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Volume 16
Issue 1 *Winter 1983*

Article 1

1983

The Recent Shift in United States Policies toward the International Monetary Fund and the World Bank

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Polly R. Allen, The Recent Shift in United States Policies toward the International Monetary Fund and the World Bank, 16 *Vanderbilt Law Review* 1 (2021)
Available at: https://scholarship.law.vanderbilt.edu/vjtl/vol16/iss1/1

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Vanderbilt Journal of Transnational Law

VOLUME 16 WINTER 1983 NUMBER 1

THE RECENT SHIFT IN UNITED STATES POLICIES TOWARD THE INTERNATIONAL MONETARY FUND AND THE WORLD BANK

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I. INTRODUCTION

Today's world economy is characterized by recession, reduced growth in international trade, high oil prices, and high interest rates. Although industrial countries face these problems and the problems often originate in the industrial countries, the developing countries that are not major oil exporters are encountering

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particularly serious difficulties. The external pressures on these developing countries, combined with their problems of structure and policy, are causing severely reduced rates of growth, higher rates of inflation, increasing problems with balances of payments, and growing foreign debt. Because many of these difficulties arise outside these countries' economies, and because the solutions often require long-term structural adjustments, most industrial and developing countries recognize the need for expanded lending to the developing countries by the International Monetary Fund (IMF or Fund) and the International Bank for Reconstruction and Development, commonly known as the World Bank.

The United States, by contrast, appears to be reducing its traditionally strong support for these institutions. President Reagan's opening address at the annual meeting of the IMF in 1981 was notable not for its general assertions of continued support, but for its emphasis on the need for developing countries to adopt the policies necessary to help themselves.[1] A major topic of discussion at the annual meeting of the IMF in September 1982 was the need to increase members' quota subscriptions, which are the basic source of money for the Fund's operations. The United States delegation opposed the "substantial" increase of quotas supported by most other countries.[2] Perhaps the most telling manifestation of the United States declining support for the international lending institutions is the failure to honor its financial commitment to the International Development Association (IDA), the arm of the World Bank responsible for lending on concessionary terms to countries in need of aid. Although the United States finally has promised to pay the balance of its three-year commitment for 1981-1983 to the IDA during the fourth year,[3] the contribution is not yet assured. This delay has reduced IDA's ability to lend substantially.

A summary of the current world economic situation, particularly the predicament of the developing countries, and a discussion of the purposes, financing provisions, and evolving policies of the IMF and the World Bank, can provide background for evalu-

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1. *See* Address by President Reagan, Summary Proceedings of the Annual Meetings of the International Monetary Fund 4 (1981) [hereinafter cited as Reagan].

2. IMF SURVEY, Sept. 20, 1982, at 294.

3. Martin, *Views Clash on World Bank Agency*, N.Y. Times, Sept. 8, 1982, at D6, col. 1.

ating this apparent shift in United States policy and considering its economic implications.

II. Developments in the World Economy, 1979-1982

Unemployment, inflation, and high interest rates present problems to almost all countries, but the nature and extent of the difficulties vary widely. Nonetheless, certain groups of countries have many factors in common. For purposes of economic analysis, the IMF puts countries into three categories: *industrial countries,* including eighteen countries in Europe and North America plus Japan, Australia, and New Zealand; *oil-exporting developing countries,* those twelve countries in which exports of oil make up at least two-thirds of their total exports and a minimum of 100 million barrels a year; and the remaining *non-oil developing countries.*[4] Considerable differences among countries occur within each of these three groups. The divergences among the non-oil developing countries are large enough to warrant sub-categories: the twelve *net oil exporters,* whose oil exports are not large enough for categorization as oil-exporting countries; *major exporters of manufactured goods,* of which there are ten; the *middle-income countries,* exporting mainly primary commodities; and the group of forty *low-income countries,* whose per capita production in 1978 was no more than 350 dollars.[5]

The industrial countries, particularly the United States, the Federal Republic of Germany, and the United Kingdom, have experienced slow growth rates and high unemployment rates since 1980. The blame for this recession is placed mainly on the increases in oil prices during 1979-1980, increasing inflation rates, and, in several of these countries, restrictive financial policies directed toward reducing inflation. The rates of inflation in several countries have decreased in the past year, but the costs in unemployment and lost output have been high. The economic performance in the industrial countries has been hampered further by high and fluctuating interest rates which have resulted from a combination of restrictive financial policies, expansionary fiscal policies, and expectations of continued high rates of inflation. Moreover, substantial differences in the economic structures and

4. These categories do not include the Soviet Union and several other socialist countries that are not members of the IMF. International Monetary Fund, World Economic Outlook 140 (1982) [hereinafter cited as IMF Outlook].

5. *Id.*

policies of the industrial countries have produced wide fluctuations in currency exchange rates.

The oil-exporting developing countries have experienced declines in output and export revenue during the past two years. The price of oil increased 170 percent from the end of 1978 to early 1981[6] when it reached a peak of thirty-five dollars per barrel. Since early 1981 demand for oil in the industrial countries has been falling. Total world oil consumption fell by five percent per year in 1980 and 1981 and is continuing to fall in 1982 after rising about two percent per year for the preceding six years.[7] The industrial countries account for almost all of the decline. This downturn was caused by rising oil prices during 1979-1980, the world recession, and substitution of other energy sources and conservation of oil in response to the 1974 increase of oil prices. In spite of the cutback in demand, the price of oil fell only slightly in 1981-1982 and is expected to remain constant in real terms for several years; that is, oil prices should just about keep pace with the general rate of inflation.[8]

These developments in the industrial and oil-exporting countries have added to the economic problems of the oil-importing developing countries. Perhaps most importantly, the world recession has reduced demand for their exports, thereby cutting their rates of growth and reducing their export revenues. Moreover, the increase in oil prices has added enormously to their import bills. The oil-importing developing countries no longer have many alternatives for reducing oil imports without curtailing domestic production or cutting back on basic necessities of life. As a result, these countries reduced oil imports only slightly in the face of the recent rise in price.[9] The rising prices of oil and other imports have been accompanied by falling prices for the goods exported by middle-income primary-producing countries and low-income countries,[10] such that their terms of trade (ratio of export prices to import prices) have fallen by ten and twenty percent, respectively, since 1978.[11]

The high levels of world interest rates have created two kinds

6. *Id.* at 131.
7. *Id.* at 127.
8. *Id.* at 132.
9. *Id.* at 163.
10. *Id.* at 59.
11. *Id.*

of problems for the non-oil developing countries. First, they have been forced to raise their interest rates to prevent capital from moving abroad. The high cost of borrowing, either domestically or internationally, makes many of these countries' potential investment projects unprofitable and cuts deeply into their economic development. Second, these countries have borrowed heavily from foreign sources—largely commercial banks—at variable rates of interest.[12] The increase of interest rates in the last year and a half greatly increased the interest payments on their existing debt and made new borrowing expensive. Furthermore, an increasing proportion of their borrowing has been short-term and requires early repayment.[13] Interest payments to foreigners by the non-oil developing countries increased from five and one-half percent of exports in 1978 to eight and one-half percent in 1981. Total debt service, including both interest payments and repayments of principal, rose to almost one-fifth of their export revenues.[14]

