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Out of time

The case for replacing the World Bank and IMF

WORLD DEVELOPMENT MOVEMENT

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Abbreviations

BIT	Bilateral Investment Treaty
CEE	Central and Eastern European countries
CFF	Compensatory Finance Facility (of the IMF)
CPIA	Country Policy and Institutional Assessment
EIR	Extractive Industries Review
EU	European Union
ED	Executive Director (of the World Bank and IMF)
ESAC	Enhanced Structural Adjustment Credit (of the World Bank)
ESAF	Enhanced Structural Adjustment Facility (of the IMF)
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
HIPC	Heavily Indebted Poor Countries Initiative
HNP	Health, Nutrition and Population
IBRD	International Bank for Reconstruction and Development
ICSID	International Centre for the Settlement of Investment Disputes
ICU	International Clearing Union
IDA	International Development Association
IFC	International Finance Corporation
IFIs	International Financial Institutions (the World Bank and IMF)
IMF	International Monetary Fund
ILO	International Labour Organisation
LDC	Least Developed Country
LIC	Low Income Country
MIGA	Multilateral Investment Guarantee Agency
NGO	Non-governmental Organisation
OED	Operations Evaluation Department (of the World Bank)
PPP	Public Private Partnership
PRGF	Poverty Reduction Growth Facility (of the IMF)
PRSC	Poverty Reduction Support Credit (of the World Bank)
PRSP	Poverty Reduction Strategy Paper
SAC	Structural Adjustment Credit (of the World Bank)
SAF	Structural Adjustment Facility (of the IMF)
SAP	Structural Adjustment Programme
SAPRI	Structural Adjustment Participatory Review Initiative
UK	United Kingdom
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
USA	United States of America
USSR	Union of Soviet Socialist Republics
WCD	World Commission on Dams
WTO	World Trade Organisation

1 Introduction

"Although the IMF and World Bank have changed considerably since 1944, they have changed less than the global economy they oversee. Not only has the distribution of world economic power shifted substantially, making the distribution of power within the institutions seem anachronistic, the financial system has been transformed."
Christopher Swann, Financial Times, 2004[1]

The world has changed. The International Monetary Fund (IMF, also referred to as the Fund) and World Bank (also referred to as the Bank) have not changed enough. This was the message in the mainstream press during the institutions' 60th anniversary. But this is not the only reason why these institutions do not meet the needs of the world's poorest people or the global economy.

The World Development Movement (WDM) has been campaigning for international debt cancellation for many years and has been criticising the structural adjustment programs (SAPs) foisted on poor countries in return for aid, loans and debt relief for just as long. But these problems persist. There seems no end in sight to the cycle of debt, and the free market policies imposed on poor countries continue, albeit with new names. Increasingly obvious is the need not just for debt write-offs and changes to Bank and Fund conditionality but for a more fundamental change to the role, remit and functioning of the international financial institutions (IFIs).

This report is WDM's contribution to an ongoing debate over what kind of global institutions we need in order to improve everyone's quality of life in a highly interconnected world. We argue that, in their current forms, the World Bank and IMF are part of the problem rather than part of the solution and need a radical overhaul.

After this brief introduction, the report is split into three principal chapters. A brief history of the World Bank and IMF is followed by a detailed critique explaining the overwhelming case for change, followed finally by WDM's suggested agenda for scrapping the World Bank and IMF and creating very different IFIs. We call on anyone who is interested in their own future and the future of others to understand the history, consider the evidence and demand change.

2 A brief history of the IMF and World Bank

"In a televised address, Thaksin Shinawatra, prime minister, vowed Thailand would never again 'fall prey to world capitalism' or require IMF help. Standing in front of a giant Thai flag, the premier said he intended to modify laws adopted under IMF tutelage."
Financial Times, July 2003.[2]

A nation celebrating escape from imposed policies as debts are finally repaid – as happened in the case of Thailand – was perhaps not the future that the founders of the IMF and World Bank would have envisaged when these institutions were created in 1944.

This chapter aims to provide a potted history of the two institutions. While it is not possible to cover all that has happened over the past 62 years, the intention is to give a sense of how the World Bank and IMF came into being and how they have changed since.

2.1 A difficult birth

Gathering towards the end of the Second World War in the New Hampshire resort town of Bretton Woods, 45 countries attended a conference aimed firstly at creating global economic rules that would promote stability and prevent another great depression and secondly devising a strategy for rebuilding Europe once the war had ended.

While most countries at the conference were engaged in a superficial exchange of views, the real negotiations took place amongst just a few. Prominent among these were the United States of America (USA) and the United Kingdom (UK) – represented by world-renowned economist John Maynard Keynes.

In order to address the first aim of the conference (greater economic stability) Keynes wanted to create a mechanism, called the International Clearing Union (ICU), to automatically balance governments experiencing trade and other payments deficits with those in surplus. However, the US, a major 'surplus' country at the time, dismissed Keynes's proposal, rejecting the idea that surplus (or creditor) countries were part of the problem and should therefore come under pressure to balance their payments (see Box 1).

Instead the US proposed the creation of an international monetary fund

aimed at lending to countries in deficit – a mechanism that would essentially replace one kind of debt with another. The US, being by far the most dominant player in the negotiations, got its way and the IMF was established. Its remit was twofold: first, to encourage financial stability by managing a system of fixed but adjustable exchange rates tied to the US dollar (backed by gold reserves) and second to lend, on a short-term basis, to countries with balance-of-payments problems.

After failing to convince the US government over the ICU, the UK and other European negotiators concentrated on the second aspect of the meeting, the strategy for post-war European reconstruction. On this there were no great political differences as the US government recognised the importance to the US economy of kick-starting growth and job creation in Europe. The result was the creation of the International Bank for Reconstruction and Development (IBRD), more commonly known as the World Bank.[3]

The other key decision made at the Bretton Woods conference concerned how the two IFIs would be governed. The job of determining financial contributions (with commensurate voting shares) in the IMF fell to US secretary of state Raymond Mikesell. As Ariel Buira, director of the developing country 'G24' secretariat in Washington, outlines: "The formula developed by R. Mikesell in 1943 had the political objective of attaining the relative quota shares that the US president and secretary of state had agreed to give the 'big four' wartime allies, with a ranking which they had decided. Thus, the US was to have the largest quota, approximately $2.9 billion, the UK including colonies an amount about half the USA quota, the Union of Soviet Socialist Republics (USSR) a quota just under that of the UK and China somewhat less."[4]

This was achieved through a confusing formula using various economic indicators. Mikesell states that when he was questioned on how the distribution of quotas had been reached: "I … gave a rambling twenty minute seminar on the factors taken into account in calculating the quotas, but I did not reveal the formula. I tried to make the process appear as scientific as possible, but the delegates were intelligent enough to know that the process was more political than scientific."[5]

The voting shares in the World Bank were similarly distributed amongst the major powers and two boards of executive directors were created, each currently with 24 members, to oversee the IFIs.

Also agreed at the time was the process for selecting the heads of the two institutions. The main protagonists, the USA and Europe, did a deal whereby the US government would choose the president of the World Bank and European countries would choose the managing director of the IMF.

Box 1

ICU versus IMF
Keynes versus US government
Broad vision versus narrow self interest

The British government, led by John Maynard Keynes, went into Bretton Woods proposing that debtor and creditor countries should share the responsibility for achieving and maintaining equilibrium in balance of payments. By definition, if certain countries remained creditors, then others would have to be debtors. Keynes himself had already devised a system for an ICU that would put equal pressure on deficit and surplus nations to reach equilibrium.

