the “transnationalization” and “neoliberalization” of state forms. In comparison to the state form of *pax Americana*, the most critical difference in contemporary state-society relations is the marginalization of organized labor. As noted above, class compromise forged in capitalist states in the mid-20<sup>th</sup> century served to constrain both emerging factions of globalizing capital and nationally based capital in the Bretton Woods era. In the post-Bretton Woods period, the mobility of capital and concentrated efforts of the globalist bloc to undermine unions and Keynesian welfare state policies has drastically reduced the bargaining position of labor.<sup>480</sup> As articulated by Robinson, “In the new capital-labor relation, labor is increasingly only a naked commodity, no longer embedded in relations of reciprocity rooted in social and political communities that have historically institutionalized in nation-states.”<sup>481</sup> In both industrial societies and LICs, this has translated in part to sharp reductions of unionization levels, and subsequent increases in flexible labor markets, subcontracting, outsourcing, part-time and temp work, and informal economic activities.<sup>482</sup>

Gill and Robinson contend that this more adversarial relationship between labor and capital is one example of a broader theme of the “politics of supremacy” that has marked the post-Bretton Woods

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<sup>479</sup> Robinson, *A Theory of Global Capitalism: Production, Class, and State in a Transnational World*, p.79.

<sup>480</sup> Marxist state theorist Bob Jessop describes the contemporary state form as a “post-Fordist Schumpeterian workfare state.” For further discussion on the relationship of post-Fordist labor flexibility and state forms, see Bob Jessop, “Towards a Schumpeterian Workfare State? Preliminary Remarks on Post-Fordist Political Economy,” *Studies in Political Economy* 40 (1993), pp. 7-40 and David Harvey, *A Brief History of Neoliberalism* (Oxford: Oxford University Press, 2005), pp. 64-86.

<sup>481</sup> Robinson, *A Theory of Global Capitalism, Production, Class, and State in a Transnational World*, p.75.

<sup>482</sup> *Ibid.*, p.104.

historical structure and actions of the globalist historic bloc. Supremacy in this context refers to “rule by a non-hegemonic bloc of forces” that exercise dominance over other groups.<sup>483</sup> Multiple factors in the contemporary era facilitate supremacy over hegemony. These include the socially destabilizing effects of inherent contradictions found in capitalism (e.g., overproduction and under consumption, polarization of wealth) that are exacerbated by the increased scale of globalized production and the elimination of Keynesian welfare and ISI state forms.<sup>484</sup> In addition, the globalization of production produces tension between the ascendant transnational and weakening nationally based capital. Workers tied to transnational capital will not share the same interests and policy positions (e.g., rejection of protectionism) as those tied to nationally based companies.<sup>485</sup>

The globalist bloc has also failed to produce and sustain a universal and unified social vision to ideologically legitimate its dominant position and policy reforms. This is not due to lack of effort. Most salient in this regard is the influence of discourses surrounding globalization employed by the globalist bloc. Starting in the 1980s and becoming most pronounced after the collapse of communism and the economic boom of the 1990s, liberal market globalization was articulated as the inevitable and best option to maximize economic well-being, individual freedom, and democratic rule. Manfred Steger, in his study of the ideology of the globalist bloc, describes this framing of globalization in liberal market terms as “globalism”:

...globalism...endows the concept of globalization with market-oriented norms, values, and meaning. The only viable public policy, so this dominant story of globalization goes, is one supportive of economic deregulation, privatization, free trade, unfettered capital movement, low taxation, and fiscal austerity, especially with regard to social programs.<sup>486</sup>

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<sup>483</sup> Gill, *Power and Resistance in the New World Order*, p.60.

<sup>484</sup> Robinson, *Production, Class, and State in a Transnational World*, pp.145-158.

<sup>485</sup> Bieler and Morton, “A Critical Theory Route to Hegemony, World Order, and Historical Change,” p.95.

<sup>486</sup> Manfred Steger *Globalism: Market Ideology Meets Terrorism* (New York: Rowman & Littlefield, 2005), xi. Steger references Thomas Friedman, including his bestselling *The Lexus and the Olive Tree: Understanding Globalization*, as a quintessential example of globalist thinking.

Specific to the IMF, its implementation of SAF and ESAF lending served as a primary vector to reinforce this ideological framework of globalism in the 1980s and 1990s in LICs. As with the framing of Fordism, the implementation of new policy direction was presented in universal terms. Liberal market restructuring and the elimination of ISI, despite the fact it prioritized the interests of local elites tied to transnational capital, was to benefit the population at large in the new global era.<sup>487</sup>

By the early 1990s, several factors undermined the globalist vision in LICs and broader prospects of a hegemonic world order. The success of the Asian miracle, built around state centered export-led industrialization, appeared to contradict the liberal market positions pushed by the Fund and Bank. Low and negative growth rates in LICs that had implemented SAPs also increased internal and external criticism of Washington Consensus programs and policy directives. As documented in chapter 3, protest movements and NGOs also began to more forcefully challenge the liberal market restructuring of state-society relations and did so through presenting alternative conceptions of globalization. Specific to the IMF and LICs, the reaction to these challenges was primarily a defensive posture in the late 1980s through the mid-1990s. Rather than address the concerns of policy insiders and NGO critics, the Fund and World Bank rolled out a new program focused on “good governance.”

Proponents of good governance within the Fund argued that the primary variables responsible for poor growth outcomes in LICs that had entered into SAPs were corruption and/or poor government institutions. Structural adjustment was not to be abandoned, but rather deepened through accelerated privatization efforts in conjunction with conditionality requirements that focused on restructuring

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<sup>487</sup> Ian Taylor, “Hegemony, Neoliberal “Good Governance” and the International Monetary Fund: A Gramscian Perspective,” in *Global Institutions & Development: Framing the World*, eds. Morton Bøås and David McNeill (London: Routledge, 2004), pp. 124-136 at pp.134-136.

government institutions in ways that would reduce potentials for rent-seeking and corruption.<sup>488</sup> This position was captured in the Fund's 1997 overview of its role in governance issues, where the staff was advised to highlight how corruption and rent-seeking could sabotage the benefits derived from privatization:

The potential risk that poor governance could adversely affect private market confidence and, in turn, reduce private capital inflows and investment...should also be brought to the attention of the authorities. IMF policy advice should...be based on the broadly agreed best international practices of economic management and on the principles of transparency, simplicity, accountability, and fairness.<sup>489</sup>

NeoGramscians argue this linkage of governance issues to structural adjustment served to strengthen the hand of elites in LICs who pushed highly unpopular privatization policies in the late 1980s and early 1990s.<sup>490</sup>

Fallout of these policy decisions included a dramatic increase in social upheaval in much of the global South during the Washington Consensus period. Along with pockets of violent resistance (e.g. the Zapatista movement) to policies of trade liberalization, over 146 austerity protests against IMF and World Bank restructuring were documented in LICs between 1976 and 1992.<sup>491</sup> Incidents of protest and social movement mobilization continued through the 1990s. In Latin America and the Caribbean, for example, 281 protest campaigns and 961 protest events targeting various aspects of liberalization and privatization policies occurred between 1995-2001.<sup>492</sup> Various campaigns focused around the fifty

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<sup>488</sup> The IMF described privatization efforts as a 'second-stage' strategy of structural adjustment.

<sup>489</sup> IMF, *Good Governance: The IMF's Role* (Washington, D.C.: IMF, 1997), p.7.

<sup>490</sup> Rückert, "Producing Neoliberal Hegemony? A neoGramscian Analysis of the Poverty Reduction Strategy Paper (PRSP) in Nicaragua," p.98; Taylor, "Hegemony, Neoliberal "Good Governance" and the International Monetary Fund: A Gramscian Perspective," p.133.

<sup>491</sup> Jan Aart Scholte, "The IMF and Social Movements," in *Contesting Global Governance: Multilateral Economic Institutions and Global Social Movements*, ed. Robert O' Brien, Anne Marie Goetz, Jan Aart Scholte, and Marc Williams (Cambridge: Cambridge University Press, 2000), pp.159-205 at p.173.

<sup>492</sup> Paul Almeida, "Defensive Mobilization: Popular Movements Against Economic Adjustment Policies in Latin America," *Latin American Perspectives*, 34, no.3 (2007), pp. 123-139 at p. 128.

year anniversary of the IMF and Bank in 1994 also highlighted the lack of broad based ideological buy in and consensus around the benefits of the globalist model.<sup>493</sup>

NeoGramscians also highlight the central role of the U.S. in reinforcing a global governance framework that facilitated the interests of the globalist bloc, but reinforced this process primarily through non-consensual means. Gill, for example, argues that U.S. pressure was central in Fund and other multilateral institutional efforts to restructure global governance and country specific reforms in a manner that attempted “to make transnational liberalism, and if possible liberal democratic capitalism, the sole model for future development.”<sup>494</sup> Gill describes the governance strategy pushed by U.S. led globalist bloc as “new constitutionalism.” Under new constitutionalism, governments were pressured to limit the input or influence of politicians and citizens on fiscal, monetary, trade, and investment policy. This was manifested in a move toward central bank independence in many LICs and laws to forcefully protect private property rights and free trade. Managing Director Camdessus, in a 1995 speech on the theme of globalization and the IMF, reiterated these themes as follows:

First and foremost, countries must maintain sound domestic macroeconomic policies that will attract and retain the market’s confidence. In particular, policymakers must recognize that the scope for countries to depart from traditional macroeconomic discipline is now sharply reduced...Trade liberalization, privatization, and the establishment of transparent regulatory systems...help create an environment in which capital inflows can be more readily used for long-term productive investment...At the same time, it is critically important to establish solid domestic institutions – especially independent central banks and strong domestic banking systems – that can accommodate tighter fiscal and monetary conditions as the need arises.<sup>495</sup>

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<sup>493</sup> Jackie Smith, *Social Movements for Social Democracy* (Baltimore: John Hopkins Press, 2008), pp.100-101.

<sup>494</sup> Gill, *Power and Resistance in the New World Order*, p. 132.

<sup>495</sup> Michel Camdessus, “The International Monetary Fund and the Challenges of Globalization,” Address at The Free University, Amsterdam, 18 November 2005, (IMF Archives), pp.3-4.