For the oil-importing developing countries, decreases in the volume and prices of exports, increases in the prices of oil and other imports, and rising debt-service payments over the last three years have enlarged their deficits on current account.[15] Even the net oil exporters, who have benefited to some degree from higher oil prices, suffered a sharply reduced volume of exports and experienced export revenues far below what they expected. At the same time, their debt-service payments have escalated sharply because these countries have been among the world's heaviest borrowers. In 1978 the non-oil developing countries had a combined deficit on current account of $39 billion.[16] In the following three years, this combined deficit jumped to $59 billion, $86 billion, and $99 billion, with a predicted deficit of $97 billion in 1982.[17] The IMF predicts that, because of their inability to reduce imports of oil and other goods, difficulties of increasing exports,

12. *Id.* at 64.

13. *Id.*

14. *Id.* at 65.

15. *Id.* at 58-59. The current account of a country's international balance of payments includes all trade in goods and services, payments of interest and dividends, and gifts, grants, and other transfers. A deficit on current account must be financed by payments of international reserves or by borrowing from foreigners. Conversely, a surplus on current account is matched by payments from foreigners of international reserves or by lending to foreigners.

16. *Id.* at 166.

17. *Id.*

and rising debt-service burdens, the non-oil developing countries will face even larger deficits by 1986.[18]

The industrial countries have much more flexibility for adjusting imbalances on current account than the non-oil developing countries. As a result of the recent increase in oil prices, the combined current account of the oil exporting countries jumped from being nearly balanced in 1978 to a surplus of $115 billion in 1980.[19] Almost one-third of this surplus was reflected in deficits of the industrial countries.[20] The decline in oil consumption in the past two years should bring the 1982 surplus for the oil-exporting countries down to $25 billion.[21] The industrial countries will move from a deficit of $45 billion in 1980 to a surplus of $11 billion in 1982.[22] Over the next four years, the predicted worsening of the deficits of the non-oil developing countries is expected to be matched by increasing surpluses for the industrial countries.

The deficits of the non-oil developing countries do not fully measure the extent of their problems with external payments. Some of these countries have had to adopt restrictive domestic policies and impose curbs on imports because of their inability to finance the deficits they otherwise would have on current account, resulting in further production cutbacks and a slowing of economic development.

For every dollar of deficit in one country's current account there must be a dollar of surplus in another country's current account. Because the present and projected deficits of the non-oil developing countries reflect, in large part, economic conditions in the rest of the world, it is unrealistic to expect correction of these imbalances entirely from the deficit countries. Further, balanced current accounts should not necessarily be a goal. Countries with excess capital to invest, usually industrial and oil-exporting countries, should lend to countries with investment opportunities and shortages of capital, which are usually non-oil developing countries.

Problems occur when the structural factors that determine cur-

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18. *Id.* at 21-22, 174. These projections are based on the assumptions of no changes in oil prices, in trade restrictiveness of industrial counties, or in official development assistance.

19. *Id.* at 160.

20. *Id.* at 159-60.

21. *Id.* at 160.

22. *Id.* at 159.

rent accounts produce imbalances in these accounts that do not match the desired flow of capital; the surplus countries want to invest, but not always in the deficit countries. This is the situation the world faces in the 1980s. It is important that the non-oil developing countries adjust their current accounts to sustainable levels; that is, to deficits that can be financed by ongoing loans from the surplus countries. By the most optimistic counts, however, making these adjustments without stopping the development process and creating unwarranted hardships will take time and assistance. Both can be gained through a careful expansion of lending by the IMF and the World Bank.

III. LENDING BY THE IMF AND THE WORLD BANK

The IMF and the World Bank are both international institutions that make loans to member countries. The two institutions share many of the same aspirations for the growth and development of their members' economies. Though the IMF and the World Bank often cooperate, the specific purposes of their lending and the means of financing their loans are quite different. The IMF is responsible for overseeing countries' balances of payments and arrangements for exchange rates among currencies.[23] It lends to countries with temporary balance-of-payments problems and helps them bring their external payments into balance.[24] The World Bank is responsible for promoting economic development.[25] It extends long-term loans for specific projects that will contribute to a country's development.[26] The means by which the two organizations obtain resources for lending reflects these differences of purpose.

A. Financing and Conditionality of IMF Loans

Most of the IMF's resources come from the subscriptions of its members. Each member is assigned a quota, based on the size of the country's economy, and each member must deposit an amount equal to its quota with the Fund.[27] One-quarter of this

23. J. RICHARDSON, UNDERSTANDING INTERNATIONAL ECONOMICS: THEORY AND PRACTICE 71 (1980).

24. *A Conversation with Mr. de Larosière,* 19 FIN. & DEV., June 1982 at 4, 6.

25. *Id.*

26. *Id.*

27. J. GOLD, LEGAL AND INSTITUTIONAL ASPECTS OF THE INTERNATIONAL MONETARY SYSTEM: SELECTED ESSAYS 412 (1979) [hereinafter cited as J. GOLD, SE-

contribution is paid in assets other than the member's own currency; this payment originally was made in gold and now, for new members or increases of quotas, is made in foreign currencies or SDRs.[28] The remaining three-quarters may be contributed in the member's currency.[29] These contributions of gold, currencies, and SDRs are the main resources for the IMF's lending.

Strictly speaking, a member having difficulty financing a deficit in its balance of payments does not "borrow" from the IMF. Instead, it purchases from the IMF—with its own currency—other currencies needed to settle its international obligations, with the understanding that the IMF will use that country's currency to repurchase the foreign currencies at a later date.[30] The country pays interest to the IMF on its purchases. These purchase/repurchase agreements are effectively the same as loans and shall be referred to as loans throughout this Article.

The twenty-five percent of a member's quota that it has deposited in gold, foreign currencies, or SDRs is called a "reserve tranche."[31] A member has an automatic right to borrow against its reserve tranche; that is, to make a purchase that will not raise the Fund's holdings of the purchasing country's currency above the country's quota.[32] No conditions are imposed on purchases against the reserve tranche. This unconditional right makes the reserve tranche a legally assured reserve asset for the country.

Beyond the reserve tranche, the member countries may borrow additional amounts up to 100 percent of their quotas.[33] These borrowings are divided into four credit tranches and are not automatic, but are subject to "conditionality" by the Fund.[34] Conditionality means that the IMF will grant loans only if the loans are

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LECTED ESSAYS].