Keynes argued that trade imbalances could become self-perpetuating as debtor nations were depressed by the drain of money abroad and so output, competitiveness and exports declined. Surplus nations were stimulated toward greater growth and investment and so increased output, competitiveness and exports. Creditor countries failed to spend the surplus in debtor nations economies. Keynes argued that there needed to be an international mechanism to ensure that imbalances in trade between nations were redressed. He proposed an ICU holding a neutral unit of international currency, which he called the ‘bancor’. All trade would be measured in bancors: exports would accrue bancors and imports would expend bancors. Countries would be expected to maintain, within a small percentage, a zero account with the ICU. Both debtor and creditor nations would receive a small interest charge on their unbalanced account – whether deficit or surplus – giving every country the incentive to move towards a balance of trade.[6]

The ICU proposal was discussed with many British economists and treasury officials. Lord Robbins commented, “it would be difficult to exaggerate the electrifying effect felt throughout the whole relevant apparatus of government of the production of this document … Nothing so imaginative and so ambitious had ever been discussed as a possibility of responsible government policy.”[7]

The US on the other hand formulated a proposal for an IMF. This focused on a system of fixed exchange rates centred around the US dollar, with the dollar being backed by gold. Countries with excessive trade deficits could borrow from the Fund to help finance the gap between their imports and exports. Charges would have to be paid on this debt and the more they borrowed, the higher the charges would be. The US argued that this would force debtors to reduce deficits. The US, as the largest creditor at the time, opposed any suggestion that pressure should be placed on creditors as well as debtors to return to equilibrium.[8] Keynes's ICU proposal was rejected and the USA's IMF proposal was adopted.

After Bretton Woods, there was much debate within Britain over the creation of the IMF. In a BBC radio broadcast Edward Holloway, former secretary of the Economic Research Council argued: "There is no point in the continuation of a system which automatically leads to unpayable indebtedness between nations … the IMF does nothing to bring pressure to bear on nations to balance their accounts with the world in terms of goods and services … In our memorandum we pointed out our reasons for believing that the Bretton Woods Agreement would not work – and we particularly stressed the obligation of creditor nations enabling debtor nations to discharge their indebtedness by accepting a surplus of imports over exports … the Bretton Woods agreement ignores this obligation – and actually strengthens the position of creditor nations whilst imposing penalties on debtor nations … These proposals, we argued, would inevitably lead to a desperate competition for world markets … default … was certain to be the unfortunate fate of one or more of the nations concerned."[9]

Geoffrey Crowther, former editor of the Economist, and one of the foremost economists in the UK at the time, stated: "The two governing principles of the Keynes plan were thus that the problem of settling outstanding balances should be solved by 'creating' additional international money, and that debtor and creditor should be treated almost alike as disturbers of equilibrium. It was these two principles that failed to find favour in the United States … It is the belief of the present author that Lord Keynes was right, and that the world will bitterly regret the fact that his arguments were rejected."[10]

2.2 Growing pains

Although the IBRD was initially meant to finance reconstruction in Europe, this role was quickly usurped by the US Marshall Plan. By 1953,

the IBRD was lending $497 million for European reconstruction in comparison with $41.3 billion transferred to Europe under the Marshall Plan.[11] This, according to one author, drove the Bank to proactively seek lending opportunities in developing countries during the 1950s[12] and lending to developing countries duly began to pick up during this decade.[13]

Also, over time, the World Bank expanded beyond the IBRD so that, rather than being the World Bank, the IBRD became the central member of what is known as the World Bank Group. The additions to the group were the International Finance Corporation (IFC) in 1956 the International Development Association (IDA) in1960, the International Centre for Settlement of Investment Disputes (ICSID) in1966 and the Multilateral Investment Guarantee Agency (MIGA) in 1988. (See appendix 1 for details on the remit of these institutions.)

The 1950s and 1960s saw a period of world economic stability and growth. According to one author, it was a "golden age of economic development … an era of unprecedented sustained economic growth in both developed and developing countries"[14] with governments pursuing the types of intervention in the economy advocated by Keynes in the 1930s and 1940s.[15] Consequently, apart from lending to the four countries involved in the Suez crisis,[16] the IMF's active lending role was minor until the 1970s.[17]

Industrialised countries accounted for over half of the IMF's modest lending between 1950 and 1969 and continued to account for just less than half through the 1970s. This included large loans to Italy and the UK in the mid-1970s. In 1978, contingency arrangements were made for a lending programme with the US after the dollar came under pressure from speculators but this was never implemented. Since 1982, industrialised countries have no longer needed to resort to IMF loans so it is developing countries and economies in transition that have become the clients of the IMF.[18]

By 1971, with the US increasingly unwilling to sell its gold reserves to finance its growing war debts, the fixed exchange rate system that the IMF had managed became a target for removal.[19] By 1973, industrialised nations had colluded to create a new system of allowing countries to float their currencies, although this was not formally recognised in the IMF's articles of agreement until 1978.

With the dollar replacing gold as the world's de-facto reserve currency, the

US was able to sustain greater deficits as other countries needed to buy dollars in order to engage in international finance and trade. As Ann Pettifor has pointed out: "They constructed a new financial architecture that effectively *obliges* central banks of both rich and poor countries to lend to the US – by buying US treasury bills (debt) … It is US treasury bills that have now effectively become the world's reserve currency – where once that reserve currency was neutral (gold)"[20] (emphasis as in original).

Since the late 1970s, the IMF's only relation to non-borrowing members has been its function of surveillance, primarily through Article IV consultation (where IMF staff assess a country's economic performance). However, particularly for richer countries with their own surveillance capacity and an ability to ignore, if they wish, IMF advice, this IMF function has little significance.[21]

As well as the abolition of the exchange rate system, the early 1970s also saw an increase in the price of oil. This had two critical impacts. First, it created a glut of OPEC foreign exchange invested in commercial banks available for lending to poor countries – a threat to the role of the Bank and Fund. And second, it led to a balance of payments crisis in many oil importing poor countries – an opportunity for the Bank and Fund to expand their lending. The IMF duly opened up access to its resources for the poorest countries and the World Bank undertook more policy-based, as opposed to project-based, lending.

2.3 Bloated middle age

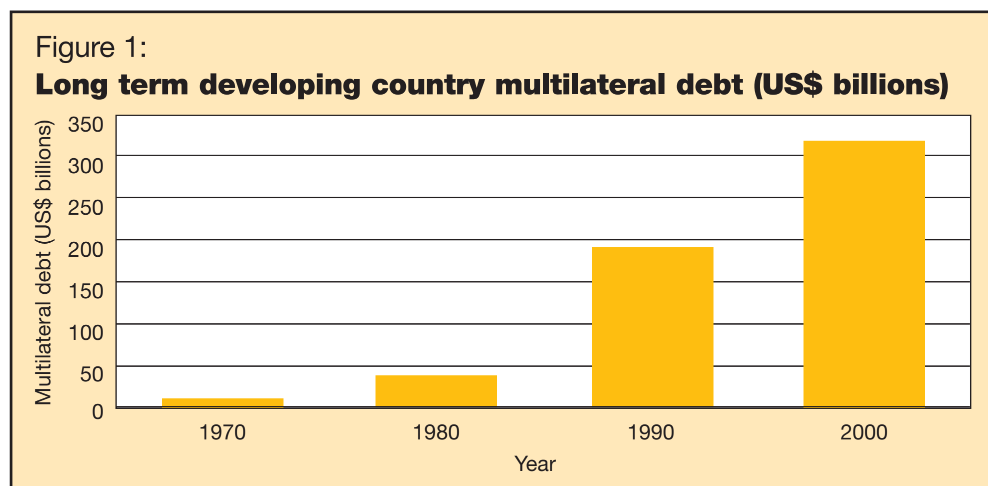
In 1979, the US Federal Reserve began to control the growth of money in order to lower inflation. Whilst this only had a small impact on money growth, short-term US interest rates doubled between 1978 and 1981.[22] The rise in rates left many borrowing countries unable to meet their debt repayments owed in dollars. Default would have meant the bankruptcy of several large commercial banks. The IMF and World Bank began to make loans to debtors to ensure that they would not default, an entirely new form of 'defensive lending' not foreseen at Bretton Woods.