Along with support of good governance and “traditional market discipline,” the new era of globalization also required that the Fund increase its surveillance role in member states.<sup>496</sup> As outlined by Camdessus, in order to avert the cascading effects of economic and financial crisis, the IMF has developed a relationship with LICs that was “...more continuous, intensive, and probing.”<sup>497</sup>

In sum, a historical structural understanding of the IMF in the Washington Consensus period highlights how a reconfiguration of social forces and state-society relations by a globalist bloc tied to transnational capital shifted the role of Fund in relation to LICs. Rather than reinforce a hegemonic world order underwritten by Fordist class compromise and U.S. consensual leadership as seen in the Bretton Woods era, IMF LIC policy in the last three decades of the 20<sup>th</sup> century reflected the interests and actions of an emerging globalist bloc unable to secure hegemony. As such, the social and economic restructuring of LICs to support globalizing capital were implemented generally through disciplinary measures. Specific to the IMF, this included conditionality requirements focused on dismantling remnants of ISI in SAF and ESAF concessional lending agreements. Not surprisingly, this approach failed to garner broad based support from a variety of sectors in LICs, including elites tied to national capital and urban working and middle classes who had previously benefited from the ISI model.<sup>498</sup> If the globalist bloc was unable to secure hegemony by the mid-1990s, the growing number and militancy of protest movements focused on the policies of the IMF, World Bank, and the newly

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<sup>496</sup> Themes of surveillance and ‘new constitutionalism’ in LICs was also reinforced by the Uruguay Round of the GATT (lasting from 1986-1994) and the formation of the World Trade Organization in 1995. Three trade agreements were formed during the Uruguay Round that moved multilateral trade policy beyond a focus only on manufactured and agricultural goods. These included the General Agreement on Trade in Services (GATS), the Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPs), and the Agreement on Trade Related Aspects of Investment Measures (TRIMs). The GATS, TRIPs, and TRIMs were incorporated into the newly formed WTO along with the controversial Dispute Settlement Body (DSB). A state can lodge a formal grievance to the DSB if they believe another member state has violated its rights under WTO agreements.

<sup>497</sup> Camdessus, “The International Monetary Fund and the Challenges of Globalization,” p.6.

<sup>498</sup> Resistance also occurred in the industrialized world. Rupert, for example, documents various progressive and reactionary responses to the implementation of NAFTA in the early 1990s. See Mark Rupert, *Ideologies of Globalization: Contending visions of a New World Order* (London: Routledge, 2000).

formed World Trade Organization in the late 1990s further undermined attempts to form a consensual global political order.

Internal dissent among policy elites in regard to the wisdom of the Washington Consensus also increased following the Asian crisis of 1997-1998. By the turn of the century, prominent economists, including Joseph Stiglitz, Jeffrey Sachs, Paul Krugman, and Jagdish Bhagwati, called for alternatives to the development and trade strategies pushed by the U.S. and the IMF.<sup>499</sup> Powerful institutional leaders, including World Bank president James Wolfensohn, United Nation's General Secretary Kofi Annan, and World Economic Forum (WEF) Executive Director Klaus Schwab, lobbied for a rethinking of development and trade strategies, often invoking the theme of "globalization with a human face."<sup>500</sup> Critiques of the IMF following the Asian crisis also came from conservative voices, particularly within the United States. In return for support of Clinton administration funding requests for the IMF in 1998, the Republican controlled Congress created the Financial Institution Advisory Commission (known more commonly as the "Meltzer Commission") to review the IMF and other multilateral institutions. The Meltzer Commission highlighted multiple IMF policy failures in LICs and called for a drastically reduced role for the institution in structural adjustment lending.<sup>501</sup>

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<sup>499</sup> The most developed critique of the Washington Consensus was that of Joseph Stiglitz. Stiglitz was fired from his position of chief economist of the World Bank in 1999 for his pointed critique of the IMF and the U.S. Treasury regarding their development policy positions and response to the Asian Crisis.

<sup>500</sup> Robinson, *A Theory of Global Capitalism*, p.164.

<sup>501</sup> Formed through the efforts of Republican Senator Phil Gramm and House majority leader Dirk Armey, the Meltzer Commission released its findings in March 2000. The majority of the eleven commissioners argued that future IMF lending to LICs should be: short term only (no longer than 120 days) and preconditioned on the credit viability of the state in question (no lending to countries with questionable credit). Two unanimous recommendations from the Commission included a call for the write off of debt for heavily indebted poor countries and that the Fund limit any future lending to short term loans. See Kathryn Lavelle, *Legislating International Organization: The US Congress, the IMF, and the World Bank* (Oxford: Oxford University Press (2011), pp. 143-152.

For Gramscian scholars focused on this time period, the growing criticism of globalist orthodoxy from below and internal division among elites signaled a prominent shift in the nature of the contemporary historical structure and world order. Robinson, for example, argued that the “clamor for reform from the top down” signified “a crisis of confidence in the global capitalist system within the ranks of the transnational elite and a willingness among the more politically astute to promote a ‘post Washington Consensus’ project reform to save the system itself.”<sup>502</sup> Rupert highlights a similar loss of confidence and consensus among globalist bloc elites that emerged in the late 1990s.<sup>503</sup> Even U.S. president Bill Clinton, perhaps the most ardent cheerleader for neoliberal reform throughout the 1990s, now argued that these same policies bore some responsibility for undermining working class support of free trade and globalizing capitalism.<sup>504</sup>

### **Toward a new hegemony? IMF LIC reform in the post Washington Consensus.**

The turmoil and crisis seen within the globalist bloc in the late 1990s and early 2000s serves as the contextual foundation for neoGramscian explanations of post Washington Consensus policy change. As introduced in chapter 1, Robinson and Rückert maintain that post Washington Consensus reforms are a form of “inclusive neoliberalism” ultimately designed to undermine growing resistance and challenges to the globalist bloc and the broader project of globalizing capitalism. Specific to the IMF, reforms including debt relief through the HIPC and HIPC II initiatives, “pro-poor” lending through introduction of the PRGF, “participatory” development strategies with the introduction of Poverty Reduction Strategy Papers (PRSPs), and Keynesian-inspired policies of the ECF/RCF/SCF are explained as attempts by the globalist bloc to “attenuate some of the sharpest social contradictions of

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<sup>502</sup> Robinson, *A Theory of Global Capitalism*, p.163.

<sup>503</sup> Mark Rupert, *Ideologies of Globalization: Contending visions of a New World Order* (London: Routledge, 2000) pp.143-144.

<sup>504</sup> *Ibid.*, pp.144-145. Rupert documents the growing concern exhibited by Clinton in 1998 and 1999 to the lack of political support for the globalist project both in the U.S. and world community. In response, Clinton focused on integrating concerns raised by the International Labor Organization (ILO) into WTO, IMF, and World Bank policy decisions. Clinton also pushed the WTO and IMF to address concerns from the NGO community.



global capitalism” in the interests of assuring “long term stability and reproduction” of the current historical structure.<sup>505</sup> In this section, I assess and build on this interpretation of IMF LIC reforms in the post Washington Consensus as follows. I first briefly outline the concept of “inclusive neoliberalism” as initially developed by David Craig and Doug Porter and applied by contemporary neoGramscians to their understanding of contemporary multilateral policy reforms. I then examine if and how post Washington Consensus IMF LIC policy changes were reflective of discord within the globalist bloc. I focus specifically on if there is evidence to support the notion that the impetus for these reforms is rooted in broader attempts by the globalist historic bloc to build a new hegemonic order reinforced by a more inclusive form of capitalism and development.

Gramscian explanations of post-Washington Consensus Fund policy reforms maintain that these policy shifts are rooted in a new inclusive form of capitalism that has emerged within the globalist bloc. As outlined by Craig and Porter, the inclusive liberal market model is rooted in the belief that the pursuit of free markets and social goals are not only mutually compatible, but also produce a positive feedback loop of improved development outcomes.<sup>506</sup> Within the IMF ( and World Bank), this has translated into the “participatory” and “pro-poor” reforms that emerged in the late 1990s that focused on the interdependence of the economic growth, reduced poverty, and increased social empowerment and inclusion.<sup>507</sup> As outlined in the Fund’s current guidelines for LIC policy, for example, poverty reduction strategies “should be...country-driven, promoting national ownership of strategies through

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<sup>505</sup> Robinson, *A Theory of Global Capitalism*, p.163.

<sup>506</sup> David Craig and Doug Porter, “The Third Way and the Third World: Poverty Reduction and Social Inclusion Strategies in the Rise of ‘Inclusive’ Liberalism,” *Review of International Political Economy* 12, no.2 (2005), pp.226-263.

<sup>507</sup> Along with Craig and Porter and Rückert, various critical explorations of more inclusive forms of neoliberalism in LICs include: Graham Harrison, “Economic Faith, Social Project, and a Misreading of African Society: The Travails of Neoliberalism in Africa,” *Third World Quarterly* 26, no.9 (2005), pp.1303-1320; Adam David Morton, “Structural Change and Neoliberalism in Mexico: ‘Passive Revolution’ in the Global Political Economy,” *Third World Quarterly* 24, no.4 (2003), pp.631-653; and Palash Kamruzzaman, “Poverty Reduction Strategy Papers and the Rhetoric of Participation,” *Development in Practice* 19, no.1 (2009), pp.61-71.

broad-based participation of civil society; ...partnership-oriented, involving coordinated participation of development partners (government, domestic stakeholders, and external donors); and based on a long-term perspective for poverty reduction.”<sup>508</sup>

Craig and Porter maintain that explanations for a move away from the strict model of market liberalization to a more inclusive variant is clarified through comparison of early 21<sup>st</sup> century dynamics to those seen in episodes of 19<sup>th</sup> and 20<sup>th</sup> century capitalist development. They argue that prior to the current era of globalizing capitalism, trends followed roughly Karl Polanyi’s concept of “double movement” in market-society relations.<sup>509</sup> The first movement of market liberalization and state-society restructuring to support capitalist development was supported by an ideological framework that separated economics from politics and replaced traditional and local social regulation with the ‘laws’ of market-based relations. The second movement, social regulation and government policies that moderate the effects of market forces, followed soon thereafter as was seen in the emergence of Keynesian welfare states, ISI state models, or more nefariously expressed in state capitalist models of fascist regimes.<sup>510</sup>

For Craig and Porter, the post Washington Consensus period differs from previous eras in that policies of inclusive neoliberalism appear to pre-emptively undermine the possibility of the second movement in LICs:

Comparison with Polanyi’s account leads to the conclusion that Poverty Reduction and Social Inclusion are in fact an attempt to secure and embed liberal reforms in the social order...but one that is being actively managed from the top down, drawing potential adversaries into managed dialogues and partnerships... [and acts as]...a kind of pre-

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<sup>508</sup> IMF, “International Monetary Fund Factsheet: Poverty Reduction Strategy Papers.” Available at <http://www.imf.org/external/np/exr/facts/prsp.htm>.