28. *Id.* at 412, 442. Special drawing rights (SDRs) are a new reserve asset, created by the IMF under the provision of the First Amendment to the Articles of Agreement, effective June 28, 1979. The Fund can allocate new SDRs to members or withdraw them by cancellation. Members can use SDRs, under certain limitations, to satisfy their obligations to other countries and to the IMF. *Id.* at 90-94.

29. *Id.* at 412.

30. J. RICHARDSON, *supra* note 23, at 72.

31. J. GOLD, SELECTED ESSAYS, *supra* note 27, at 443.

32. *Id.* at 426-27.

33. J. RICHARDSON, *supra* note 23, at 72. Lending against the credit tranches is the traditional kind of financing by the IMF. Provisions for additional kinds of borrowing have been established, mostly in the mid-1970s.

34. *Id.*

consistent with its policies of promoting adjustment in the balances of payments of its members. In practice, conditional loans by the IMF require that the borrowing country carry out certain measures, specified by the Fund, to reduce its imbalance of payments.

The original Articles of Agreement did not mention conditionality and there was disagreement over whether the Articles gave the Fund the right to impose conditions on members' right to borrow. In the 1940s the United States was contributing almost all the money, and the United States wanted conditions.[35] Consequently, in practice the IMF has always reserved the right to determine under what conditions it shall lend to a country.[36]

The Fund's policies on conditionality evolved gradually. In 1969 the First Amendment to the Articles gave legal standing to the concept of conditionality. The First Amendment did the following: (1) it guaranteed that loans against the reserve tranche, which at that time was the gold tranche, would be unconditional and (2) it prohibited the Fund from extending any of its other resources without a policy of conditionality.[37]

The requirement for imposing conditionality is unquestioned, but the First Amendment does not state what kinds of policies are needed. The IMF requires, as a condition for borrowing against the first credit tranche, that a country have a program that represents reasonable efforts to overcome its balance-of-payments difficulties.[38] To borrow against the upper three credit tranches, the country must provide stronger justification of its efforts; these loans usually are granted under stand-by arrangements whereby the money is disbursed in installments and then only if the country meets certain performance criteria.[39]

The appropriateness of the Fund's conditionality policies has been the subject of much recent controversy. Two of the major issues are how rapidly a country must adjust its balance of payments and how soon the Fund should require repayment of its

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35. S. DELL, ON BEING GRANDMOTHERLY: THE EVOLUTION OF CONDITIONALITY 8-9 (1981).

36. *Id.* at 10.

37. J. GOLD, CONDITIONALITY 8-9 (1979) [hereinafter cited as J. GOLD, CONDITIONALITY].

38. Guitián, *Fund Conditionality and the International Adjustment Process: The Changing Environment of the 1970s,* 18 FIN. & DEV., March 1981, at 8, 9 [hereinafter cited as Guitián, *1970s*].

39. *Id.* at 9.

loans. Under the stand-by arrangements the IMF traditionally limited its commitment to one year—sometimes renewable for a second or third year—and required repayment within three to five years.[40] The use of loans of short duration and maturity assures that the Fund's resources are revolving and capable of being used again to lend to another country with temporary balance-of-payments difficulties.

Since the passage of the First Amendment, only two ways remain for increasing members' unconditional claims on the Fund's resources. One way is to increase the quotas; this involves raising members' subscriptions and expanding the sizes of the unconditional reserve tranche. Quotas are reviewed every five years and have been increased regularly,[41] but not nearly as rapidly as the growth of world trade. The second way is for the IMF to make a new allocation of SDRs. Allocations currently are made in proportion to countries' quotas, with no reference to members' balances of payments or policies.[42]

Subscriptions to the IMF are not its only source of funds; it also may borrow.[43] In the past the IMF has borrowed from member countries to support various kinds of special financing, some of which are discussed below. Increased borrowing, either from member countries or from the private markets, is one possibility for expanding the Fund's resources for future lending. The IMF, however, feels strongly that quotas should continue to be its main source of funds.[44]

B. Financing of World Bank Loans

The World Bank's operations are in many ways similar to those of a commercial bank. It is a profit-making institution that borrows and lends at close to market rates of interest. In several important ways, however, the operations of the World Bank differ from those of commercial banks.[45]

The Bank's equity consists of paid-in capital from the member

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40. *Id.* at 9-10.
41. J. RICHARDSON, *supra* note 23, at 73; Guitián, *1970s, supra* note 38, at 10.
42. J. RICHARDSON, *supra* note 23, at 75.
43. Guitián, *1970s, supra* note 38, at 10.
44. IMF SURVEY, Sept. 20, 1982, at 287.
45. *See* Clausen, *A Financial Appraisal of the Bank,* 19 FIN. & DEV., June 1982, at 6, 8.

countries and retained earnings, in about equal parts.[46] The Bank has never paid dividends to its members, but rather chooses to retain its earnings to support additional lending.[47] An unusual feature of the Bank's capital structure is that its paid-in capital of $4 billion is only one-tenth of its total subscribed capital.[48] The remaining $37 billion of "callable" capital is available from the members,[49] if needed, to protect the bondholders and other creditors of the Bank. The Bank has never called on this capital, and never expects to, but its availability helps to maintain the Bank's high credit rating.

In addition to its equity, the Bank's resources come from borrowing. About thirty percent of the Bank's debt is held by central banks and governments, who hold its obligations as part of their foreign exchange reserves.[50] The remainder is borrowed on private markets all over the world. The Bank assures that its private debt is highly diversified by country, currency, source, maturity, and technique of borrowing.[51] The average maturity of its debt is seven years, all at fixed rates of interest; this provides a match against its medium-and long-term loans, also at fixed rates.[52] By contrast, commercial bank borrowing is primarily short-term and is often matched against variable-rate loans. The ratio of debt to equity for the Bank is four to one, compared with an average of twenty-five to one for commercial banks.[53] In sharp contrast with the commercial banks, the World Bank does not take currency risks on its borrowing.[54]

Approximately one-third of the Bank's assets are held in liquid cash balances.[55] This is an unusually high proportion. These liquid balances have consistently earned profits, being invested at higher returns than the cost of borrowing. They also provide flexibility in the Bank's borrowing. When conditions for borrowing are unfavorable, the Bank can meet its loan commitments by drawing down cash balances.

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46. *Id.* at 9.
47. *Id.*
48. *Id.*
49. *Id.*
50. *Id.*
51. *Id.*
52. *Id.*
53. *Id.*
54. *Id.*
55. *Id.* at 8.