With these loans came an increased level of conditionality. The IMF and World Bank argued that the debtor countries had been unable to pay their loans due to failures in the structure of their economies, and so they needed to 'stabilise' and 'adjust' in order to overcome their 'structural' problems. A typical IMF stabilisation programme at this stage included policies to reduce inflation, increase interest rates, reduce public spending, increase

taxation, eliminate subsidies and stabilise the exchange rate. The World Bank pushed the liberalisation of trade, privatisation and general deregulation.[23]

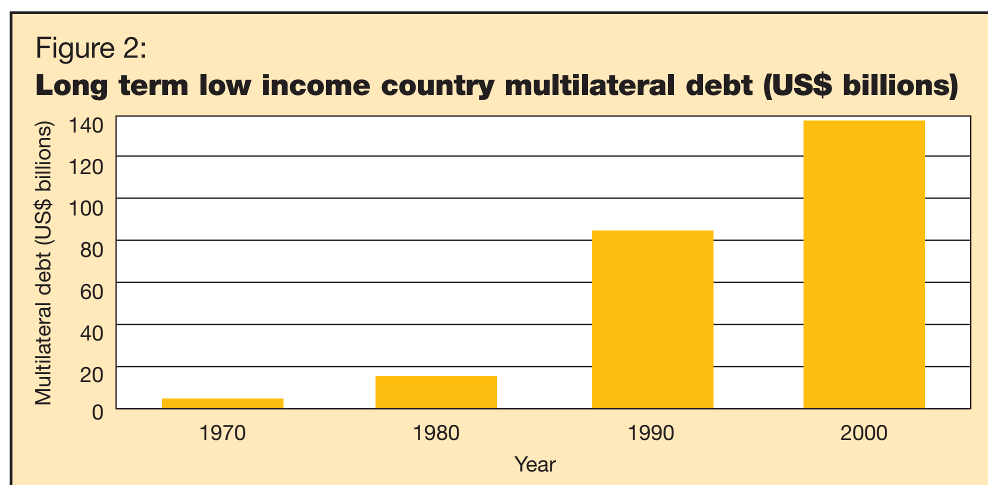
Although the creation of the Compensatory Financing Facility (CFF) in 1963 had introduced the first IMF loans for purposes related to what the IMF saw as the *causes* of balance-of-payments problems, rather than financing the overall balance of payments,[24] it was the onset of the debt crisis that resulted in this role expanding significantly.

Figure 1:
Long term developing country multilateral debt (US$ billions)



As figures 1 and 2 clearly show, the multilateral debts of developing countries have ballooned over the past 30 years, in the process morphing from a modest economic management issue to a full-blown crisis.

Figure 2:
Long term low income country multilateral debt (US$ billions)



During most of this period, neoliberal economic policies were in vogue at the IMF and World Bank. This can be attributed to the rise of free market thinking and a rejection of the 'Keynesian consensus' in US and UK university economics departments through the 1960s and the election of right-wing governments in countries dominating decision-making within the IFIs, most notably Ronald Reagan (1980) in the US and Margaret Thatcher (1979) in the UK. The IMF expanded its reach into developing country economic policy-making through the 1980s with the creation of the Structural Adjustment Facility (SAF) in 1986, giving low-interest one year loans to the poorest countries in return for policy reform, and the Enhanced Structural Adjustment Facility (ESAF) in 1987, doing the same over three years.

In contrast to its original remit, the IMF had become a perpetual lender to poor indebted countries because their balance of payments problems were not temporary and IMF intervention was not helping them overcome their deficits. In becoming indebted to the IMF, deficit nations were actually increasing their debt obligations; the fears expressed by UK economists when the IMF was created had become reality. In addition, once the IMF started demanding trade liberalisation in return for loans, it was imposing a policy that could easily exacerbate rather than ameliorate a country's fiscal and balance of payments problems.

With the failure of many developing countries to escape the debt crisis by the end of the 1980s, industrialised countries agreed to reduce the value of certain bilateral debts of the world's poorest countries through the Paris Club – a group comprising the world's main aid donors. The first agreement was in Toronto in 1988, and subsequent agreements in London (1991) and Naples (1994) gradually improved the debt reduction available. However, the small quantities involved combined with the inappropriate economic policies being implemented in poor countries meant these reductions had no effect on reducing total indebtedness. In fact the total external debt (multilateral plus bilateral plus private debt) of low-income countries rose from US$121 billion in 1980 to US$411 billion in 1990, and US$526 billion in 2000.[25]

The end of the Cold War, and the dissolution of the USSR, gave the IMF and World Bank a new role in transition economies. This typically involved structural adjustment including privatisation, abolition of price controls, trade liberalisation and curbs on state spending.[26] Although some of the richer countries to the west such as the Czech Republic and Poland, have now graduated from their IFI programmes, further east, especially in former

Soviet states in central Asia, the Bank and Fund still have a strong presence. Many now access concessional funding through the IMF's Poverty Reduction Growth Facility (PRGF) and through the IDA due to their status amongst the poorest countries of the world, and so also have to formulate Poverty Reduction Strategy Papers (PRSPs).

In 2005 WDM research revealed that of the ten Central and Eastern European (CEE) countries that have completed a PRSP, all include privatisation and tight fiscal policy, eight include investment deregulation and eight include trade liberalisation.[27] Although PRSPs are supposedly 'country-owned' documents drawn up independently (see section 3.5), the influence of the Bank and Fund remains strong as there seems to be little independence or variation in the policies being adopted by poor CEE countries.

2.4 Time to retire

With the failure of the various Paris Club debt reduction deals to make any significant difference, the 1990s saw the IMF and World Bank pushed into addressing the issue of debt. The result was the creation of the Heavily Indebted Poor Countries (HIPC) Initiative in 1996, which was replaced by the Enhanced HIPC in 1999. At best, this was finally a recognition that the severe debt problems of many poor countries could not be ignored. At its worst though, it was based on a flawed analysis of debt sustainability that resulted in too little debt relief being delivered and proved to be yet another lever with which to ratchet yet more structural adjustment out of poor countries.

The most recent debt deal, proposed in 2005 and finalised in 2006, is again a tacit recognition that previous efforts (Paris Club and HIPC) have failed. However, although total debt cancellation to the Bank and Fund is on the table for the first time, it is being delivered to too few countries and, as ever, they have to jump through the IFIs' economic hoops in order to qualify. Add to this structural adjustment the IMF's continuing role in low income countries alongside the continued use of World Bank loans rather than grants for the poorest countries and there currently seems to be little prospect of an end to the debt crisis.

From the mid 1990s, under the guidance of James Wolfensohn, then president, the World Bank expanded its role in development research and policy advocacy. Dubbed 'the knowledge bank', the strategy was to place the Bank as a dominant, if not *the* dominant voice on international development issues. It has been reported that "between 1997 and 2002

$283 million was spent on reorganising the Bank to be a knowledge institution [and] far more was spent on actual activities such as training and reports."[28] However, this has been accompanied by criticism that the World Bank portrays a narrow view of development issues with the Bank's own Operations Evaluation Department (OED), after conducting a survey of those using the institution's research, concluding, "for a majority of respondents, this insistence that the Bank's way is the only way underlies most [Bank] reports, strategic models, and policy analyses."[29]

As for the IMF- alongside its continuing 'adjustment lending' to poor countries – after the attacks on the World Trade Centre in September 2001 the institution was given an additional role in developing anti-money laundering schemes in an attempt to control the financing of similar terrorist acts. This is one contributing factor to an increase in the costs of the IMF by 30 per cent between 2001 and 2003.[30] The other reasons for this increase in the IMF's administration budget were more economic surveillance work and a decision to increase reserves due to a perceived greater risk from a small number of countries owing large amounts to the Fund. At the time, Argentina, Brazil and Turkey accounted for two thirds of debt owed to the General Resources Account.[31]

This risk has been short-lived. As mentioned at the beginning, Thailand has paid off its debts to the IMF and in December 2005, within two days of each other, both Brazil and Argentina announced their intention to complete early repayment of their debts to the IMF.[32,33] In May 2006, Indonesia announced its intention to repay its outstanding debts to the IMF within two years.[34] The sum total of the repayment by these three countries amounts to over $30 billion.