<sup>509</sup> Karl Polanyi, *The Great Transformation* (New York: Rinehart, 1944).

<sup>510</sup> Craig and Porter, “The Third Way and the Third World: Poverty Reduction and Social Inclusion Strategies in the Rise of ‘Inclusive’ Liberalism,” pp. 231-233.

emptive, strategic inoculation against a more broadly and socially contested double movement, the kind of double movement arguably most feared by the agents of a wider liberal project.<sup>511</sup>

Rückert argues that a key dynamic in this “strategic inoculation” against more statist or redistributive centred reactions to the Washington Consensus period is the role that the Bretton Woods institutions currently play in absorbing radical challenges to a market driven development paradigm. Two primary mechanisms are identified. First, incorporation of LIC elites into decision-making processes around poverty reduction strategies and policy choices tied to lending arrangements undermines potential challenges to the globalist model. Increased dialogue with civil society over the last decade also absorbs “counterhegemonic ideas and concepts to make it seem as though the concerns of critics are being heard and taken seriously.”<sup>512</sup>

Internal IMF documents over the past decade and interviews with various IMF LIC staff demonstrate that the institution was aware of growing resentment and push back by the late 1990s. Fund staff, for example, specifically recognized and articulated the need to secure ‘buy in’ from various constituents in LICs as seen in a 2001 staff paper titled “IMF Conditionality and Country Ownership of Programs”:

Ownership matters because it directly affects program implementation... When the program is owned by the country, decisions on such action are likely to be made quickly and in support of the program, which makes it more likely that the program will succeed. Furthermore, ownership will make it easier to generate domestic political support for the program, since it is likely to be seen, as an indigenous product, rather than a foreign imposition.<sup>513</sup>

In 2003, the IMF prepared an internal “Guide for Staff Relations with Civil Society Organizations” that reiterated similar themes. The rationale for engaging with civil society concluded that “Active civil society involvement with global institutions like the IMF is not only an inescapable fact of life in

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<sup>511</sup> *Ibid.*, p.257.

<sup>512</sup> Rückert, “Producing NeoLiberal Hegemony,” p. 97.

<sup>513</sup> Mohain S. Khan, “IMF Conditionality and Country Ownership of Programs,” IMF Working Paper No. 01/142, 25 February 2001, p. 14, available at <http://www.imf.org/external/pubs/ft/wp/2001/wp01142.pdf>, as cited by Rückert, “Producing Neoliberal Hegemony?,” p. 103.

21<sup>st</sup> century politics, but there are also significant reasons for the Fund to welcome and nurture these relationships.” These reasons included dispelling “public misconceptions regarding the Fund and its activities,” increasing “support for Fund backed measures,” and deepening “ownership of the policies that the Fund advances.”<sup>514</sup>

LIC staff interviewed also highlighted a shift toward a more consensual approach with LIC authorities following the turmoil of the late 1990s and early 2000s:

One area where there has been a sea-change in the last ten to fifteen years is that we are turning more and more to the countries and saying, “What’s your plan?, What do you think? How can we help you do this?” rather than “This is the answer, the Washington Consensus, here is the recipe.”<sup>515</sup>

We noticed with the debt campaigns in the late 1990s how important it was that certain topics be discussed in the public domain and that we take into account what people are thinking about these things and listen carefully to what they say.<sup>516</sup>

Structural adjustment had gotten a very bad name over the ten years from 1986, particularly within the recipient countries. I think it is still debatable whether that was a cover for their own failings, but structural adjustment certainly coincided with a time that really was very hard for low income countries. It is natural that people would say that it was the IMF’s fault. You still hear that a lot in Ghana and Nigeria as they went through very difficult periods. So our changes reflected at some level the pressure from the African countries on our policy who said we couldn’t go on like this, that we had to rethink how you do business.<sup>517</sup>

A move toward a more consensual approach is noted by several LIC country authorities, including the former Permanent Secretary of Tanzania’s Minister of Finance, who noted a shift in the Fund’s “willingness to listen” following the Asian crisis.<sup>518</sup> The notion that the Fund was sensitive to public

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<sup>514</sup> IMF, “Guide for Staff Relations with Civil Society Organizations,” 10 October 2003, p.4, available at <http://www.imf.org/external/np/cso/eng/2003/101003.htm>.

<sup>515</sup> Author interview with Deputy Director of the Africa Department, Washington D.C., 13 June 2011.

<sup>516</sup> Author interview with staff member from the Strategy, Policy, and Review Department (Special IMF Representative to the United Nations), Washington D.C., 20 September 2011.

<sup>517</sup> Author interview with Division Chief of the Africa Department, Washington D.C., 21 September 2011.

<sup>518</sup> “The relationship between the IMF and Tanzania has become stronger over the past decade. Two most important factors explain this positive trend: The first is Tanzania’s commitment to reform, with enhanced ownership to the reform agenda. The second is the IMF’s willingness to listen and allow Tanzania to determine policies suitable to Tanzania’s circumstances and the IMF responding with adequate support and minimum conditionality. This is a reflection of the IMF’s commitment to reform within itself, which was not the case before.” Gray Mgonja, “Tanzania-Reform and Progress,

perception and the need to build legitimacy at the turn of the century is further supported by evidence from a series of Executive Board evaluations of its external communications strategy. These studies, undertaken in 1998, 2000, and 2003, included in-depth analysis of the number and slant of media reports on the IMF and also undertook surveys to gauge public opinion.<sup>519</sup> The 2003 report concluded that in regard to its public perception, “the challenge the Fund faces is long-standing and deep rooted” and “that its public image continues to be slightly less favourable than the World Bank, and both trail the United Nations in polls of elites and the general public.”<sup>520</sup> The report also noted that despite current low favourability ratings, the IMF was now seen as a less secretive institution and “should seize on this opportunity to build on this opportunity through a continuous, well-coordinated communications effort aimed at improving understanding of and support for the Fund and its activities.”<sup>521</sup>

Field studies that evaluate the engagement of the Fund with civil society actors in African LICs undertaken by Jan Aart Scholte also support the notion that the IMF actively worked to increase consensus building in the 2005-2010 time period.<sup>522</sup> Since 2006, the IMF and Bank have sponsored up to forty civil society actors from LICs to participate in each round of the Annual and Spring Meetings. In 2007, the Fund also created a “civil society liaison” position within its external relations department focused specifically on relations with LICs. And in 2010, a new Regional Advisory Group

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1995-2007,” in *Successes of the International Monetary Fund: Untold Stories of Cooperation at Work*, ed Eduard Brau and Ian McDonald (London: Palgrave Macmillan, 2009), pp. 101-105 at p.105.

<sup>519</sup> The 1998 and 2000 reports are discussed in the 2003 review. See IMF “A Review of the Fund’s External Communications Strategy,” 13 February 2003, pp 5-6, available at <http://www.imf.org/external/np/exr/docs/2003/021303.pdf>.

<sup>520</sup> *Ibid.*, p.3.

<sup>521</sup> *Ibid.*

<sup>522</sup> Jan Aart Scholte, “A More Inclusive Global Governance? The IMF and Civil Society in Africa,” *Global Governance* 18, no.2 (2012), pp. 185-206.

for Sub-Saharan Africa was formed that includes three civil society representatives among its twelve members.<sup>523</sup>

Fund Documents and staff responses also point to the fallout of the 2008 crisis as deepening the participatory, consensual approach to IMF LIC policy implementation. LIC staff highlight the March 2009 Tanzania conference organized by Strauss Kahn as a key moment in this process. As articulated by a senior LIC staff member of the African Department, while the direction of LIC policy didn't radically change due to the Tanzania conference, the interactions with LICs policy makers shifted considerably:

Another watershed moment was the Tanzania Conference where Strauss Kahn said, "Look, I want to speak for you at the G-20, but you need to tell me what you want me to say for you." It can sound a bit patronizing, but it wasn't seen that way. The point of this was that now it was our turn to listen to the LICs. The very fact of the way he said it and the way he held that conference, it didn't change fundamentally the advice we were giving or the economic framework we had on our mind, but it changed the way policy makers would approach and talk to us, and assert themselves. The Tanzania Conference, on one hand, can be seen as a bunch of fluff because the intellectual ideas bantered about were not new, but it was the idea that this is your institution that has to be responsible to your [LIC] needs. So tell us, talk to us about what you want.<sup>524</sup>

Along with a concerted effort to build a more consensual framework of market-driven development in the past fifteen years, the Fund also revamped the form in which LIC conditionality requirements are implemented and monitored following the 2008 crisis. Since the introduction of the SAF in 1986, the Fund employed highly specific "structural performance criteria" to assess if countries borrowing from the institution were on track to comply with loan conditions focused on structural reform. If a member state failed to meet these structural performance criteria, a formal waiver approved by the EB was needed to gain access to future release of loan resources. In May 2009, structural performance criteria

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<sup>523</sup> *Ibid.*, p.199.

<sup>524</sup> Author interview with staff member from the African Department, Washington D.C., 13 June 2011.

were eliminated from IMF conditional lending and replaced by a more general review process coordinated by the EB. The Fund describes the rationale behind this shift as follows:

In the past, the IMF has been criticized by some governments and civil society organizations for demanding too many reforms in exchange for financial assistance.... structural performance criteria came to be seen as a key source of stigma attached to borrowing from the IMF. The IMF is hoping that its new lending framework will overcome the lingering mistrust that has marred its relations with some countries, particularly after the Asian crisis in the 1990s, and that countries in need of help to overcome what has been billed as the worst economic crisis since the Great Depression will no longer hesitate to approach the IMF.<sup>525</sup>

According to a senior staff member in the SPR Department, the elimination of the structural performance criteria was a calculated cost-benefit analysis focused on increasing buy in from LIC authorities and civil society to the necessity of structural reform: “There was a feeling that conditionality had gotten a bit out of control and it was time to trim it back. The benefit is that you will have a program that had greater ownership by the authorities and we were willing to go down that road.”<sup>526</sup> IMF LIC policy reform in the post-Washington Consensus period thus is characterized by an active consideration for consensus building and a less disciplinary framework of market driven development.