The loans of the World Bank are the reason for its existence. The Bank lends to developing countries at a profitable rate of interest, almost always for specific projects that would not be financed by the private markets. The terms of the loans, while profitable for the Bank, are usually better than those available from the commercial banks because of the Bank's ability to borrow on favorable terms. The World Bank works closely with a country to develop and appraise a project, providing technical assistance and advice. This process takes, on average, more than two years before a project is submitted for loan approval.[56] In part because of the Bank's careful preparation, there has never been a default or loss on a loan.[57]

Some of the low-income developing countries cannot afford to borrow at market terms, even from the World Bank. The projects most needed by these countries—projects in agriculture, power, transportation, and education—often have indirect or long-range returns and will not generate enough income to repay loans extended at market rates. The International Development Association (IDA) is the arm of the World Bank that grants loans for such projects on concessionary terms with lower interest rates and longer maturities than those available in the markets or from the World Bank itself.[58] Some of IDA's borrowers borrow simultaneously from the World Bank. For example, of IDA's three largest borrowers in fiscal 1982, India and Pakistan both borrowed similar amounts from the World Bank,[59] while Bangladesh borrowed solely from IDA.[60] Contributions by some thirty countries provide the funds for concessionary IDA loans.[61]

The Sixth Replenishment of IDA provides for contributions of approximately $12 billion for fiscal years 1981-1983.[62] During the Carter Administration the United States pledged $3.24 billion. Now well into the third fiscal year, the United States has paid only $1.2 billion of this amount.[63] The pro-rata provisions in the Sixth Replenishment Resolution allow the IDA to commit re-

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56. *Id.*
57. *Id.*
58. The World Bank Annual Report 3 (1982) [hereinafter cited as World Bank].
59. *Id.* at 11.
60. *Id.*
61. *Id.* at 15.
62. *Id.*
63. *Id.*

sources from other donors only in the same proportion as the unqualified commitments received from the United States.[64] The delayed contributions from the United States resulted in a twenty-three percent reduction in IDA commitments during fiscal 1982.[65] Whereas IDA loans equaled approximately forty percent of World Bank loans in the preceding three years, in 1982 they equaled only twenty-five percent.[66]

The World Bank, realizing that its funds together with the IDA funds are insufficient to meet the developing countries' borrowing needs, promotes and encourages lending and investments from other sources. The Bank serves as a catalyst for private lending by funding projects, and it takes specific measures to increase private lending. First, the World Bank and IDA have increased their cofinancing of projects with official aid agencies, export credit institutions, and commercial banks.[67] Cofinancing with private banks has become the most important source of the Bank's cofinancing and, in the Bank's view, has the greatest potential for expansion.[68] Second, the International Finance Corporation (IFC) is an affiliate of the World Bank that was established to generate private resources for development on commercial terms.[69] The IFC invests in development projects for which a market approach is preferable, but which would not be undertaken without its participation. The IFC invests in equity, lends, mobilizes other private funds, and provides technical advice and assistance.

The World Bank has been authorized to double its subscribed capital from $40 billion to $80 billion, and will do so over the next four to five years.[70] In 1977 the member countries of the IFC approved a five-fold increase in its capital, which is now almost complete.[71] The area of serious concern is the IDA.

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64. *Id.* at 16.

65. *Id.* at 11.

66. *Id.* at 10.

67. *Id.* at 13-14.

68. *Id.* at 14.

69. Bell, *Promoting Private Investment: The Role of the International Finance Corporation,* 18 FIN. & DEV., Sept. 1981, at 16, 16-17.

70. WORLD BANK, *supra* note 58, at 147.

71. Bell, *supra* note 69, at 17, 19.

IV. CHANGES IN LENDING POLICIES OF THE IMF AND THE WORLD BANK

The IMF, with responsibility for financing temporary deficits in balances of payments, traditionally has focused its attention on macroeconomic variables, particularly the aggregate demand for goods and services.[72] When assisting a country to adjust its balance of payments, the IMF usually recommends or requires as a condition of the loan that the country implement more restrictive monetary and financial policies, reduce budget deficits, and depreciate its currency.[73] These "demand-management" policies reduce the country's demand for goods and services relative to the supply and thus work to bring the balance of payments into equilibrium. Such policies are particularly appropriate when a country's deficit has been caused by overly expansionary domestic policies, an over-valued currency, or a general increase of demand.

Whereas the IMF adopts a macroeconomic perspective, the World Bank traditionally has taken a microeconomic approach, looking at the particular industry or sector in which it is funding a project.[74] The Bank is concerned with efficient allocation of resources within a country and the promotion of growth and development. It furthers these goals by identifying and supporting individual projects, rather than by looking at general economic policies.[75]

Changes in the world economy during the 1970s called into question the traditional approaches of the IMF and the World Bank. The 1974 rise in the price of oil left many developing countries with a choice between large deficits in their external payments, sharp cutbacks of production and consumption, or possibly both. New responses were needed. As a result, the past nine years have constituted a period of experiment and change for both lending institutions.

A. Evolution of IMF Policies in the 1970s

The quadrupling of the price of oil in 1974 created large imbal-

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72. Crockett, *Issues in the Use of Fund Resources*, 19 FIN. & DEV., June 1982, at 10, 10-12.

73. *Id.* at 11-12.

74. Wright, *World Bank Lending for Structural Adjustment*, 17 FIN. & DEV., Sept. 1980, at 20, 22.

75. *Id.* at 21.

ances of payments throughout the world that were much larger than previous imbalances. The traditional means of correcting imbalances were considered unworkable for the following reasons: (1) sharply restrictive policies by countries in deficit would worsen the recession already caused by oil price increases, in some cases creating real hardship and possible social and political instability; (2) the oil-exporting countries with the large surpluses did not have the capacity to absorb or spend the new oil revenues within a short time; and (3) the demand for oil was not very responsive to price changes in the short run, so little could be expected from adding to the relative price change through adjustments of exchange rates. The oil-exporting countries were investing or lending revenues in oil-importing countries, but the distribution of their investments did not match the distribution of deficits on current account.[76] For some countries the only means of financing their deficits was official financing. The alternative was an immediate, wrenching adjustment of their balances of payments, which would have meant increased restrictions on trade and a deepening of the world recession.

The IMF responded to this situation by extending its lending programs in several ways. In 1974 it established an "oil facility"[77] from which it lent, with minimal conditionality, to countries experiencing particularly severe problems financing oil imports. The Fund borrowed resources for these loans from member countries with stronger balances of payments.[78] The oil facility was extended in 1975; the terms of conditionality were slightly tightened because it was becoming apparent that the change in the price of oil would not be reversed.[79] The oil facility ended in March 1976.[80] Altogether approximately $8 billion was loaned through the oil facility;[81] the Fund has repaid about ninety-three percent of this debt.[82] The Fund charged market rates of interest on the

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76. R. Dunn, Jr., Exchange Rates, Payments Adjustments, and OPEC: Why Oil Deficits Persist *passim* (1979).

77. Guitián, *1970s, supra* note 38, at 8.

78. *Id.* at 8-9.

79. *Id.*

80. *Id.* at 9.