At the same time as several major developing countries are paying off their debts to the IMF, the US is running up the largest current account[35] deficit in history. In 2005, it ballooned to $805 billion – 7 per cent of the USA's massive national income.[36] Unlike poor countries with balance of payments problems, the USA does not need to seek help from the IMF. This is because, as mentioned earlier, the dollar is the de-facto international reserve currency. In other words, countries like China with a net surplus hold their savings in dollars which act as a kind of no-interest loan to US citizens.

Economists have been predicting that this situation cannot go on forever. The question seems not to be whether the US deficit will fall but when it will do so and whether this will be in the form of a relatively benign series of

adjustments or whether it will be in the form of a major crash with drastic economic consequences. Either way, the IMF is powerless to force either the Chinese or other net exporters to introduce policies to reduce their surpluses or to force the US to introduce policies that will cut its deficit.

These economic changes have also rendered the voting structure in the IMF obsolete and the institution is now trying to find ways to tweak its decision-making apparatus to keep some larger developing countries happy. A further shift taking place has been China's emerging use of its savings as development finance to secure and satisfy its increasing resource needs. For almost 20 years, going back to the latter days of the cold war, poor countries have had little choice but to seek development finance from western powers, with the most obvious manifestation of this being the World Bank. Accepting this finance has meant accepting the policies promoted by western governments: free markets and deregulation.

However, this period may be coming to an end with the increasing involvement of China in poor countries, particularly those in Africa. For the first time in two decades, some poor countries are getting a choice. While this may not be the most appetizing range of options there is now a distinction between finance from China that comes with no broader economic policy strings, but in all likelihood with some political and foreign policy strings, and finance from the World Bank with all its associated conditionality. It is hard to find any official World Bank reaction to China's activities, but it is likely that this new development will have rattled the World Bank hierarchy as much if not more than any civil society campaign.

It is increasingly clear that the Chinese are ambivalent about who they do business with, which has been a cue for much hand-wringing in the west about the Chinese undermining the World Bank's 'good governance' agenda by doing deals with dictators and human rights abusers. However, while in an ideal world development finance would indeed be a tool that could foster greater public scrutiny of government, better human rights and more democratic governance, the record of the World Bank and other aid donors has been poor. Whereas buying or imposing privatisation in poor countries is a relatively easy transaction that can involve a small group of technocrats with few consequences for the governing elite, this is not the case when it comes to buying or imposing democracy (which in any case would seem to be a contradiction in terms). As a result, the World Bank has often ignored this latter kind of intervention in favour of the former or, when it has tried to intervene on governance issues, has not had much success.[37]

3 The overwhelming case for change

"Today, [the World Bank and IMF] have become dominant players in the world economy. Not only countries seeking their help but also those seeking their 'seal of approval' so that they can better access international capital markets must follow their economic prescriptions, prescriptions which reflect their free market ideologies and theories."
Joseph Stiglitz, former Chief Economist, World Bank.[38]

Although recently some governments in Asia and Latin America have, to varying degrees, escaped their clutches, after more than 60 years it is clear that the influence of the IMF and World Bank in the poorest countries is greater than ever. Perhaps this is the most damning critique – particularly of the World Bank – that after 60 years, it has a bigger not smaller role in poor countries. If the role of the World Bank is to ultimately make itself obsolete, it is clearly failing.

The following chapter looks at the case for change. It examines the failed policies and inappropriate development projects; the fact that the best performers have often ignored the Bank and Fund; the evidence produced by expert commissions and UN agencies; the massive public protests against Bank and Fund policies and projects; and the lack of transparency and democracy in the IFIs. Any one of these factors presents a compelling argument for radical change. Put together, the case is overwhelming.

3.1 Decades of disasters

"After 20 years of implementing structural adjustment programs, our economy has remained weak and vulnerable and not sufficiently transformed to sustain accelerated growth and development. Poverty has become widespread, unemployment very high, manufacturing and agriculture in decline and our external and domestic debts much too heavy a burden to bear."
Kwamena Bartels, Ghanaian Minister for Works and Housing, May 2001.[39]

3.1.1 Financial crises

The IMF has received heavy criticism for its handling of various financial crises in middle-income countries: Mexico (1995), East Asia (1997-98), Russia (1998), Brazil (1998), Turkey (1998) and Argentina (2001). But perhaps the most famous is the Asian financial crisis of the late 1990s, occurring during Michel Camdessus' tenure as head of the IMF (more recently he has sat on Tony Blair's Commission for Africa). The IMF and its then leader have come under fire not only from activists and affected

people but also from governments and a growing number of economists for the policies imposed on Thailand, Indonesia and Korea in return for financial bail-outs.

Throughout the 1960s, 1970s and 1980s, East Asia was synonymous with the words ‘economic miracle’. Growth rates had been seen as high as 10 per cent, and were 6.4 per cent in Thailand, 7.6 per cent in Indonesia, and 8.0 per cent in Malaysia in the early to mid-1990s.[40] This all changed in July 1997 when East Asian economies fell like dominoes after the value of the Thai Baht dropped by 20 per cent in a week and currency speculators pulled out of the economy and then out of other East Asian countries.

Millions were thrown out of work and living standards plummeted as the economic crisis spread to Indonesia, Korea, Malaysia and the Philippines. The ‘Asian Tiger’ economies were forced to borrow heavily from the IMF to keep their economies afloat. As usual the IMF attempted to mould their economies in the image of the free market, which ended up making the recession in some countries worse rather than better.

There were three main policy areas in which the IMF used conditionality in order to change recipient’s policies: tight monetary policy (eg, high interest rates), clamping down on public spending and increasing tax revenue in an attempt to balance budgets and financial sector restructuring.

For example, in Indonesia, the required cuts in government spending led to the elimination of subsidies for basic necessities such as food and fuel.[41] This is despite the fact that, with rising unemployment and falling real wages, these subsidies were needed more than ever. The IMF subsequently agreed that it had been mistaken to demand a balanced budget, and agreed to a deficit of 8.5 per cent in Indonesia. Immediately, social spending could increase and roughly three quarters of this deficit spending was used on restoring subsidies for essential foodstuffs.[42]

The IMF has come in for heavy criticism for the policies it imposed. For example, as Joseph Stiglitz has argued, “not for sixty years have respectable economists believed that an economy going into a recession should have a balanced budget”.[43]

At the time, the IMF blamed the crisis on what it called the ‘crony capitalism’ operating in these countries. In other words it was the fault of East Asian countries for allowing forms of corruption to distort the

effective functioning of the market. Yet it is increasingly recognised that it was the taking away of controls on the movement of capital that was responsible; a policy that had been vigorously promoted by the IMF.[44] So not only did the IMF fail in its response to the crisis, it was a key advocate of the policies that created the crisis in the first place.