More controversial is the claim articulated by Robinson and Rückert that post-Washington Consensus IMF policy shifts and broader themes of inclusive liberalism are the by-products of a conscious effort by elements of the TCC and the globalist bloc to move away from the “politics of supremacy” toward a more consensual, hegemonic global order. As introduced above, Robinson argues that since the late 1990s, “the transnational elite had moved from the offensive to the defensive as the system began to

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<sup>525</sup>Camilla Anderson, “New Rules of Engagement for IMF Loans,” *IMF Survey Online* 13 April 2009, p.1 , available at <http://www.imf.org/external/pubs/ft/survey/so/2009/pol041309a.htm>.

<sup>526</sup> Author interview with Fund staff member from the Strategy, Policy, and Review Department, Washington D.C., 20 September 2011.

enter a crisis of legitimacy.”<sup>527</sup> Reforms including the HIPC, HIPCII, PRGF, and ECF/RCF/SCF thus represent a reaction to “a crisis of confidence in the global capitalist system within the ranks of the transnational elite and a willingness among the more politically astute to promote a “post-Washington consensus” project of reform in order to save the system itself.”<sup>528</sup>

In the final section of chapter 6, I examine if there is evidence to support this notion through analysis of annual meetings and policy documents of the World Economic Forum (WEF) in the post-Washington Consensus period. The WEF, as highlighted by Robinson, is the “comprehensive transnational planning body of the TCC.”<sup>529</sup> Kees van der Pijl makes similar claims: “The most comprehensive transnational planning body operative today, the WEF...is ...a true International of capital, the first identifiable forum in which concepts of control are debated and if need be, adjusted, on a world scale.”<sup>530</sup> If Robinson’s assertions have validity, we should at a minimum witness three tendencies within the WEF in the post-Washington Consensus period. First, recognition of various crises that characterized this time period. Second, recognition that these crises represent a broader threat to globalizing capitalism. And third, in response to these crises, debate and policy suggestions designed to increase buy in from the global citizenry to the globalist political project.

I focus my analysis on WEF Annual Meetings. Held each January in Davos, Switzerland, the meetings focus on one central theme (see figure 5.2 below) and involve approximately 2500 participants.

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<sup>527</sup> Robinson, *A Theory of Global Capitalism: Production, Class, and State in a Transnational World*, p.146.

<sup>528</sup> *Ibid.*, p.163.

<sup>529</sup> *Ibid.*, p.127.

<sup>530</sup> Kees van der Pijl, *Transnational Classes and International Relations*, pp.132-133.



Figure 5.2 Central Themes of World Economic Forum Annual Meetings (1999-2012)

<u>Year</u>	<u>Theme</u>
1999	Responsible Globality: Managing the Impact of Globalization
2000	New Beginnings: Making a Difference
2001	Sustaining Growth and Bridging the Divides: A Framework for Our Global Future
2002	Leadership in Fragile Times: A Vision for a Shared Future
2003	Building Trust
2004	Partnering for Security and Prosperity
2005	Taking Responsibility for Tough Choices
2006	The Creative Imperative
2007	Shaping the Global Agenda: The Shifting Power Equation
2008	The Power of Collaborative Innovation
2009	Shaping the Post-Crisis World
2010	Improve the State of the World: Rethink, Redesign, Rebuild
2011	Shared Norms for the New Reality
2012	The Great Transformation: Shaping New Models

I start with the 1999 Annual Meeting focused on “Responsible Globality.” WEF documents highlight that participants demonstrated concern in regard to fall out of the economic crises in Asia, Brazil, and Russia, the limitations of free markets, and discussed how to reform globalization in a more inclusive manner:

Crucial discussions were held to look at where globalization is taking us and how we can make it a more responsible process. In the midst of the Asia crisis, after the financial collapse in Russia, and the Brazilian crisis,... it was clear that globalization and free markets left to themselves do not always produce the desired or necessary results for society at large. There was wide spread agreement that although a free market system is the best and most efficient, there are inequalities that government, in new partnerships with other sectors of society, needs to address.<sup>531</sup>

Direct reference was also made to the IMF’s role in the Asian crisis and a need for Fund and other multilateral institutions to “adjust their modus operandi and programmes to the new requirements created by the global economic environment” in order to respond to the “growing backlash of large segments of the world’s population.”<sup>532</sup>

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<sup>531</sup> World Economic Forum, *World Economic Forum Annual Report 1998/1999* (Geneva: World Economic Forum, 1999), p.8.

<sup>532</sup> *Ibid.*

These themes of crisis, backlash, and a more inclusive form of globalization dominated the discussion a year later at the 2000 Annual Meeting. As described by a WEF summary of the event, the fallout of the failed 1999 Seattle World Trade Organization's meeting was a wakeup call for those in Davos who championed globalization:

Two themes dominated the Annual Meeting in Davos this year- the Internet and Seattle. And while opinion was fairly unanimous on the former – it's going to change the world – few exactly knew what to do with the latter. One and a half decades into the technological revolution there is an increasing number of people crying “stop the world, we want to get off.” In Seattle, the protesters may not have spoken with a clear voice that was heard above all others. Although the 20,000 plus protesters that hijacked the agenda probably had as many individual goals, they shared a common view that globalization has somehow turned the planet into a commodity. It was certainly easier in Davos to forge an ideological consensus in favor of globalization, but in the aftermath of Seattle, there also seemed little doubt that the system needed reworking.<sup>533</sup>

Within this context of “reworking the system,” a panel led by British Prime Minister Tony Blair focused on the difference between market economy and market society. “The market economy has clearly won the battle. While people are happy – even eager – to live in a market economy, most do not want to live in a market society. The challenge addressed in Davos is to ensure that society is more than just the market.”<sup>534</sup>

A panel including U.S. President Bill Clinton and World Bank President James Wolfensohn focused on issues of inequality and globalization. Clinton referenced the Seattle protests in his discussion, noting “that too many people felt that had no voice in a world that is changing very rapidly.”<sup>535</sup> He also scolded fellow Davos participants to stop ignoring the realities of increased inequality: “Number one, we should stop denying that there is in so many places an increase in inequality, and we should

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<sup>533</sup> World Economic Forum, *New Beginnings: Making a Difference: Report of the Annual Meeting 2000 of the World Economic Forum* (Geneva: World Economic Forum, 2000), p.18.

<sup>534</sup> *Ibid.*, p.10.

<sup>535</sup> *Ibid.*, p.11.

instead start explaining why it has happened and what we can do about it.”<sup>536</sup> Rolf-Ernst Breuer, Co-Chairman of the Annual Meeting 2000 and Spokesman of the Group Board, Deutsche Bank introduced the term “globalization trap” to describe two levels of individuals divided by income that have emerged in the era of globalization. Wolfensohn, while recognizing global stratification, also argued that “you have to look at other factors including the quality of economic policies being pursued by nations, policies that foster the rule of law, a sound financial system, a strong social framework and measures to combat corruption.”<sup>537</sup>

While a focus on acute crisis receded from 2002-2008 at Davos, the theme of reducing inequality remained. This was complemented by heightened discussion around the eradication of extreme poverty, particularly in Africa. At the 2005 Annual Meeting, for example, the kickoff event prioritized poverty and equitable forms of globalization as the two primary areas in need of attention.<sup>538</sup> The headline panel (including rock star Bono) focused on African poverty also was representative of another trend seen throughout this time period. Namely, voices previously highly critical of the WEF were now invited to participate. This also extended to relations with the NGO community. As outlined in the WEF 2004/2005 Annual Report, “The World Economic Forum has always recognized the importance of engaging civil society, encouraging its representatives to articulate their views to all our events. During 2004/2005, we continued to foster strong relationships with an expanding cross section of unions and NGOs.”<sup>539</sup>

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<sup>536</sup> *Ibid.*, p.18.

<sup>537</sup> *Ibid.*

<sup>538</sup> World Economic Forum, *World Economic Forum Annual Report 2004/2005* (Geneva: World Economic Forum, 1999), p.6.

<sup>539</sup> *Ibid.*, p.24.

While the 2002-2008 period was relatively stable, fallout from the 2008 crisis was of deep concern to WEF participants. At the 2009 Davos meeting, aptly titled “Shaping the Post Crisis World,” the discourse of global crisis management and social backlash reemerged. WEF Executive Chairman Klaus Schwab summarized his concerns as follows:

There is a growing consensus, among the young and the old as well as across developing and industrializing countries that we are experiencing a transformational economic crisis-one that is on course to fundamentally change globalization well beyond the domain of international finance. We face a destructive social backlash that could foment political instability, revive economic nationalism, and reverse development gains should our leaders fail first to develop effective solutions to the current economic crisis and then fail to manage the growing roster of global risks such as climate change, non-proliferation, and food security.’<sup>540</sup>

The theme of social unrest and protectionism was reiterated by then French Minister of Finance Christine Lagarde: “Social unrest and protectionism are the two major risks of the world economic crisis.”<sup>541</sup> In the short term, the message from the 2009 Davos meeting was that a three pronged strategy was necessary to climb out of the crisis. This included a coordinated global fiscal stimulus, a restoration of capital flows to the developing world, and increased global financial regulation.<sup>542</sup> In regard to the former, “although some participants held out hope for “quantitative easing,” most agreed coordinated fiscal stimulus in the G-20 countries is the best hope for supporting global demand.”<sup>543</sup>

Along with calls for Keynesian inspired policy response, the 2009 report also documented a more fundamental discussion that emerged in regard to 21st century capitalism. Schwab, for instance, argued that the crisis required that Davos participants “overhaul our institutions, our systems, and

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<sup>540</sup> World Economic Forum, *Shaping the Post-Crisis World: Report of the Annual Meeting 2009 of the World Economic Forum* (Geneva: World Economic Forum, 2009), p.3

<sup>541</sup> *Ibid.*, p.7.

<sup>542</sup> *Ibid.*, p.12-13.