81. *Id.*

82. International Monetary Fund Annual Report 115 (1982) [hereinafter cited as IMF Report]. The IMF denominates its borrowing in SDRs. Through the oil facility, it borrowed and loaned 6,902.43 million SDRs. At exchange rates prevailing in October 1982, this equaled approximately $7,400 million. When the

loans from the oil facility to cover its borrowing costs. In 1975 an interest subsidy account was established with voluntary contributions from twenty-five countries.[83] This account alleviated the burden of interest payments for those developing countries least able to pay them. In 1976 the IMF set up a trust fund for low-income developing countries financed by profits from sales of gold owned by the Fund.[84] The trust fund provided concessionary lending with the same conditionality as the 1975 oil facility.[85] Before it ended operations in 1980, the trust fund lent over $4 billion.

The oil facility, the interest subsidy account, and the trust fund made loans with minimal conditionality. All three were temporary. Other new policies were designed to expand the IMF's ongoing programs for conditional lending.

In 1974 the IMF made provisions for larger loans, to be disbursed over longer periods and with greater maturities than those permitted under the traditional stand-by arrangements.[86] This "extended facility" provides medium-term financing, guaranteed for three years, to countries with severe payment imbalances that cannot be adjusted rapidly without undue hardship.[87] These loans are made to alleviate "structural imbalances" caused by widespread and long-standing distortions of costs and prices, which result in the wrong goods being produced and traded.[88] The extended facility also covers a country whose slow growth and inherently weak balance of payments constrain development.[89] Under the original provisions countries could borrow up to 140 percent of their quotas with as long as four to eight years to re-

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loans were made in 1974 and 1975, however, the exchange rate for the dollar was lower and the dollar value of the loans was approximately $8,300 million.

83. Guitián, *1970s*, *supra* note 38, at 10.

84. *Id.*

85. *Id.*

86. *Id.* at 9. Two other special lending facilities were established before the 1970s. The compensatory financing facility lends to countries who experience temporary shortfalls of exports; major liberalizations of this facility in 1975 and 1979 increased its use. The buffer stock financing facility lends to countries for purchases of approved world buffer stocks of primary commodities; buffer stocks have been approved for tin, sugar, cocoa, and rubber. Only tin and sugar have been purchased through the facility. *Id.*; *see* IMF SURVEY, Nov. 29, 1982, at 382.

87. Guitián, *1970s*, *supra* note 38, at 9.

88. *Id.*

89. *Id.*

pay,[90] terms that since have been liberalized. The terms of conditionality do not focus solely on demand-management policies, as do the stand-by arrangements. They also include policies to correct structural imbalances, improve utilization of resources, and reduce restrictions on trade.[91] In return, as a part of the conditionality, a country must pledge to follow policies that will lead to a sustained adjustment in its balance of payments over the medium term.[92]

Developing countries' borrowing requirements exceeded lending capacity under existing arrangements, particularly after the expiration of the oil facility.[93] In 1977 the IMF agreed to set up an interim supplementary financing facility that would allow developing countries to borrow more than was permitted under the stand-by arrangements and the extended facility until quotas could be increased in 1980.[94] The borrowed funds, totalling over $8 billion, were not available until early 1979.[95] Since then, all have been committed for loans.[96]

The IMF's additional lending was used readily by countries with serious deficit financing problems. The Fund's polices, however, have attracted severe criticism, the strongest of which is from those countries who were actual or potential borrowers. The main criticisms have been that the Fund's terms of conditionality are too strict, concentrate too much on bringing external payments into balance, and ignore the effects on the country's other goals.[97] The Fund also has been criticized for its emphasis on market solutions, particularly for refusing to let countries balance their payments by imposing trade restrictions.[98] Critics claim that the IMF's requirements for restricting the growth of money, reducing the government's spending, and depreciating the currency reduce real income in the country and often worsen the distribution of incomes, creating serious political problems for the government.[99] In recent years many countries with large deficits

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90. *Id.* at 9-10.
91. *Id.* at 10.
92. *Id.*
93. *Id.*
94. *Id.*
95. *Id.* at 11.
96. *Id.*
97. B. NOWZAD, THE IMF AND ITS CRITICS 9-10 (1981).
98. *Id.* at 10.
99. *Id.*

avoided coming to the IMF, preferring to borrow from the private markets at much higher rates of interest. Some countries came to the IMF only as a last resort when private lending was no longer available and debt-service payments were very high.

The IMF's program for Jamaica, which came to the Fund in 1977 as a last resort, is an example of a particularly controversial program.[100] Jamaica was neither able nor willing to meet the strict performance criteria set up by the Fund as conditions for a two year stand-by arrangement. From the outset, its budgetary deficits and credit expansion were greater than the targets agreed upon with the Fund, and in December 1977 the Fund interrupted Jamaica's drawings from the IMF.[101] In 1980 the IMF negotiated a new three year program with Jamaica under the extended facility that emphasized revived economic growth and investment. During the IMF's program, Jamaican production has fallen at increasing rates.[102] Critics cite the Jamaican case as an example of the political impracticality and rigid application of the Fund's conditionality.[103] The IMF in turn argues that Jamaica's poor performance resulted from the desperate economic straits existing before the country approached the IMF, and that Jamaica's adjustment would have been even more painful without the IMF's financing.[104]

The IMF, after a comprehensive review of its policy of conditionality, established new guidelines in 1979 in response to its experience during the 1970s.[105] Many of the principles of the 1968 guidelines were retained and important new provisions were added, most of which affirmed practices adopted during the preceding few years. The new guidelines provide for loans over a longer period—up to three years for stand-by arrangements.[106] Countries are encouraged to come to the IMF at an earlier stage, when adjustment will be less costly.[107] The IMF promises to take into account the "domestic, social, and political objectives, the ec-

100. Kincaid, *Conditionality and the Use of the Fund's Resources: Jamaica*, 18 FIN. & DEV., June 1981, at 18, 18-19.

101. *Id.* at 19-21.

102. INTERNATIONAL MONETARY FUND, INTERNATIONAL FINANCIAL STATISTICS YEARBOOK 269 (1982).

103. Kincaid, *supra* note 100, at 21.

104. *Id.* at 100.

105. Guitián, *1970s*, *supra* note 38, at 11.

106. *Id.* at 11.

107. *Id.*

onomic priorities, and the circumstances of members, including the causes of their balance of payments problems."[108] The performance criteria are to be limited to those necessary to evaluate the implementation of the program, normally confined to macroeconomic variables, and "those necessary to implement specific provisions of the Articles or policies adopted under them."[109] In general, the new guidelines recognize that structural imbalances in countries' payments take longer to correct than imbalances caused by excess demand.[110] The guidelines broaden the Fund's adjustment programs to include a wider range of policies and financing over a longer period of time and they provide for greater flexibility in the administration of the programs.[111] The terms of conditionality have been less eased than expanded in scope.