3.1.2 ***Russia – free market 'shock therapy'***

The fall of communism in Russia was supposed to herald a bright new prosperous future for the Russian people. However, this did not materialise as the IMF and western-sponsored economic consultants, including Jeffrey Sachs (now a prominent aid advocate), parachuted into Russia preaching radical free market economics with no account taken of how this might work in a Russian context and how this would affect Russian people. The result was dubbed economic 'shock therapy' as it constituted one of the most radical economic reform programmes ever implemented and it provided myriad opportunities for a small number of people to become unbelievably wealthy.

As Professor John Gray (now at the London School of Economics) points out: "Implemented briefly in the aftermath of the Soviet collapse, shock therapy aimed to construct a free market in post-communist Russia. It produced instead a species of mafia-dominated anarcho-capitalism."[45]

While a small elite got rich from policies such as eradicating price controls and selling off state-owned companies, the majority of Russian's suffered. For example, after getting rid of government price controls on 90 per cent of traded goods, prices rose by 250 per cent literally overnight. As one author, Robert Skidelsky commented, "in that first year Russians suffered terribly, their living standards dropping by as much as 50 per cent. They kept going only by taking to their plots of land and growing their own food."[46]

Between 1991 and 1996, consumer prices increased 1,700 times. Between 1991 and 1996, 45 million people fell into poverty in Russia.[47] In 1997, the Economist reported that, after five years of economic reform, life expectancy had dropped from 74 to 72 for women and from 62 to 58 for men, putting Russia roughly on a par with Kenya at the time.[48] While this was certainly a shock, it was hard to classify as therapy.

3.1.3 ***Inappropriate development***

The World Bank has been associated with countless development disasters causing massive social and environmental upheaval. During the 1970s

and 1980s, Bank lending for agriculture, colonisation and infrastructure in forest areas led to massive deforestation in Brazil and Indonesia. The Bank also directly financed logging in West African rainforests in the late 1980s. By the early 1990s, forest related activities had caused the largest international outcry of all World Bank lending areas. A new forestry policy was formulated in 1991 which was meant to prevent all support for logging in primary moist tropical forests. However, between 1992 and 1999, forestry lending was 78 per cent higher in nominal terms than between 1984 and 1991. As part of its so-called 'high risk, high reward' programme to provide more loans for more risky investments that have high potential returns, the Bank has now endorsed a new 'forest strategy', which seeks to engage in more lending for commercial forestry.[49]

World Bank agriculture lending resulted in similar upheaval. For example, between 1960 and 1980, 28.4 million people were displaced by World Bank sponsored agricultural reform programmes in Brazil.[50]

The World Bank has also been involved in a series of controversial dam building projects. Perhaps the most famous the Sardar Sarovar dam project in Narmada Valley, led to protests from thousands in the potentially affected area. In an unprecedented move, the Bank agreed to an independent enquiry which found the Bank culpable of 'gross delinquency', particularly with regards to the resettlement of over 200,000 poor farmers. On this occasion, the Bank decided not to fund the dam but this apparent shift away from funding such mega-projects has been short-lived with the advent of the World Bank's new 'high risk, high reward' strategy.

Sustained criticism led to the creation of the World Commission on Dams and the Extractive Industries Review (see section 3.3) and much debate over social and environmental safeguard policies but little seems to have changed in practice. For example, a recent World Bank inspection panel has criticised the World Bank for ignoring its own rules in an environmentally and socially damaging forestry project in Cambodia.[51]

3.1.4 ***Privatisation***

Privatisation has been a key feature of Bank and Fund structural adjustment lending for the past 20 years. Yet, in typical fashion, the story is of a 'one-size-fits-all' policy being imposed on all countries regardless of their different social, economic and political circumstances. This policy, particularly in the case of essential service[52] privatisation, is also based more on an erroneous theoretical assumption – that governments are

inherently bureaucratic and corrupt while private companies are inherently efficient and well managed than on real evidence that it benefits the poor.

A review of structural adjustment-related privatisation case studies concluded that privatisation of public utilities often resulted in increased charges – adversely affecting the poor – and often resulted in net unemployment.[53] A study conducted by four IMF researchers concluded that, "the empirical evidence suggests that significant reductions in employment are indeed associated with privatisation."[54]

In contrast, there is no sound evidence to suggest that public sector involvement in, or control of, essential services is necessarily and always less 'efficient' or less effective. In fact, there is a growing body of evidence to suggest that both the public sector and alternative forms of service supply (eg, not for profit and community-managed systems) can achieve levels of efficiency and effectiveness equal to or above those of the standard privatisation model.[55,56]

For instance, the IMF concludes: "It cannot be taken for granted that Public-Private Partnerships (PPPs) are more efficient than public investment and government supply of services … Much of the case for PPPs rests on the relative efficiency of the private sector. While there is an extensive literature on this subject, the theory is ambiguous and the empirical evidence is mixed."[57]

In the energy sector, an empirical global study examining the performance of both public and private energy companies concluded that in generation, transmission and distribution there is no significant difference in efficiency between the two types of operator.[58] And in the water sector, research for the World Bank Economic Review says that studies on water utilities in Asia, "show that efficiency is not significantly different in private companies than in public ones."[59]

This evidence points strongly to the conclusion that there is no intrinsic advantage to private sector operation in terms of efficiency. Equally, there is no evidence to assume that a public sector operator is intrinsically less efficient and effective.

At the same time, there is a growing body of literature cataloguing the failures of privatisation programmes all over the world from both an economic and social perspective.[60] Not only is there evidence of widespread failure

in well-publicised sectors such as water and sanitation,[61] there is also an emerging understanding of privatisation failure when it comes to less well known sectors such as providing financial services to the poor.

A recent study conducted for the IMF concludes that in poor countries, foreign bank presence is strongly associated with less credit for the private sector - particularly small and medium sized enterprises and less access to credit. This is a particular problem for the rural poor.[62] This finding is supported by recent evidence from Mozambique where bank privatisation has resulted in closure of more than half of rural branches and has reduced by a quarter the lending to farmers.[63] The lesson to draw from this is that privatised (often foreign-owned) banks are happiest lending to more homogenous big companies (often foreign-owned) rather than to the diverse indigenous private sector. Yet it is the activities of this indigenous private sector that play a critical part in development and poverty reduction.

Although not all privatisation of state-run enterprises (eg, some state-owned factories) necessarily and always has adverse impacts on the poor, and the ‘private sector’ encompasses a wide diversity of operators so cannot be stereotyped, the weight of evidence demands a major change in the approach of the Bank and Fund, particularly when it comes to essential services.

Yet, current conditionality suggests a continued zeal in the IFIs for privatisation. Recent analysis of IFI programmes in 20 countries found that 18 out of the 20 included privatisation conditions, often with a focus on essential services such as banking and energy.[64]

And despite the World Bank’s recent claims to being ideologically neutral on privatisation, it is clear from such documents as the Water Resources Sector Strategy, and its involvement in a range of financing initiatives to encourage private sector involvement in essential service delivery, that the Bank is still prioritising privatisation over funding public sector service provision or alternative forms of supply.[65]

3.1.5 ***Export-led growth***
Increasing a country’s exports has been seen by the World Bank and IMF as a principal route through which developing countries will grow their economies, with the assumption that increasing GDP growth is essential for job creation and poverty reduction. This strategy can be questioned both in terms of its underlying assumption and in terms of how it has been pursued.

In relation to the underlying assumption that GDP growth is an essential condition for poverty reduction, there is mounting evidence calling this into question. For example, work by the International Labour Organisation (ILO) demonstrates a long-term trend across the globe of failure to convert GDP growth into reduced unemployment.[66] According to the New Economics Foundation, "between 1990 and 2001, for every $100 worth of growth in the world's income per person, just $0.60 found its target and contributed to reducing poverty for those living on less than a dollar a day – 73 per cent less than in the 1980's."[67] In other words, countries were significantly worse at translating growth into poverty reduction in the 1990s than in the 1980s. It is hard to find an adjective to describe the 1990s given that the 1980s was itself dubbed 'the lost decade for development'.