<sup>543</sup> *Ibid.*, p.12.

above all, our way of thinking.”<sup>544</sup> Specifically, Schwab called for a rethinking of short versus long term economic gain:

Businesses need to look deeply at their systems of remuneration and governance. Industry leaders, policy makers and regulators...all have to consider the damage wrought by excessive greed. In today’s highly interdependent world, the pursuit of short term gain is not a sufficient driver of optimal decision making. The systemic and intergenerational impact of our actions now are more important than they have been before – our ethics, as well as our governance institutions and regulatory systems, must somehow reflect this new reality.<sup>545</sup>

A focus on short term greed among Davos participants was also noted within the context of public buy in or rejection of globalizing capitalism: “In Davos, the potential for social backlash was clearly high on the agenda as participants were discussing how to keep rising joblessness and public outrage over perceived corporate greed from sparking a rollback of globalization. Capitalism need not be jettisoned, they concluded, but it needs to be brought back in line with its role as tool for humanity’s advancement.”<sup>546</sup>

Themes of reforming capitalism continued into the 2011 and 2012 Davos meeting. A synopsis of a 2011 session on “Rethinking Market Capitalism,” for example, concluded that the “Anglo-Saxon” model of capitalism favored by multilateral institutions had fallen out of favor and inferred that a more regulated form was preferable: “Capitalism has created lucrative returns for a few over the past few decades, but has widened the gap between the rich and the poor. Some 34 million jobs have been lost in the last two years alone. Such trends have caused a crisis of confidence in capitalism and corporate executives in particular... Financial institutions that relied on the Anglo-Saxon model of profit maximization fell out of favor in many regions, while Asian banks remained largely healthy and even

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<sup>544</sup> *Ibid.*,p.13.

<sup>545</sup> *Ibid.*,p.3.

<sup>546</sup> *Ibid.*,p.7.

expanded their market share....Some new global regulatory structure is needed and the G-20 may be best positioned to formulate it.”<sup>547</sup>

In sum, evidence from the Davos meetings in the past decade and a half supports Robinson’s claim that the globalist bloc recognizes that crises of the past decade and a half threaten their interests. In response to both the Asian crisis of the late 1990s and the global financial crisis of 2008, members of the TCC demonstrated concern and increased sensitivity to the fact that the status quo of liberal market capitalism was not in the long term best interest of the globalist bloc. Specifically, themes of short term vs. long term profit, inclusivity, poverty reduction, and reduction of inequality were framed as a necessary response to maintain global buy in to the project of transnationalizing capitalism.

## **Conclusions**

Historical structural analysis of post Washington Consensus IMF LIC reform explains these policy shifts through the development of the following themes. First, the Fund is conceptualized not as a thing, but as an expression of time-specific social forces and power relations. A focus on explaining change at the IMF thus directs analysis toward clarifying the major tendencies and contradictions of social forces and power relations in a particular historical structure and how the Fund is interconnected to those tendencies. Second, world orders are broadly characterized as either hegemonic or non-hegemonic in nature. During the Bretton Woods era, the IMF played a key role and was an expression of a hegemonic world order led by a U.S. international-Fordist bloc. From the late 1960s to the 1990s, the IMF’s role changed with shifts in historical structure. Along with other multilateral institutions, the Fund now helped reinforce a non-hegemonic world order characterized by the emergence and consolidation of transnationalizing capitalism and a U.S. supported globalist historic bloc prone to

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<sup>547</sup> World Economic Forum, “World Economic Forum Annual Meeting 2010: Rethinking Market Capitalism,” 28 January 2010, available at [http://www.weforum.org/pdf/AM\\_2010/transcripts/market-capitalism.pdf](http://www.weforum.org/pdf/AM_2010/transcripts/market-capitalism.pdf).

exert more overt forms of coercive power. A key component of this shift in historical structure included the dismantling of Keynesian state forms in the global North and ISI state forms in much of global South. Specific to IMF LIC policy, this was expressed in an increased focus on structural reform issues designed to move poor states away from the ISI model by the late 1970s. Following the 1982 crisis, the Fund more assertively pushed for liberal market economic restructuring in LICs through use of SAF and ESAF conditional lending followed by a focus on issues of good governance in the early 1990s.

Growing resistance to the agenda of the globalist bloc and the Washington Consensus model of development grew throughout the 1990s. By the late 1990s, the combination of growing global protest movements and the Asian crisis ushered in the current post Washington Consensus period. For neo-Gramscians including Robinson and Rückert, the post Washington Consensus is seen in broad terms as an attempt by the globalist bloc to soften globalizing capitalism in order to secure its long term survival. Specific to the IMF and LICs, this is expressed primarily in *how* policies supportive of liberal market development are implemented. Rather than the top down, disciplinary mode of the Washington Consensus period, there is now a focus on inclusion of LIC elites and civil society organizations into lending arrangements through the introduction of the PRSP process. This participatory process thus is one strategy to secure long term buy in to the globalist political project. Another “strategic inoculation” against more radical challenges to capitalist development includes the connection of participation with a focus on poverty reduction. As seen with the replacement of the SAF and ESAF with the PRGF in 1999, lending to LICs now requires both participation and specific policy plans to reduce poverty. Following the 2008 crisis, the removal of structural performance criteria also supports the notion that the Fund has adopted a less disciplinary development model.

Robinson and Rückert maintain that IMF post Washington Consensus reforms are tied to a broader and conscious effort by an increasingly concerned TCC wary of potential backlash to the globalist political project. Evidence from Davos meetings held between 1999-2012 demonstrates that members of the WEF expressed deep concern of potential blow back from the Asian crisis and the 2008 crisis and also saw these crises as potential threats to the contemporary world order. Recommendations to manage globalizing capitalism that emerged from the WEF through the post Washington Consensus period mirror those found in IMF LIC reform. For example, the general consensus coming out of Davos following the 2008 crisis was the need for broad based and coordinated countercyclical fiscal stimulus and a rethinking of New Consensus monetary policy. At the IMF, this need for a Keynesian-inspired response was shared by Managing Director Strauss Kahn, chief economist Oliver Blanchard, and staff, and was implemented in the ECF/RCF/SCF policy reform. IMF staff, however, were broadly dismissive that their policy choices following the crises of the late 1990s and 2008 were driven by broader concerns of global capitalist crisis management. Rather, the shift in the institution toward more pro-poor and Keynesian practices was a practical response to events on the ground in LICs. Further analysis is needed to tease out how LIC staff self-perceptions around the implementation of LIC reform speaks to the broader role the IMF plays in hegemony construction. I examine this dynamic in chapter 6.



## **Chapter 6- Drivers of Change: Explaining IMF LIC Reform in the post Washington Consensus**

This project focuses on five major areas. First, through a comparative case study of IMF LIC reform from 1995 to 2010, it identifies potential variables and mechanisms that drove these instances of policy change. Second, it evaluates if there are any recognizable patterns across these cases of policy reform. And third, it assesses if and how policy reform is interconnected to changing social relations and social forces in the contemporary historical structure. These three areas, covered in chapters 3-5, constitute the empirical component of this project and are first briefly summarized below.

The next two goals of this project revolve around theoretical concerns and constitute the primary focus of this concluding chapter. I first assess the strengths and weaknesses of rationalist, constructivist, and historical structural theory in regard to the study of contemporary IMF LIC reform. I then evaluate the potential and limitations of a research framework focused on IMF change open to use of both positivist and social relational ontologies. Such an approach will not produce one correct answer and suffers at some level from divergent baseline understandings of the social world. I focus specifically on what I see as intractable differences between theoretical frameworks of IO change that conceptually see the social world as made of externally related ‘things’ versus approaches that embrace Marxist-inspired conceptions of dialectic, internal relations. Despite these tensions, I maintain that the complexity of that world and processes of change within it merit space for mainstream and critical ontologies and epistemologies. Future studies of the IMF should explore more fully how diverse paths of inquiry can be effectively used to explain policy reform.

### **Drivers of IMF LIC Change**

From chapter 3, evidence uncovered through the use of principal-agent modeling and sociological organizational theory suggests that a necessary condition for IMF LIC change involves processes of

coalition building between two tiers of actors. Primary actors include the Managing Director, powerful states, and IMF staff. Secondary actors include weak states, NGOs, and the U.S. Congress. In all four cases of LIC policy reform studied, some form of coalition that advocated for reform was formed between two primary actors or a primary actor and a secondary actor. Second, principal-agent theory maintains that increases in preference heterogeneity between powerful states produces conditions that give staff or management greater room to initiate or resist change. Evidence from these cases supports this hypothesis. In the case of the HIPC, for instance, divisions among powerful states gave Managing Director Camdessus and staff leverage to initially block attempts to institutionalize large scale debt relief. While the HIPC was ultimately adopted, Camdessus and the staff were able to water down the scope and depth of debt relief. Third, principal-agent theory also hypothesizes that pressure applied by NGOs on the IMF for policy reform will not be effective if that pressure is directly applied. Rather, if NGOs instead focus on winning over powerful states, the IMF will respond to these proximate principals. While the general consensus among staff and management interviewed was that NGOs played an integral role in IMF's adoption of the HIPC and HIPC II, this project is unable to discern if pressure applied distally or proximately had any more or less causal effect on processes of reform.

In chapter 4, three major hypotheses that draw from conventional constructivist theories of IMF change were identified. First, changes in economic ideas and norms about development impact LIC policy reform. Second, the mechanisms by which ideas and norms change within the IMF revolve around crises of legitimacy. Actors within the Fund are hypothesized to change their framework of thinking around certain policy choices when these frameworks are deemed illegitimate by a critical mass of elites including the economics profession, powerful states, and private market actors. And third,

a rejection of ideas or development norms that fundamentally challenge liberal market solutions to LIC issues is unexpected.

The evidence derived from a constructivist study of IMF LIC reform is as follows. First, systematic crises appear to play a central role in changing ideas around what is deemed legitimate in policy choices. A stable framework of economic ideas (the New Consensus) constituted what was considered appropriate monetary and fiscal policy from the early 1980s until the 2008 global financial crisis. The 2008 crisis delegitimized ideas and policy recommendations of the New Consensus among development economists and IMF staff. This opened up ideational space for more traditional Keynesian themes to emerge in IMF LIC policy and helped catalyze the replacement of the PRGF with the ECF/RCF/SCF framework. The Asian crisis of the late 1990s led to a reevaluation of role in the state in its relation to market efficiency, growth, and development. Here, in reaction to the policy positions of the Washington Consensus, emphasis on poverty reduction and investment in human capital were reflected in the replacement of the SAF/ESAF with the PRGF and the introduction of PRSPs. The Asian crisis and the 2008 crisis, however, did not challenge more intractable ideas deeply embedded in institutional common sense. Despite the turmoil of the late 1990s and 2008, confidence in free markets and aversion to large scale and coordinated redistribution remains firmly entrenched in IMF thinking. As of 2014, LICs are advised to avoid protectionism, over or undervalued exchange rates, subsidies, redistributive tax arrangements, and large scale entitlement programs.