B. A Shift of Policy by the World Bank

The severe balance-of-payments problems many developing countries encountered during the 1970s were partly responsible for the lower growth rates in these countries. In many cases a country's development was affected adversely by the restrictive policies and curtailment of imports needed to reduce its deficit in external payments. Furthermore, the World Bank perceived the prospects for developing countries as being much worse in the 1980s. This inverse relationship between problems with the balance of payments and development caused the World Bank to reevaluate the almost exclusive use of its resources for "project lending."

In 1979 the World Bank adopted a new policy for "structural adjustment lending." The Bank recognized that long-term adjustments in external payments deficits could be accomplished either by reducing programs for investment and development, which conflicted with its mandate, or through a program of financial measures and structural adjustment supported by external borrowing. It decided that its goals for development would be served by programs supporting the second alternative—structural adjustment.

Structural adjustment lending is not too different from "pro-

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108. J. GOLD, CONDITIONALITY, *supra* note 37, at 22.
109. *Id.* at 30.
110. Guitián, *1970s, supra* note 38, at 11.
111. *Id.* at 11.

gram lending"—lending to finance imports—which the Bank has always done to a limited extent. In the 1940s, when the World Bank was lending mostly to developed countries for postwar reconstruction, program loans made up a large proportion of its commitments.[112] Nevertheless, the Articles of Agreement for both the World Bank and the IDA require that, except in special circumstances, loans be limited to specific projects of reconstruction and development.[113] During the past twenty-five years, program lending has constituted only five percent of the total commitments of these institutions, usually limited to special circumstances caused by war, natural disasters, a sudden fall in revenues from exports, or a sharp rise in prices of imports.[114]

During fiscal years 1980, 1981, and 1982, the World Bank has approved fifteen structural adjustment loans totaling about $2 billion, which is less than six percent of total loans from the World Bank and IDA.[115] The Bank's programs for structural adjustment include macroeconomic policies that correct relative prices in the country, promote a shift of production toward goods in which the country has a comparative advantage, and improve market operation to increase the efficient use of resources.[116] These projects have been concerned mainly with pricing policies, priorities for public investment, management of the government's budget and debt, and the strengthening of public enterprises.[117] The Bank reports that these loans permit a better response to the needs of some countries, but that it cannot yet determine whether the program is well conceived or is achieving the Bank's goals.[118]

The World Bank structural adjustment lending is similar to the IMF's extending financing for structural imbalances. As a result, cooperation between the two institutions has increased during the last three years. Nonetheless, they consider their activities to be complementary rather than overlapping. The IMF's immediate aim is to help countries adjust their balance of payments, whereas the World Bank concentrates on improving efficient use of resources.

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112. Wright, *supra* note 74, at 21.
113. *Id.*
114. *Id.* at 22.
115. WORLD BANK, *supra* note 58, at 10, 40.
116. Wright, *supra* note 74, at 21.
117. Landell-Mills, *Structural Adjustment Lending: Early Experience*, 18 FIN. & DEV., Dec. 1981, at 17, 19.
118. WORLD BANK, *supra* note 58, at 39-40.

Critics of the World Bank's structural lending program argue that the Bank is moving too close to the IMF's area of responsibility and that it may not have the expertise to develop macroeconomic programs.[119] Others feel that a cooperative effort to advise a country on a broad range of policies will give these institutions too much control over that country's internal affairs.[120]

C. Policies of the IMF in the 1980s

After two years of operating under its new conditionality guidelines, the IMF has drawn certain conclusions that will influence its decisions in the next few years. The Fund believes that many of the new balance-of-payments difficulties countries have experienced in the last three years are additions to other long-standing problems.[121] Although these problems are externally caused, they are not temporary. Consequently, the IMF does not intend to create additional special facilities to lend under low conditionality.[122] The Fund will continue to stress policies that encourage expanded production and intends to continue its cooperation with the World Bank.

In the past three years, the IMF has increased members' access to its resources under the extended facility. Countries are now permitted to borrow up to 450 percent of their quotas.[123] Implementation of the new guidelines means more lending; for this reason the IMF stresses the importance of a substantial increase of members' quotas.[124] In spite of the thirty-three percent increase in 1978, and the fifty percent increase in 1980, the quotas have been eroded severely by inflation[125] in a period of growing world trade and rising deficits. The IMF already has found it necessary to borrow to meet its lending commitments. In 1981 the Saudi Arabian Monetary Agency agreed to extend a medium-term loan

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119. Landell-Mills, *supra* note 117, at 17.

120. *Id.*

121. Guitián, *Fund Conditionality and the International Adjustment Process: A Look into the 1980s*, 18 FIN. & DEV., June 1981, at 14, 15 [hereinafter cited as Guitián, *1980s*].

122. *Id.*

123. *Id.* at 16.

124. IMF SURVEY, Aug. 16, 1982, at 249.

125. Guitián, *1980s*, *supra* note 121, at 16.

to the IMF of approximately $8 billion over a six year period.[126] In April 1982 eighteen member countries agreed to make short-term loans of almost $1.5 billion to the IMF.[127] Estimates of new borrowing needs suggest that the IMF may have to increase its resources by six to seven billion dollars per year.[128] Even if a new increase of quotas can be agreed upon, these funds will not be available until 1984 or 1985.[129] Additional borrowing by the IMF is certain for the next three years.

V. Role of the Private Markets

The international institutions provide only a small fraction of the debt held by the developing countries. In recent years over half of their new debt has come from the private markets, predominately from the commercial banks.[130]

After the price of oil rose in 1974 there was much discussion and concern about how the revenues that formed the surplus on current account for the oil-exporting countries could be recycled to the countries in deficit. Many felt that this recycling would have to be done by the official institutions.[131] There was, however, no agreement about whether or how this could be done. As it turned out, the private markets moved most of the money by taking deposits from the oil-exporting countries and relending the money to the countries with deficits, often developing countries.[132]

The long-term external debt owed by the non-oil development countries to private creditors has increased from $48.5 billion in 1973 to $305.7 billion in 1982.[133] Because of inflation the real value of this debt has grown much less rapidly, but it has grown significantly. Distribution of this private lending to the developing countries is uneven. Private creditors lend to make a profit and limit their lending to countries they consider to be

126. IMF Report, *supra* note 82, at 86.

127. *Id.*

128. Guitián, *1980s*, *supra* note 121, at 17.

129. IMF Survey, Sept. 20, 1982 at 294. On February 11, 1983, the IMF agreed to expand its quotas by $32.5 billion, or 47.4%. *See* Gilpin, *IMF Plan Helps Ease Debt Crisis*, N.Y. Times, Feb. 14, 1983, at D1, col. 3.