After showing that GDP growth does not necessarily mean pro-poor growth, the United Nations Development Programme (UNDP) has consequently argued for different measures that better account for whether or not the lives of the poorest have improved.[68] Such an approach has yet to permeate the thinking of the World Bank, the IMF or the industrialised country governments that dominate these institutions.

The second problem with the World Bank and IMF's focus on 'export-led growth' or 'export-led development' as it is also known, is the way that it has been pursued. Most industrialised or newly-industrialised countries have moved away from communities, jobs, economies but most of all exports that are focused on agriculture. It is not an over-generalisation to say that most of these countries have pursued an active strategy to get *out* of trading agricultural commodities and *in* to trading manufactured goods. As Norwegian Economist Erik Reinert points out, "No nation has ever taken the step from being poor to being wealthy exporting raw material in the *absence of a domestic manufacturing sector*" (emphasis as in original).[69]

Although history suggests nobody gets rich by exporting low value agricultural commodities, the Bank and Fund seem to be encouraging and/or forcing poor countries to pursue just such a strategy, with disastrous results. Take the international coffee trade as a case in point.

In coffee producing countries, the World Bank and IMF have been advising or requiring governments to liberalise. This has involved measures such as eradicating controls on supply and on prices, disbanding state trading boards and actively encouraging increased production and exports. For example, in 1998, under the HIPC Initiative, Côte d'Ivoire's eligibility for

debt relief was made conditional on the full liberalisation of the coffee sector by the 1998/99 crop year.[70] This was also backed up with a second national agricultural services support project, funded by the World Bank, which sought to increase productivity for all crops, including coffee, as well as stressing the requirement to fully liberalise the coffee sector.[71]

Perhaps the greatest 'success' has been in Vietnam where the World Bank has helped promote a massive expansion of coffee growing. In 1993, for example, the World Bank funded an agricultural rehabilitation project with an aim of diversifying export income through the expansion of coffee and rubber exports.[72] Since the late 1980s, Vietnam has risen from a marginal coffee producer, producing less than 50 thousand metric tons, to one of the world's largest. By the late 1990s it was producing some 400,000 tons of coffee.[73]

During the same period, the World Bank and IMF were requiring other coffee producing nations – such as Uganda, Ethiopia and Kenya – to liberalise their agricultural sectors and were encouraging increased coffee exports. For example, a study of Uganda by the World Bank in 1993 advised the Ugandan government to plan for a greater share of the world coffee market. The study argued that Uganda "could double its coffee exports to perhaps 5 million bags, without significantly effecting medium-term international prices for Robusta coffee".[74]

Unfortunately, the study did not seem to take into account the implications of increased production and exports being encouraged by the IMF and World Bank in *other* parts of the world. The result of the oversupply has been a price collapse and a crisis in coffee producing countries. According to a World Bank study in 2002, "Coffee prices have declined sharply in recent years because of large increases in coffee production and exports from traditional exporters such as Brazil and new entrants such as Vietnam. Between July 1998 and June 2001, coffee export prices declined by almost 50 percent."[75]

Ironically, the kind of policies that now help coffee producing countries *qualify* for debt relief under HIPC (ie, reducing state intervention in coffee markets) have contributed to increased coffee production causing oversupply in the market resulting in a price crash and a commodity crisis, making their debt problems even worse.

Of course, any standard economic textbook will tell you that an increase

in supply, without an increase in demand, will lower prices. Yet it looks like the IMF and World Bank economic experts forgot, or chose to ignore, the basics as they encouraged increased production and exports and reduced state intervention across the globe.

3.1.6 Trade liberalisation

The other side of the trade equation to increasing exports is liberalising imports, which the World Bank and IMF have pushed with almost theological zeal. Trade liberalisation has been a key feature of Bank and Fund conditionality throughout the 1980s and 1990s.

Yet the United Nations Conference on Trade and Development (UNCTAD) has found that the rapid and extensive trade liberalisation undertaken by the LDCs during the 1990s failed to benefit the poor. In fact, it was associated with rising poverty, with the countries worst affected being those that had liberalised most.[76] Similarly, another UNCTAD report concludes, "The more recent evidence from liberalisation episodes in sub-Saharan Africa as well as Latin America suggests that they have often been accompanied by an increase in unemployment."[77] UNCTAD also highlights the association between liberalisation and increased wage inequality and reductions in average wages. According to calculations done for Christian Aid, trade liberalisation has cost sub-Saharan Africa $272 billion US over the past 20 years.[78]

African governments are, of course, well aware of this evidence. In a paper submitted to the Doha Round WTO negotiations, Ghana, Kenya, Nigeria, Tanzania, Uganda, Zambia and Zimbabwe point out that, subsequent to IMF and World Bank structural adjustment, including unilateral trade liberalisation, "the broad-based development that was expected to ensue has remained elusive … Indeed, empirical studies show that industrial growth has fallen behind GDP growth in Sub-Saharan Africa since the 1980s with de-industrialization in a number of African countries being associated with trade liberalisation."[79]

Table 1 opposite shows a calculation by UNCTAD of whether, and how much, poverty has been reduced in different LDCs compared to their level of trade restrictiveness. The table shows that poverty has on average *increased* in those countries categorised in the top four least trade restrictive bands. In LDCs where government intervention is greater and policy is more trade restrictive poverty has, on average, been *reduced*. But in the most closed LDC economies (ie, those ranking '10' on the

Table 1:
The impact of trade liberalisation in Least Developed Countries (LDCs) 1987-89 to 1997-99[80]

IMF trade restrictiveness index (1 = most open to trade, 10 = most restricted)	Percentage change in US$1-a-day poverty level in LDCs (figures weighted to account for more populous countries)	Percentage change in US$1-a-day poverty level in LDCs (figures with every country treated the same, regardless of population)
1	**+24**	**+16**
2	**+5**	**+5**
3	**+4**	**+2**
4	**+3**	**+8**
5	**-1**	**-3**
6	**-1**	**-1**
7	**-4**	**-4**
8	**-7**	**-10**
9	**0**	**0**
10	**+6**	**+5**

(Note: the plus sign denotes an increase in poverty, the minus sign denotes a reduction in poverty)

IMF's trade restrictiveness scale) poverty also increased. Although the IMF's measure of the trade restrictiveness of government policy may not be perfect, this table suggests that, while it is not wise to maintain a closed economy, it makes sense for poor countries to have a high degree of government intervention in trade.

The development failure caused by the Bank and Fund's insistence on import liberalisation is not only about de-industrialisation and job losses. Just as damning is the fact that the pursuit of liberalisation has been so blinkered that there is no acknowledgement that it can actually contradict the remit of both institutions.

As mentioned earlier it is strange at the very least that the IMF, a body set up to help countries with balance-of-payments problems, should be requiring recipients of its financial assistance to implement policies that will increase their imports of high value goods thus likely making their balance-of-payments problems even worse.

Trade liberalisation also creates problems for sustainable government income. Research has shown that cutting import tariffs has reduced tax revenue resulting in a fiscal squeeze, exacerbating the debt problem and causing cutbacks in infrastructure investment.[81] Although the *theory* is that governments can replace tariffs with other taxes, this is easier said than done in the real world. Two IMF researchers conducted a study

across 111 countries over 25 years on the recovery of tax revenues lost as a result of trade liberalisation and concluded that: "For middle-income countries, recovery has been in the order of 45-60 cents for each dollar of lost trade tax revenue, with signs of close to full recovery when separately identifying episodes in which trade tax revenues fell. Troublingly, however, revenue recovery has been extremely weak in low-income countries (which are those most dependent on trade tax revenues): they have recovered, at best, no more than about 30 cents of each lost dollar. Nor is there much evidence that the presence of a VAT has in itself made it easier to cope with the revenue effects of trade liberalisation."[82]

It is therefore perplexing that the World Bank, a body whose remit to promote development requires countries to *reduce* their debts and become *less* reliant on aid, should be requiring recipients of its financial assistance to implement policies that will reduce their tax base – a predictable source of income – *exacerbating* their debt problems and making them *increasingly* reliant on unpredictable, not to mention conditional, bilateral and multilateral aid.