In chapter 5, use of a critical framework focused on the post Washington Consensus period invoked the concept of “inclusive neoliberalism” to study contemporary IMF LIC reform. Global elites, increasingly conscious of the fallout of economic crises and resistance to globalization, have embraced

strategies designed to build long term support for the economic and political project of transnationalizing capitalism. IMF post Washington Consensus reforms thus are one expression of these efforts. Inclusivity in this context has two dimensions: shifts in thinking embedded in new policy positions and processes of how the policy positions are implemented. In regard to the latter, Fund policy documents and interviews of IMF staff and management demonstrate that the Fund consciously shifted the manner in which its policy initiatives were implemented to increase buy in from LICs. Along with a focus on participation through the PRSPs, this move away from top down approaches has also included the removal of structural performance criteria and increased LIC NGO participation in formal Fund events.

In regard to the nature of the policy shifts themselves, the shift toward poverty reduction and “pro-poor” policies in the post Washington Consensus period has been framed as something best achieved through maintenance of market efficient processes. In this sense, this study verifies claims put forth by Gramscian scholars that a central component of IMF LIC policy choices remains firmly entrenched in neo-classical aversion to market distortive policies. The major ideational shift that has happened in the post Washington Consensus period is support of countercyclical, expansionary fiscal and monetary policy. This move toward more Keynesian practices through the adoption of the ECF/RCF/SCF is seen by the majority of LIC staff interviewed as a practical response to economic downturn rather than a reaction to a broader crisis in capitalism. This interpretation by Fund staff as to why the IMF shifted policy direction, however, stood in contrast to the discourse seen in elitist forums including the Davos Annual Meetings of the World Economic Forum. Here, individuals clearly identified that the governance of globalization required substantive reforms to make capitalism work for the world’s poor majority.

In sum, while this study is unable to report that there is one thing that explains LIC policy reform, the process of testing hypotheses from three distinct ontologies uncovers potential causal variables and mechanisms associated with contemporary IMF LIC reform. I also maintain that each framework offers a reasonable way of looking at social reality and also offers a plausible causal story concerning why the Fund shifts policy position. In this sense, the spirit of this project and conclusions reached about potential future research open to multiple ontologies falls in line with recent calls for “analytic eclecticism” in middle range IR analysis. As outlined by Rudra Sil and Peter Katzenstein:

Analytical eclecticism...trains its sights on connections and interactions among a wide range of causal forces normally analyzed in isolation from one another. This does not guarantee consensus on forecasts or prescriptions that can assist policymakers and lay actors. It does, however, encourage a wider, more open-ended conversation about how the different causal forces identified by proponents of different paradigms might coexist as part of a more complex, yet useable analytic framework that helps in making sense of concrete social phenomena.<sup>548</sup>

In this spirit, I turn to an assessment of strengths and tradeoffs of rationalist, constructivist, and historical structural approaches used in chapters 3-5. I then explore the potential and limitations of moving forward with a research program open to use of both mainstream and critical theory.

### **Assessing Strengths and Weaknesses of IO Theories of IMF Change**

This project is driven ultimately by normative and practical concerns. While the power of the IMF to shape policy outcomes across the globe is well established, explanation as to why the institution shifts policy direction is not. Given that IMF decisions impact millions of individuals, scholarship that accurately pinpoints dynamics that produce change in the institution is critical to real life outcomes. It is this context that I first assess the strengths and weaknesses of rational, constructivist, and historical structural frameworks.

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<sup>548</sup> Rudra Sil and Peter Katzenstein, *Beyond Paradigms: Analytical Eclecticism in the Study of World Politics*, (London: Palgrave Macmillan, 2010), pp.12-13.

In chapter 3, the question of IMF LIC policy change is approached through application of principal-agent modeling supplemented by components of sociological organizational theory. The primary strength of this approach, as is the case in rational frameworks generally, is that its assumptions take what is a complex reality and simplifies it. It identifies who the major actors are (powerful states, Managing Director, staff) and what drives their behavior around instances of policy reform (shirking, increased preference division among powerful state principals, and aversion to market distortive practices). It therefore has the advantages typical of parsimonious approaches: high predictive capacity and generalizable application. Returning to Cox, the rational approach thus falls clearly into the problem-solving category. As such, application of this approach has the highest potential of producing useable knowledge on how to induce successful reform efforts in the institution. In this project, for example, use of a rationalist framework to compare cases of LIC change highlights that coalition building appears to be a necessary condition to produce policy reform. If future studies more conclusively demonstrate that coalition building is for LIC change, this knowledge can be used toward practical ends by NGOs or internal Fund actors interested in policy reform.

Conventional constructivist studies of IMF policy focus start with the following ontological assumptions. The primary entities that drive IMF behavior are individuals within the institution driven by the “logic of appropriateness.” These individuals seek legitimacy from peers and external actors in regard to economic ideas and policy choices. If a policy choice, economic idea, or development norm is deemed illegitimate by a critical mass of fellow economists, powerful states, or private market actors, change can occur. While this framework recognizes the interrelationship between multilateral institutional actors and broader structural forces and power relations, it argues that every institution

has unique dynamics and that ultimately change comes from within. This approach thus ontologically recognizes a complex social reality, but presents a relatively simple causal story: delegitimization of economic ideas increases the chance for periods of reform. The methodological legwork required to support hypotheses derived from this logic involves process tracing and discourse analysis to establish how individuals think about economic ideas or development norms at time X, if they change at time Y, and if that change in thinking impacts policy reform.

The notion that every institution has its own particular dynamics and culture that must be studied to clarify processes that lead to reform is not a radical one. Yet, this emphasis on institution-specific “change from within” pushed by constructivist IO scholars has fundamentally reshaped how this literature studies multilateral institutions. Process tracing into dynamics of how ideas shape outcome in the IMF, for example, provides stronger empirical support to verify or refute claims concerning its institutional behavior. This method also can uncover new information pertinent to explanations of reform. In chapter 4, for example, drilling down into how the IMF thinks uncovered two levels of ideas that shape IMF LIC policy choices. Market distortive practices, including protectionism, subsidies, and large scale redistribution, remain off limits in the institution. Any policy reform that suggests adoption of these policies as solutions to LIC issues, even after the 2008 crisis, is unexpected. Ideas around appropriate monetary and fiscal policy and policy choices to reduce poverty and inequality through non-distortive mechanisms instead fall within the debatable category.

While the methodological focus on internal micro processes is an important contribution, I argue that constructivist insights into IMF LIC change are limited in two key areas. At the ontological level, constructivists draw from a dialectic approach in presentation of their causal story focused on the role of ideas and social legitimacy in institutional change. Rather than externally related variables, norms,

individual agents, and institutional culture are presented as internally related, ontologically intertwined entities. As outlined by Barnett and Finnemore: “Bureaucratic culture guides action but does not determine it. The rules and routines of a bureaucracy shape bureaucrats’ views of the world, define their social tasks, shape their interests, and orient them in similar way toward the world.”<sup>549</sup>

Organizational and bureaucratic culture, likewise, is conceptualized as constituted and implicitly shaped by these same norms and individuals: “...the relationship between bureaucrats and rules is mutually constitutive and dynamic. Bureaucrats create rules that shape future action, but action, in turn, shapes the evolution and content of rules.”<sup>550</sup> Alexander Wendt, along similar lines, describes the internal relation of structure and agency as follows: “Just as social structures are ontologically dependent upon and therefore constituted by the practices and self-understandings of agents, the causal powers and interests of those agents, in their own turn, are constituted and therefore explained by structures.”<sup>551</sup>

While constructivists present a framework that highlights the constitutive nature of structure and agency, the current emphasis on multilateral institutional change from within contradicts at some level how and where this understanding is applied. Specifically, the trend among constructivist IO scholars involves the analytical separation of the multilateral institution in question from social forces and power relations ‘out there’ as a means to more precisely capture internal dynamics that impact reform. Chwieroth is perhaps the most adamant in this respect as he emphasizes “the role of personnel and internal institutional configurations” rather than a focus on dynamics above or below the IO in question.<sup>552</sup> Momani makes similar arguments: “...social constructivists are not suggesting that

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<sup>549</sup> Barnett and Finnemore, *Rules for the World*, p.19.

<sup>550</sup> *Ibid.*, p.20.

<sup>551</sup> Alexander Wendt, “The Agent-Structure Problem in International Relations Theory,” *International Organization* 41, no.3 (1987), pp.335-370 at p.359.

<sup>552</sup> Chwieroth, “Organizational Change “From Within.” Exploring the World Bank’ Early Lending Practices,” p.491.



international organizations are closed-systems where an organization is argued to be self-contained and independent of power considerations in the international system... Nevertheless, international organizations are also bureaucratic entities with their own internalized sets of norms, ideologies, and cultures that need to be considered when studying their behavior and responses to change.”<sup>553</sup>

The analytical and methodological practice of bracketing off processes that occur within the Fund highlights further the tradeoffs of parsimonious and complex analysis. Along with the rationalist approach in chapter 3, the relative simplicity of the constructivist approach in chapter 4 allows us to cut through the multiple and often contradictory layers of social reality, identify key potential causal variables, and test if patterns uncovered can be applied in a predictive capacity. However, this framework conceptually is unable to engage with how and why particular processes of ideational change, crises, and processes of legitimization are interrelated with broader shifts in social structures and power relations unique to the post Washington Consensus period. If applied on its own terms, for example, the constructivist approach would simply ignore how factors tied to the rise of transnationalizing capitalism and the crises therein have impacted how economic ideas and policy choices gain or lose legitimacy.

A historical structural framework focused on IMF LIC change approaches the phenomenon from a fundamentally different ontological and epistemological position rather than rationalist and conventional constructivist frameworks. As such, the nature of the questions being asked and answers to these questions provide insights that mainstream IO approaches leave unexamined. I highlight three unique contributions of historical structural approaches to the study of IMF change that are explicitly tied to its social relational understanding of the world. First, it introduces a causal story that sees

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<sup>553</sup> Momani, “Limits of Streamlining Fund Conditionality: The International Monetary Fund’s Organizational Culture,” p.146.

processes of contemporary Fund policy change as dialectically related to the multiple and often contradictory dynamics embedded in the transnationalization of capitalist social relations. The Fund, and capitalism for that matter, are not “things” that stand separate from each other. Rather, they are understood to be internally related components of a broader social totality.<sup>554</sup> In this sense, explaining IMF change thus also involves explaining at some level how that change both acts on – and is impacted by – a particular configuration of social forces and power dynamics tied to productive relations.