130. IMF Outlook, *supra* note 4, at 166.

131. R. Dunn, Jr., *supra* note 76, *passim.*

132. Killick & Sutton, *An Overview*, in Adjustment and Financing in the Developing World 41 (T. Killick ed. 1982).

133. IMF Outlook, *supra* note 4, at 170.

creditworthy. From 1979 to 1981, for example, Brazil, China, Korea, Mexico, and the Philippines accounted for well over fifty percent of syndicated bank credits to non-oil developing countries.[134] The results of private lending to developing countries—including, for example, uneven distribution among countries, inefficient allocation of funds, and sudden withdrawal when the bankers see warning signals—are subject to criticism. Nevertheless, most analysts agree that private lending greatly lessened the world's difficulties with payment imbalances in the 1970s.[135]

For several reasons, private lending may not play as large a role in financing the deficits of the developing countries in the 1980s. Many banks already have a large proportion of their assets invested in loans to developing countries—by 1981 the figures were twenty-three percent for United States banks and twenty percent for all banks.[136] Banks thus may be reluctant to continue lending large amounts to developing countries. Other reasons for the possible decline in private lending pertain to the situations of the developing countries. The deficits of developing countries are expected to be large and prolonged. Many countries, particularly those who had been judged creditworthy, already hold large external debts and must use substantial proportions of their export earnings to service these debts.[137] The increasing debt-service problems of many developing countries make them more risky than they were several years ago. The private banks recently have renewed short-term loans to many countries although they would have preferred not to do so. When the banks are faced with the choice of writing off as a sure loss a large loan on which the borrower defaults or renewing the loan with the hope that repayment may be forthcoming in the future, the banks usually choose to renew.[138]

The most disturbing evidence of change in the creditworthiness of many countries is the actual and anticipated number of countries requesting a rescheduling of their debts.[139] Because loans to

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134. O'Brien, *Roles of the Euromarket and the International Monetary Fund in Financing Developing Countries,* in ADJUSTMENT AND FINANCING IN THE DEVELOPING WORLD 138 (T. Killick ed. 1982).

135. *Id.* at 144-45.

136. *Id.* at 141.

137. IMF OUTLOOK, *supra* note 4, at 173.

138. Killick & Sutton, *supra* note 132, at 41.

139. INTERNATIONAL BANKING STUDY GROUP, RISKS IN INTERNATIONAL BANK LENDING: FIRST REPORT OF THE INTERNATIONAL BANKING STUDY GROUP OF THE

governments usually are so large, bankers almost always prefer to reschedule rather than write off the loans as losses.[140] In recent years the commercial banks concluded rescheduling agreements with several countries on debts ranging from less than half a million dollars to $3 billion.[141] These were small when compared with the rescheduling of Poland's $60 billion debt in 1981, with $2.2 billion of principal repayments due in 1981 alone. In September 1982 the international financial community was shaken by the economic crisis in Mexico and the prospect of a rescheduling of Mexico's $60 billion debt.[142] Central bankers of the major industrial countries were concerned enough to put together an emergency loan of $1.85 billion to Mexico.[143] A survey of commercial bankers by the Group of Thirty shows that these bankers expect future reschedulings to be larger, more numerous, and more complex than in the past.[144] Furthermore, the bankers believe that the most serious threat to the stability of the international banking system would be a considerable number of reschedulings involving large sums or a default by a major borrower.[145]

The international lending institutions cannot replace the private markets for financing deficits on current account. The issues raised by this fact are to what extent can these institutions influence private lending and in what situations must they serve as an alternative to private lending. The adjustment programs developed by the IMF are an important factor in the willingness of commercial banks to continue lending to a country with balance-of-payments problems—more important than the actual loans the IMF makes.[146] It is impossible to know how much an IMF program for a country, intended to address the country's early

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GROUP OF THIRTY 11-12 (1982).

140. *Id.* at 49-50.

141. *Id.* at 11.

142. Lewis, *Mexico to Receive $1.85 Billion in Loans*, N.Y. Times, Aug. 31, 1982, at D5, col. 1.

143. *Id.*

144. INTERNATIONAL BANKING STUDY GROUP, *supra* note 139, at 15.

145. *Id.* at 7.

146. *Id.* at 51, 54; *see* O'Brien, *supra* note 134, at 152. In late 1982 and early 1983 the IMF has taken an increasingly activist role in arranging large loans to countries with serious debt problems. The IMF is, for the first time, explicitly coordinating its lending with that of commercial banks and making some of its loans contingent on additional loans from private banks. *See* Farnsworth, *A Dramatic Change at the IMF*, N.Y. Times, Jan. 9, 1983, § 3, p. 1, col. 2.

problems, can promote the flow of private capital; such a program might contribute significantly to perceptions of the country's creditworthiness. In similar ways, support from the World Bank may increase a country's access to private loans. Many countries, particularly low-income countries, have never been considered creditworthy by the commercial banks and probably will not be in the near future. The commercial banks should not be encouraged to lend to these countries, for such loans would likely lead to rescheduling and, possibly, to default. If these countries receive financing for their deficits, it must be through concessionary official lending and aid.

VI. CONCLUSION

Lending by the international institutions to the non-oil developing countries has increased significantly since 1973. Total IMF loans outstanding to these countries increased more than twelvefold, from $1.2 billion in 1973 to $14.9 billion in 1981.[147] Their outstanding long-term debt to World Bank institutions rose from $12.6 billion in 1973 to $71.5 billion in 1982.[148] The IMF has predicted that the combined deficits on current account for the non-oil developing countries will grow over the next four years by about twenty-five percent.[149] This projection is based on the assumption that official development aid will be maintained in real terms.[150]

If official lending is reduced, the deficits will almost surely be smaller. If no one will lend to it, a country cannot finance a deficit, and it has no choice but to cut its imports. One possible alternative is for developing countries to undertake rational domestic policies to reduce their deficits, if they know that financing will not be available. This is the Reagan administration's position.[151] Certainly some of the balance-of-payments problems of the developing countries can be traced to inappropriate economic policies of their governments.

Many of the reasons for the deficits, however, are external: the high price of oil, falling world prices for their exports, high world interest rates, and recession in the industrial countries. Even ex-

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147. IMF OUTLOOK, *supra* note 4, at 170.
148. *Id.*
149. *Id.* at 174.
150. *Id.* at 21.
151. Reagan, *supra* note 1, at 4.

ternal events must be adjusted to, a point emphasized by the IMF. Nevertheless, how the adjustment is made will determine the economic welfare of the developing countries, and also of the industrial countries, for all countries' economies are increasingly interdependent. The adjustment can be made without a grave reduction in growth and development only if it involves shifts and increases in the developing countries' production and exports.

These kinds of structural adjustments take more time than the traditional solution of simply reducing a country's demand, and thus require a longer period of financing a country's current-account deficit. Both the IMF and the World Bank are tailoring their lending programs to provide support for structural adjustment in order to permit the balances of payments to adjust simultaneously with growth and development. The value of the lending from these institutions exceeds the monetary value of their loans. Through technical advice and assistance, and through the discipline imposed as conditions of the loans, they promote national programs for adjustment and growth that otherwise could not or would not be carried out. Moreover, the additional confidence in the economy that is generated by these programs helps to maintain a flow of private capital.