This leads to two possible conclusions. Either the economists at the IFIs, and their political masters in the industrialised world are such believers in the power of market forces and the neo-liberal economic view of how things should work that real world evidence is simply an irrelevance to them. Or, the reduction of poor country tariffs on manufacturing goods, coupled with the Bank and Fund's export-led growth strategy in agricultural commodities is actually a deliberate political attempt to prevent their industrialisation and permanently lock these countries into being low value agricultural exporters.

Whatever the motives, the IFI liberalisation push continues. As outlined in section 3.5 below, the content of PRSPs is heavily influenced by the World Bank and IMF and is used as the basis for defining Bank and Fund policy conditionality.

WDM's analysis of recent PRSPs shows that there are further trade liberalisation measures in 72 per cent of the PRSPs on top of the significant trade liberalisation that has already happened in many of these countries.[83] Despite compelling evidence of the need to be pursuing different trade policies, it was hard to find these in in PRSPs. One example was Ghana's which mentions holding a review of trade liberalisation.[84]

True to the policy outlined in its PRSP, in 2003 the Ghanaian Parliament

passed a budget to increase the import duty on poultry products to protect Ghanaian farmers who were being priced out of the domestic market by subsidised European poultry. However, after a phone call from the IMF, the legislated increase was removed by the Ghanaian government after just two weeks. Even though Ghana had managed to mention reviewing trade liberalisation in the PRSP, and then subsequently implemented an 'alternative policy', it was pressured by the IMF to revert back to trade liberalisation.[85]

3.1.7 User fees

Starting in the 1980s, user fees for health and primary education were pushed as conditions of World Bank programmes. In a 1998 internal review of the Bank's Health, Nutrition and Population (HNP) lending, the Operations Evaluation Department (OED) reported that 40 per cent of HNP projects, and specifically 75 per cent of HNP projects in sub-Saharan Africa, included the establishment or expansion of user fees.[86] Studies have consistently shown that fees have reduced the poor's access to essential services.[87]

For example, with the implementation of fees for health services in Ghana in the late 1980s, a visit to a specialist cost ten times the daily wage. Unsurprisingly, there were "substantial declines in the utilisation of health care services. The decline was greater and more sustained in rural than in urban areas."[88]

As for Zambia, the World Bank reported in 1994 that with the introduction of user fees in health provision, "vulnerable groups seem to have been denied access to health services."[89] However, this was followed by a new Bank health project to increase the use of user fees.[90]

UNCTAD has criticised the use of user fees as, "undue emphasis is placed on market mechanisms"[91] and has called for their removal from anti-poverty policies.[92] Former executive director James Wolfensohn stated that the Bank no longer promotes user fees for basic health and education. However, Bank programmes which make countries delegate responsibility for delivering a service to local communities often include a requirement for user fees, as a community has no other way of raising finance internally.[93]

In contrast, where user fees have been abolished improvements have been seen. For example, when Malawi eliminated a small school fee in 1994, primary enrolment increased by 50 per cent from 1.9 to 2.9 million pupils.

3.2 Successful development strategy: ignore the Bank and Fund

"There is growing recognition that the IMF should not be interfering too deeply in sovereign affairs...when firemen come to your house to put out a blaze you would not expect them to meddle in your marriage."
Charles Wyplosz, Professor of Economics, Institute of International Studies, Geneva.[94]

A damning indictment of the failure of the free market model pushed by the World Bank and IMF is the fact that those countries that have developed most successfully have often been those that have ignored the Bank and Fund and pursued their own path to development.

For example, on the issue of trade liberalisation – even looking at countries using the IFI's own standard of economic growth – we can see that between 1996 and 2000 four of the top five fastest growing developing countries were those deemed to have 'trade restrictive' policies (Equatorial Guinea, China, Mozambique, and the Dominican Republic).[95] Although no data was available on the fifth, the Maldives, and Equatorial Guinea's growth can be ascribed to its oil wealth, the other three countries at the very least call into question the 'liberalisation leads to growth' dogma. More importantly, in terms of improving peoples lives, the table in section 3.1.6 above clearly shows that more interventionist LDCs have been more successful in reducing poverty.

Similarly, although during the 1990s the IMF ranked Mauritius as one of the most protected economies in the world,[96] between 1975 and 1999 the country achieved an average annual per capita growth rate of 4.2 per cent and a reduction in income inequality. The policy choices and the success demonstrated by Mauritius are perhaps no surprise, given that since 1988, the country has not owed the IMF any money under its structural adjustment programs so has not been subject to IMF conditionality.[97]

A similar story exists in terms of investment liberalisation. The more successful countries in East Asia, not to mention industrialised countries such as the USA and various European countries, used a variety of controls on foreign direct investment (FDI) to ensure that when FDI was allowed it produced benefits for local people.[98]

And the same trend can be seen when it comes to financial crises. Those that ignore the standard prescriptions of the IMF tend to do better. Perhaps the most cited example is that of Malaysia. Commenting on the Asian

financial crisis, Joseph Stiglitz said, "I think it is no accident that the only major East Asian country, China, to avert the crisis took a course directly opposite that advocated by the IMF, and that the country with the shortest downturn, Malaysia, also explicitly rejected an IMF strategy."[99]

In an ironic twist, in 2003 Malaysian president Mahathir Mohamad was the opening speaker at Davos; a place where deregulation, including financial deregulation, and unfettered markets had been the rallying cry for over two decades. As one author writes, "He excoriated global and economic policies, rightly boasted of Malaysia's success following a national regulated model and received a rapturous standing ovation."[100]

This is not to say that more successful countries have not liberalised at all. They have simply done so at times and in sectors that are deemed appropriate in achieving development progress. But critically, these countries have still maintained various degrees of control over trade policy, foreign investment and foreign capital so that if a policy approach is not working they have the ability to change course.

3.3 Ignoring people, ignoring the evidence

Another compelling argument for radical change of the World Bank and IMF is that they seem incapable of responding effectively to expert advice and public protest.

3.3.1 The Structural Adjustment Participatory Review Initiative (SAPRI)

In 1996, in response to widespread public protest, the World Bank agreed to conduct a joint World Bank non-governmental organisation (NGO) evaluation of its SAPs. The result was the launch of the Structural Adjustment Participatory Review Initiative (SAPRI) in 1997, a joint multi-year investigation across a range of countries including Bangladesh, El Salvador, Uganda and Hungary.