Second, it recognizes the role that the Fund plays in the production and reproduction of hegemonic or more overtly coercive world orders. This broadens and gives deeper meaning to the notion of legitimacy crisis presented by constructivist IO scholars. Post Washington Consensus IMF reform, for example, is explained in part by the fact that the institution plays a crucial role in managing globalizing capitalist social structures. When that order is under threat, as was seen in the late 1990s and 2008, Fund policy reform should be expected. The policy choices that the reform address, and how it addresses them, is also expected to reflect dynamics and tensions point unique to the historical structure under study.

Third, the social relational roots of historical structural theory provide a unique foundation to evaluate where and why certain ideas have been folded into post Washington Consensus reforms, while others have not, and what that signifies about the contemporary role that the IMF plays in the early 21<sup>st</sup>

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<sup>554</sup>Rupert, drawing from Carol Gould, explain the difference between internally and externally related understanding as follows: “...an internal relation is one in which the inter-related entities take their meaning from (or are constituted within) their relation, and are not unintelligible (or non-existent) outside of the context of that relation....Carol Gould contrasts these with external relations, “in which each *relatum* is taken as a separate self-subsistent entity, which exists apart from the relation and appears to be totally independent of it.”” Rupert, *Producing Hegemony: The Politics of Mass Production and American Global Power*, p. 210, footnote 3.

century world order. As uncovered in chapter 4, one prominent shift in the post Washington Consensus period is acceptance of Keynesian inspired countercyclical fiscal and monetary policy response since 2008. Combined with a focus on pro-poor participatory policies introduced after the Asian crisis of the late 1990s, this represents both a substantive and procedural shift in IMF thinking. As I developed above in Chapter 5, Craig and Porter invoke Polyani's conception of double movement in their explanation of this phenomenon. Through implementation of inclusive liberal policy reforms for some of the world's poorest societies, the Fund and other multilateral institutions undermine a potential backlash ( second movement) that would more fundamentally challenge market based development (first movement) on a broader scale.

Not surprisingly, IMF staff and Executive Directors interviewed for this project did not share this understanding as to why the institution implemented post Washington Consensus reforms. They see themselves as practical, non-ideological technocrats who simply responded to the changing facts on the ground and shifted their policy positions accordingly. This framing of post Washington Consensus policy decisions as merely technocratic tinkering while Rome burned is curious indeed. As developed in chapter 6, the Marxist and Gramscian roots of a historical structural framework is uniquely suited to explore why a technocratic self- understanding remains at the core of IMF thinking around policy reform. It also may provide clues as to why that identity is essential to how the Fund participates in (re)building hegemony in the contemporary historical structure.

Briefly introduced here, Marx recognized that the historical development of capitalism and capitalist social relations and modes of surplus value extraction requires that the realm of production be conceptualized as a distinctly economic space free of – and externally related to – that of the

political.<sup>555</sup> This framing has embedded in collective common sense a myth that there exists a separate and natural world of economics with its own laws and logic. Marx argued that this creation of a seeming apolitical economic sphere in capitalist social relations is implicitly a political act as it disguises at some level the power relations that produce the conditions necessary for market based exploitation and subsequent human alienation.<sup>556</sup> This separation of the economic from the political also is integral to the separation of public/state from private/civil society.<sup>557</sup> Civil society is the apolitical economic space where individual's right to private property and pursuit of selfish interest is expressed. The state, in contrast, is the public space where one can "do" politics.<sup>558</sup>

Applied to our concerns here, we can see that the self-identification of Fund LIC staff as rational technocrats rather than ideologically and politically motivated individuals reinforces in broad terms the separation of the economic and the political. In so doing, the IMF plays a central role in the reproduction of contemporary capitalist social relations that are increasingly transnational in scope. This understanding also can be applied to explaining the seeming contradictions that several IMF staff interviewed for this project articulated. While recognizing that IMF policy and market based

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<sup>555</sup> In pre capitalist societies, the concept of economy as separate from other components of society did not exist. Feudal ruling classes, for example, used directly coercive means to extract surplus from producers who had direct possession of the means of production. As summarized by Rupert, with the emergence of capitalism, labor is simultaneously freed from direct coercion and separated from the means of production. In order to survive, labor "must now enter into an "economic" relationship with capital in order to secure the means of physical survival. . . . Surplus labor is now extracted from the producer through the purchase of their labor power in the market (and its subsequent employment in the labor process which is controlled and directed by the capitalist class, owing to their ownership the means of production). No explicitly political coercion need enter directly into capitalist exploitation of labor, for it appears as a simple exchange of commodities in the market: labor-power is exchanged for a wage." The power and exploitation of capital over labor thus remains at some level hidden from everyday view in the apolitical economic sphere that runs on 'natural' laws. Coercive power instead is more explicitly expressed in the form of the capitalist state and "appears as law and order enforced in the public interest." See Rupert, *Producing Hegemony, The Politics of Mass Production and American Global Power*, pp.21-22.

<sup>556</sup> Alienation in capitalism takes on myriad forms. Workers, due to the fact that must sell their labor power to capitalists for survival, are estranged from potentially fulfilling potentials of productive activity, both from themselves and with others, and even from nature itself. *Ibid.*, p.20.

<sup>557</sup> Paul Thomas, *Alien Politics Marxist State Theory Retrieved* (New York: Routledge, 1994), x-xi.

<sup>558</sup> The capitalist state, however, can't ultimately serve as a vector to overcome alienation. Its existence and survival is tied to maintaining the myth of dualistic separation of the economic and the political.

development more broadly need to work for the poor, the boundaries of what is open for debate does not include policies that challenge deep held beliefs in market efficiency. Following the logic of Marx, this makes sense, as debating the efficacy of market distortive policies would bring “politics” into the arena that liberal market economists argue don’t belong and potentially could open up more radical challenges to the current historical structure. We should therefore expect that hegemony construction in the post Washington Consensus will be most successful if themes of poverty reduction, lowering inequality, and pro-poor policies in general remain framed as technocratic problems.

In sum, use of three distinct theoretical traditions provides insights into different components of social reality that inform and drive IMF LIC reform. Taken as an aggregate study of IMF reform, we perhaps begin to overcome the common tradeoffs of parsimony versus complexity. More parsimonious frameworks uncover specific mechanics of policy reform that are unique to IMF and can be used by current policy makers and activists to shape future policy reform. These mechanisms of change, however, are ultimately interrelated to broader social forces and power relations elucidated by historical structural analysis. While the use of multiple ontologies produces greater knowledge in this project, there are some tensions inherent in an approach open to the use of positivist and critical relational theory that must be further explored before we can simply embrace it as viable option for future research.

### **Squaring a Circle? Problem-Solving and Critical Theories of IMF LIC change.**

Robert Cox’s framing of problem-solving versus critical theory sets the foundation to assess if an approach open to use of both of these frameworks is ultimately a workable or productive enterprise. As is often quoted, for Cox, “Theory is always *for* someone and *for* some purpose.” As is also the case when debating major ontological differences and purposes of political science, Cox’s

differentiation between problem-solving theory and critical theory highlights in broad terms some of the major tensions that a research program open to rationalist, constructivist, and historical structural frameworks must address. Problem-solving theory, as used in chapters 3 and 4, "...takes the world as it finds it, with the prevailing social and power relationships and the institutions into which they organized as the given framework for action." Critical theory, in contrast, begins from a more overtly normative and radical position. It is critical because it "does not take institutions and social power relations for granted." Through systematic analysis of historical processes, it serves as roadmap for possible transformative change: "In this way critical theory can be a guide for strategic action for bringing about an alternative order, whereas problem-solving theory is a guide to tactical actions which, intended or unintended, sustain the existing order."<sup>559</sup>

Given this understanding, a major "elephant in the room" that emerges with an approach sympathetic to components of problem-solving and Marxist-inspired historical structural analysis is that the latter ultimately finds the ontological and epistemological position of problem-solving approaches as a mythology of sorts, and one that potentially blocks transformative social change. For critical theorists, the treatment of social reality as one where you have atomistic social objects, externally related and "out there" acting on each other is a clear expression of subject-object duality that has evolved with capitalist social relations. If we are examining the IMF through a lens that reinforces these concepts, do we at some level reinforce reification of social reality? And if so, doesn't that undermine our ability to systematically examine often unobservable power relationships that reinforce particular outcomes that undermine transformative possibilities?

There are therefore several ways one can deal with what appears to be an unresolvable tension between critical and problem-solving approach. First, we can reject attempts to bridge the gap and

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<sup>559</sup> Cox, "Social Forces, States, and World Orders: Beyond International Relations Theory

return to more paradigmatically separate positions. Second, we can ignore the normative “elephant in the room” and focus only on the particular strengths and insights that both problem-solving and historical structural approaches bring to the table. I reject both of these. In regard to the former, this project demonstrates that problem-solving and critical approaches focused on the phenomenon of IMF LIC policy change produce more knowledge, and I offer more high quality knowledge about that phenomenon than if we looked at it only through a mainstream or critical lens. In this sense, I thus find common ground with the growing popularity of the analytical eclectic approach mentioned above which prioritizes knowledge construction over sometimes needless paradigmatic divisions.

In regard to the latter, it certainly would be easier at some level to neuter the normative concerns of historical structural theory and focus only on how it empirically supplements the findings of positivist frameworks. This, however, feels intellectually dishonest and may ultimately undermine the strengths of research open to the use of both mainstream and critical approaches. I advocate for a third possibility as follows. First, a question or concern is raised to be studied. Second, a case is made as to why use of mainstream and historical structural theory is well suited for the question under study. Third, when introduced, each framework more explicitly lays out its normative position and understanding of the world, identifies potential limitations born from this understanding, and then moves forward in full embrace of that position in looking at the phenomenon under study. Historical structural theory, for its part, should be presented and understood as a radical critique. However, it also should be noted that it doesn’t have a monopoly on the politics of transformation, nor does use of social relational ontology in any way exhaust all the possible ways that political scientists can produce a future world better than this one. Problem-solving theory, for its part, should also clearly frame the parameters of its strengths and weaknesses. As outlined by Cox, it should make explicit that it is best suited for teasing out patterns within a given historical structure and that it is less well suited in

explaining how the phenomenon under study is tied to broader and deeper social forces or periods of historical structural change. It should also be recognized that despite notions of objectivity, the ontology and epistemology upon which positivist approaches are built also have normative qualities. Once respective strengths and weaknesses are out of the closet, each theoretical framework on its own terms should look at the question under consideration. It is through this process that we stay intellectually honest to different understandings of politics, and then use those different understandings to produce a better world.