The IMF and the World Bank are faced with the task of finding new and creative solutions to serious economic problems. There is a real danger that their loans will merely serve to postpone both adjustments in the balances of payments and the needed structural adjustments of the economies. For this reason, the conditionality of their loans and their assistance in devising programs for adjustment are essential.

The IMF has been criticized widely for emphasizing balance of payments adjustment at the cost of growth. Two recent studies by the IMF provide evidence to the contrary. In a study that examines changes in rates of inflation and in rates of growth across many developing countries, the IMF found that countries with low or controlled inflation have better rates of growth than countries with high and accelerating inflation.[152] Another study comparing the experience of developing countries that have borrowed from the IMF with those of other developing countries finds that, with no substantial differences in growth, those with IMF programs had significantly greater improvements in their deficits and

152. IMF OUTLOOK, *supra* note 4, at 132-35.

better, though modest, results in reducing inflation.[153] These studies are far from conclusive, but they are encouraging evidence that growth and adjustment may not be inconsistent.

The current United States administration has serious doubts about the existing and projected expansion of lending by the IMF and the World Bank. These views are made abundantly clear in the 1982 *Economic Report of the President*.[154] This shift of policy results from the current administration's strong belief in market solutions rather than reliance on governmental programs.[155] A second factor is the desire for the United States to have more control over how its contributions are used; the President's Council of Economic Advisors believes that bilateral aid is more effective than multilateral aid.[156] There is also a concern that additional loans will be inflationary, that they will increase the spending capacity of the borrowers without, presumably, any corresponding reduction in spending by the donating countries.[157] This shift in policy is consistent with the Council's economic views on the domestic economy.

There is some merit in each of these arguments, but the author believes that the change in United States attitudes toward the IMF and the World Bank does not serve the long-term interests of the United States.

First, prosperity and growth for the developing countries are important for the United States. The United States economy is increasingly dependent on exports, and the developing countries constitute a large and growing market for its exports. As a percentage of gross national product, United States exports have more than doubled in the last twenty years;[158] and in 1981, twenty-nine percent of United States exports were sold to developing countries outside of OPEC,[159] compared with only twenty-four percent in 1973.[160] Second, effective adjustment that pro-

153. Donovan, *Macroeconomic Performance and Adjustment Under Fund-Supported Programs: The Experience of the Seventies*, 29 IMF STAFF PAPERS 171, 171-203 (1982).

154. COUNCIL OF ECONOMIC ADVISORS, ECONOMIC REPORT OF THE PRESIDENT 184-89 (1982).

155. *Id.* at 183-84, 188.

156. *Id.* at 186.

157. *Id.* at 189.

158. *Id.* at 174.

159. *Id.* at 349.

160. *Id.*

motes growth and development requires fairly long-term programs which often must be implemented by successive administrations. The IMF and the World Bank have a good record of sustaining programs throughout changes in governments. This is much less likely to be the case with bilateral aid, which is often given to countries with particularly sympathetic political ties. Third, while both international lending institutions encourage countries to increase the functioning of markets as a means of allocating resources more efficiently, they also take into consideration countries' internal goals that may require intervention in the markets.[161] To deny loans to countries with such goals would severely limit the number of countries supported by the United States. The economic well-being of the United States, however, is promoted by the growth and development of as many of the developing countries as possible, not just the few which, for the time being, follow our recommendations for market solutions.

What are the likely implications of a substantial reduction of United States support for the IMF and the World Bank? The United States, with the world's largest economy,[162] also has been the largest contributor to these institutions. As a result, it has the greatest influence on their policies. If the United States refuses to support new quotas for the IMF, to increase its capital subscription to the World Bank, and to continue its contributions to IDA, the activities of these institutions will be seriously reduced. United States contributions are important in dollar terms. They also affect the willingness of other countries, which are smaller and usually less prosperous, to maintain their contributions. In some cases, a refusal by the United States to support a change in IMF or World Bank policy amounts to a veto.

Both the IMF and the World Bank have the option of increasing their borrowing without an increase in subscriptions or capital. If they do not receive United States support, they can be expected to borrow more. The IMF has expressed intentions of turning to the private markets to borrow if it must—something it has never done. The World Bank certainly could expand its borrowing, thereby increasing the ratio of its debt to its equity. As a result, both institutions would be less flexible and more vulnera-

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161. J. GOLD, CONDITIONALITY, *supra* note 37, at 22-25; *see* WORLD BANK, *supra* note 58, at 3.

162. The United States share of world output was 23% in 1980. COUNCIL OF ECONOMIC ADVISORS, *supra* note 155, at 182.

ble to changes in market conditions, and would have to charge higher rates of interest on their loans.

In the last three months of 1982 the number of countries having difficulties meeting their debt obligations increased, raising fears of an imminent banking crisis.[163] Commercial banks have reacted by reducing their lending to many countries,[164] increasing the repayment problems for yet other countries and the likelihood of defaults by some major debtors. Many see the most plausible way of avoiding an international banking crisis to be an expansion of lending by the IMF. The Reagan administration's alarm about the deteriorating world economic situation has caused it to reverse its earlier position of insisting that countries primarily help themselves. The United States has dropped its opposition, voiced at the IMF meetings in September, to a fifty percent increase of IMF quotas.[165] The United States is now taking the lead in proposing ways to strengthen the international monetary system.[166] It is too early to know whether this new attitude represents a long-term change in the Reagan administration's policies toward the international lending institutions or merely a short-term response to a perceived emergency.[167]

The United States interest would be best served by continuing its strong financial support of the IMF and the World Bank and using its influence to assure that their lending programs are as effective as possible, promoting adjustment and growth for the developing economies.

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163. Lewis, *5 Nations Address Monetary Perils*, N.Y. Times, Dec. 10, 1982, at A1, col. 1.

164. *Id.* at D2, col. 1.

165. Lewis, *U.S. Is Said to Support I.M.F. Rise*, N.Y. Times, Dec. 3, 1982, at D1, col. 6.

166. Farnsworth, *U.S. Proposal Favors Talks in Frankfurt*, N.Y. Times, Dec. 9, 1982, at D1, col. 3. On January 19, 1983, the Group of 10 industrial countries agreed to make $19 billion available for borrowing by all IMF members, a measure recommended by the United States. *See* IMF Survey, Jan. 24, 1983, at 17. Fiehn & Pearson, *IMF Loan Pool Set for Expansion to Halt Defaults*, Wall St. J., Jan. 19, 1983, at 28, col. 1. [Ed.]

167. The new increases of IMF quotas and the agreement by the Group of 10 providing new funds to the IMF together require an $8-10 billion contribution by the United States. In spite of the administration's support for these measures, in early February 1983, the necessary congressional authorization is far from assured. *See* Farnsworth, *IMF Near Accord on Quota Rise*, N.Y. Times, Feb. 11, 1983, at D1, col. 6.