### **Next Steps**

In conclusion, I highlight limitations of this project and several next steps. While evidence from the cases provides new insights into dynamics of past cases of LIC policy reform, several limitations of this study necessitate further development. Specific to chapter 3, inclusion and comparison of instances where Fund LIC policy reform did not occur in future positivist-oriented research would strengthen the potential predictive capacity around the mechanics of IMF reform. This could include examination of the roughly ten years span between the PRGF and ECF/RCF/SCF where no formal LIC policy reform was implemented. In chapter 4, one area that needs more examination is how hiring practices at the Fund could change normative positions. In chapter 5, a focus on the World Economic Forum as *the* prominent voice of global elites is a reasonable assertion. However, analysis of other elite forums in regard to how they have reacted to the past decade and a half of capitalist crisis and popular backlash would more forcefully support or refute notions that the TCC is a self-conscious group that collectively has agency in shaping outcomes in multilateral institutions, including the IMF. Finally, further analysis in regard to the benefits and limitations of approaches to IMF LIC change that



employs multiple ontological frameworks is in order. One possible way to evaluate the effectiveness of such an approach would be to apply it to other cases of multilateral institutional reform.

# APPENDIX 1: Interview Questions



MAXWELL SCHOOL OF CITIZENSHIP AND PUBLIC AFFAIRS  
COLLEGE OF ARTS AND SCIENCES  
DEPARTMENT OF POLITICAL SCIENCE

## I. General Background

What is your position in the Fund?

What specific experience do you have in regards to Low Income Countries (LICs)?

What do you see as the Fund's appropriate role in LICs?

## II. Policy Paradigms and LICs

Historically, the Fund has been resistant to call itself a development institution. Where do you fall on this? Is the Fund in the development business? If so, is this a good thing?

Given that the Fund is staffed primarily by economists, scholars focused on the internal culture of the Fund argue that its thinking is often a reflection of values and worldviews seen in the broader economics field. Does Fund thinking and changes therein reflect broader trends seen 'out there' in the economics discipline? Or is the Fund more prone to produce its own internal thinking regarding policy choices?

From your perspective, has the Fund witnessed any significant shifts in its institutional 'thinking' during your tenure (i.e. Hayekian vs Keynesian thinking). If so, when did these occur and how did they manifest themselves in policy outcomes regarding LICs?

Since the 1982 Debt Crises, the Fund has introduced three concessionary lending programs for LICs: The SAF/ESAF in the mid 1980s, the PRGF in 1999 and the recent replacement of the PRGF with the ECF/RCF/SCF in 2010. Where any of these policy shifts representative of 'deeper' institutional change at the Fund? Why or why not?

## III. LIC Policy Determinants

The literature points to various variables that shape Fund policy choices. Please comment on how significant each of the following are in shaping LIC policy choices:

- a) Powerful states, particularly the United States
- b) Recipient states
- c) IMF management
- d) Managing Director
- e) IMF staff
- f) the World Bank

g) NGOs

h) economic crises

i) public opinion

other ?

Looking at the variables above in a comparative perspective, which have become more and less important in shaping LIC policy outcomes at the Fund during your tenure?

Several IMF scholars argue that Fund programs focused on debt relief and development issues for LICs have been initiated from management and /or pressure from member states rather than from staff. Would you agree with this assessment?

How much input do LIC member states have in shaping policy choices?

#### IV. Case 1-Introduction of ECF/RCF/ SCF

What do you see as the primary factors that led to elimination of the PRGF and establishment of the ECF/RCF/ and SCF in 2010?

Who were the primary actors within the Fund who pushed for the ECF framework?

How has the shift from the PRGF framework to the ECF been received by staff working with LICs?

Can one identify any significant institutional change in thinking about LICs with the introduction of the ECF? Why or why not?

Any other comments or thoughts in regard to introduction and implementation of ECF framework?

#### V. Case 2-Introduction of PRGF/PSRPs/ HIPC II/MDRI

What do you see as the primary factors that led to elimination of the ESAF and establishment of the PRGF in 1999?

Who were the primary actors within the Fund who pushed for the PRGF?

How was the shift from the ESAF/SAF framework to the PRGF received by staff working with LICs?

What explains the emergence of a “pro-poor”, participatory framework seen under PRGF?

Who pushed for the establishment of the Policy Support Instrument?

There is a consensus in much of the political science literature looking at this period that the Fund adopted pro-poor positions and policy jargon to accommodate growing external criticism and protest movements in late 1990s. Is this accurate? Why or why not?

Any other comments or thoughts in regard to introduction and implementation of PRGF framework?

## APPENDIX 2: List of Interviews and Archival Material

International Monetary Fund, Washington DC.

<u>Date</u>	<u>Position</u>
06.13.11	Director, External Relations Department
06.13.11	Assistant Director, Research Department
06.13.11	Deputy Director, Africa Department
06.14.11	Deputy Director, Strategy, Policy and Review Department
06.14.11	Division Chief, Strategy, Policy, and Review Department
06.15.11	Senior Advisor, Middle East and Central Asia Department
09.19.11	Senior Advisor, Africa Department
09.20.11	Advisor, Western Hemisphere Department
09.20.11	Special IMF Representative to the United Nations
09.21.11	Deputy Division Chief, Africa Department
09.26.11	Assistant Director, Asia and Pacific Department
01.24.12	United States Executive Director
01.24.12	Nordic and Baltic Alternative Executive Director
01.25.12	Adviser to the UK Executive Director
01.26.12	Sub-Saharan Africa Executive Director

### Phone and E-mail Interviews

<u>Date</u>	<u>Position</u>
01.28.12	French Executive Director
02.24.12	Former Sub-Saharan Africa Executive Director
06.29.12	Deputy Director, Strategy, Policy and Review Department

### Archives: International Monetary Fund Washington, D.C.

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- World Economic Forum, *New Beginnings: Making a Difference: Report of the Annual Meeting 2000 of the World Economic Forum* (Geneva: World Economic Forum, 2000).
- World Economic Forum, *World Economic Forum Annual Report 2004/2005* (Geneva: World Economic Forum, 2005).
- World Economic Forum, *Shaping the Post-Crisis World: Report of the Annual Meeting 2009 of the World Economic Forum* (Geneva: World Economic Forum, 2009).

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## EDUCATION

### Ph.D., Political Science, June 2014, Syracuse University

Subfields: International Relations and Comparative Politics  
Specializations: International Monetary Fund; Politics of Globalization;  
Gramscian IPE; Politics of the post Washington Consensus;  
Latin American Politics

#### Dissertation (defended: May 20, 2014):

*Drivers of Change: Explaining IMF Low-Income Country Reform in the post Washington Consensus*

Committee: Mark Rupert (Chair), Jon Hanson, Matt Cleary, Audie Klotz, and Bessma Momani (University of Waterloo)

**Masters of Arts, Political Science, Syracuse University** **2007**

**Masters of Arts, International Political Economy, University of Birmingham (UK)** **2005**

**Bachelors of Science, Biology, University of Maine** **1992**

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## PUBLICATIONS

“Coalitions of Change: Coalitions of Change: Explaining IMF Low Income Country Policy Reform in the post Washington Consensus,” *Journal of International Relations and Development*, forthcoming Fall 2014.

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## TEACHING EXPERIENCE

**Saint Joseph's College of Maine, Standish Maine** **2012-2014**

**Assistant Professor**  
Comparative Politics  
Globalization  
International Relations

**University of Maine, Orono, Maine**

**Adjunct Instructor** **2008-2012**

International Relations  
International Political Economy  
Globalization  
Comparative Latin American Politics

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**CONFERENCE PAPER PRESENTATIONS and WORKING PAPERS**

**Rethinking the Keynesian Revival: The IMF and post -2008 Low Income Country Policy Reform** International Studies Association; Toronto, March 2014.

**Theorizing IMF and World Bank Organizational Cultures and their Effects on Collaborative Policy Initiatives** (co-authored with Bessma Momani) International Studies Association; Toronto, March 2014.

**The Role of the Managing Director in Low Income Country Policy Reform** International Studies Association; San Francisco, California, April 2013.

**A Keynesian Turn? IMF and LICs in the post-2008 era** International Studies Association; San Diego, California, April 2012.

**What Explains IMF Policy Shifts Toward Low Income States?** American Political Science Association; Seattle, Washington, September 2011.

**Beyond the Rationalist-Constructivist Synthesis? Evaluating Contemporary Explanatory Frameworks of IMF and World Bank Policy Shifts** Midwest Political Science Association; Chicago, Illinois, April 2010.

**Do Conceptions of Globalization Reinforce Regressive Taxation Policies in Contemporary Latin America?** Midwest Political Science Association; Chicago, Illinois, April 2009.

**The New Dependency? Predicting Redistributive Effects of Social Spending and Taxation Policies in Former ISI States** Midwest Political Science Association; Chicago, Illinois, April 2009.

**Transformative Politics or *Transformismo*? Latin America's Populist Challenge to Disciplinary Neoliberalism** International Studies Association; San Francisco, California, March 2008

**The Construction of Constraint? Globalization and the New Left in Latin America** Latin American Studies Association; Montréal, Canada, September 2007

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**GRANTS and RESEARCH AWARDS**

*Saint Joseph's College of Maine*  
**Junior Faculty Research Award**

**2014-2015**

*International Monetary Fund/ World Bank*  
**2011 IMF/World Bank Annual Meeting Academic Fellowship**

**2011**

*University of Maine*  
**Course Development Grant**

**2009-2010**

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**RESEARCH SKILLS**

Training in quantitative and qualitative methods; experience with semi-structured interviews, process-tracing, discourse analysis, and archival research.

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**LANGUAGES**

**German** (Basic Fluency)

**Spanish** (Rudimentary)

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