Once they realised that the process was unlikely to provide a ringing endorsement of their policies, the Bank hierarchy steadily withdrew from the process and ultimately refused to participate in collating and publicising the findings of the various case studies. After a year of public pressure, in 2002 then president of the World Bank James Wolfensohn went so far as to acknowledge the findings as 'important' and 'legitimate'. However, those NGOs involved in the SAPRI Initiative have been left disappointed, if not unsurprised, by the failure of the Bank to clearly

translate the findings of this study into meaningful changes in its approach towards structural adjustment.[101]

3.3.2 The World Commission on Dams (WCD)

In 1998, the World Bank appointed an independent WCD to investigate the economic, social and environmental implications of large dam building and make recommendations for Bank funding policy.[102] The WCD comprised 12 representatives from various backgrounds including industry, government and dam-affected peoples. After 30 months of intensive work, the WCD concluded that a range of social and environmental problems associated with large dams need to be addressed and that the rights of all people, particularly indigenous peoples, must be respected. The WCD recommended the Bank adopt a new approach to decision-making based on the principles of equity, efficiency, participatory decision-making, sustainability and accountability and produced guidelines for how this could be achieved.[103]

The Bank has not formally adopted these recommendations and if anything is going in the opposite direction. After some years of little or no involvement in funding major dam projects, the Bank developed a Water Resources Sector Strategy in 2003, which was criticised by the WCD commissioners, endorsing high-risk dam building as part of its contribution to water sector development.[104] In late 2003, the Economic Times of India reported that the process for Bank funding of major hydro-power projects in India was once again underway.[105] More recently it has been reported that the World Bank is involved in a major dam project in Pakistan.[106]

3.3.3 The Extractive Industries Review (EIR)

In the summer of 2001, then World Bank president James Wolfensohn appointed Proffessor Emil Salim, former Indonesian population and environment minister, to lead a consultation process called the Extractive Industries Review (EIR). According to the EIR web site, “The Extractive Industries Review was launched by the World Bank Group to discuss its future role in the extractive industries with concerned stakeholders. The aim of this independent review was to produce a set of recommendations that will guide involvement of the World Bank Group in the oil, gas and mining sectors.”[107]

The EIR submitted its final report in December 2003, making a series of progressive recommendations to change Bank funding policy. The report demonstrates that World Bank funding for oil and mining does not benefit local communities, protect basic human rights or the environment in the

majority of cases. The report recommends, amongst other things, that the Bank phase out funding for oil and coal extraction, increase funding for renewable energy projects, ensure prior informed consent for indigenous and project-affected peoples, and end support for destructive mining technologies.[108]

The Bank has refused to adopt the findings of the EIR and is in fact developing a 'high-risk high-reward' strategy that will, if anything, see an increase in its involvement in the extractive sector and reduce its adherence to social and environmental safeguards.[109] The Bank has recently been involved in an extremely controversial oil pipeline project – the Baku-Tiblisi-Ceyhan (BTC) pipeline – which has come in for massive criticism on social, environmental and human rights grounds.[110]

3.3.4 Countless public protests

Since late 1999, WDM has been documenting widespread and continuing resistance to World Bank and IMF imposed economic policies all over the developing world.[111] Between 1999 and 2003, WDM documented some 238 separate incidents of civil unrest involving millions of people across 34 countries. Many of these incidents ended with the deployment of riot police or the army, resulting in almost 100 documented fatalities, with arrests and injuries running into thousands.

These WDM reports clearly demonstrate that those affected by, and protesting against, IMF and World Bank policies are not only the poorest of the poor, such as peasant farmers, indigenous peoples and the unemployed. They are also the newly-emerging middle classes: teachers, civil servants, priests, doctors, public sector workers, trade union activists and owners of small businesses. The Bank and Fund are also ignoring national parliaments.[112]

Up to now the World Bank and IMF seem to have viewed public protest or parliamentary opposition as a hurdle for developing country governments to jump over in order to get to the finish line, rather than a reason to change the direction of policy. Such opposition tends to be dismissed by the IMF and World Bank as pleading by 'vested interest elites' blocking what the Bank and Fund claim is pro-poor policy reform. Yet the breadth and recurrence of public and parliamentary opposition to these policies in developing countries suggest otherwise. And even if this were true in some cases, it provides no justification for the IMF and World Bank to bypass national democratic processes in poor countries.

As former World Bank chief economist, Joseph Stiglitz states, "In theory,

the fund [IMF] supports democratic institutions in the nations it assists. In practice, it undermines the democratic process by imposing policies."[113]

3.4 Untransparent and undemocratic

The voting rights in the Bank and Fund determine the make-up of the 24 member group of executive directors, the day to day decision-making body of the two institutions. By each having over 2.5 per cent of votes in the IMF, the US, Japan, Germany, France, the UK, China, Saudi Arabia and Russia are able to have their own executive director. Other states have to band together and share an executive director. A group of 24, primarily francophone African countries share one executive director; a group of 19 primarily anglophone African countries share another. In the World Bank, again the US, Japan, Germany, France, the UK, China, Saudi Arabia and Russia all have one executive director each. 46 countries, on the other hand, have to share two executive directors between them.

These institutional structures of the World Bank and IMF were a product of their time. For example, the IBRD was initially funded significantly by the USA and was used primarily by European countries, so it would have made sense in 1944 for the USA and Europe to have the lion's share of the votes. It also has to be recognised that the colonial attitude towards developing countries prevailing at the time would have likely meant that few people in industrialised countries thought twice about their governments carving up most of the votes in both the IMF and World Bank between themselves. However, since the World Bank and IMF were created in 1944, the world has changed dramatically.

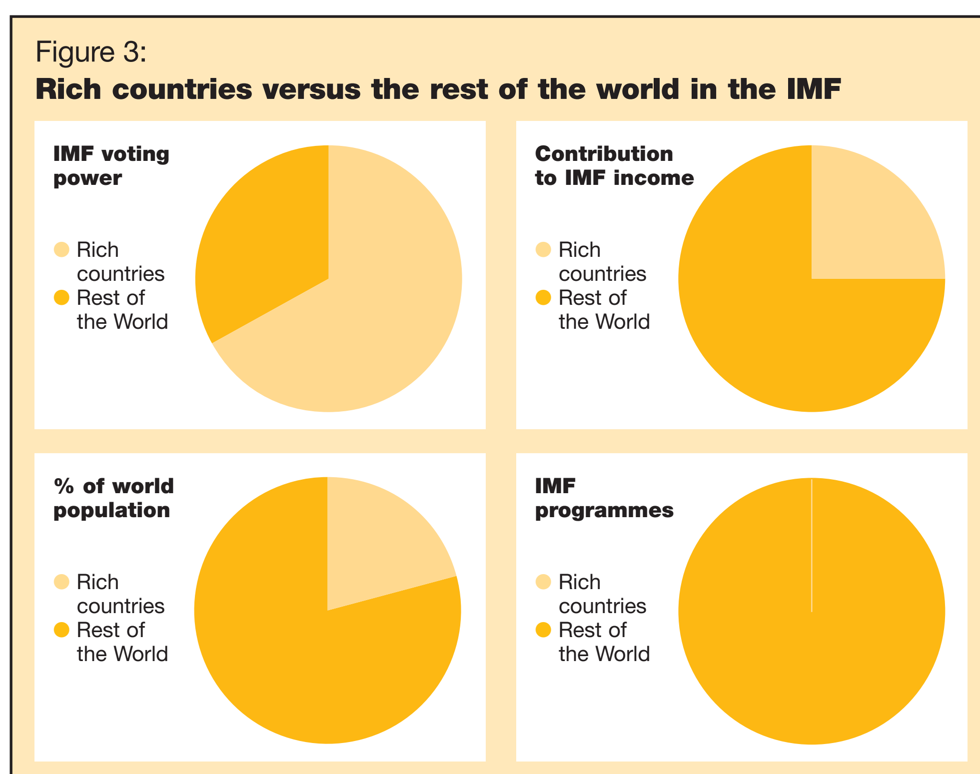
The fact that developing countries and economies in transition have become the principal users of the IMF and World Bank has resulted in a shift in the way the IFIs are funded. For example, as Table 2 shows, the debtor nations (developing countries and economies in transition) now contribute 75 per cent of the IMF's income.

Table 2:
Relative contributions to the IMF[114]

Year	Debtors	Creditors
1982	**27.7**	**72.3**
1992	**44.9**	**55.1**
2002	**75.0**	**25.0**

As one author points out: "It is often assumed that there is a simple congruence between who funds the IMF and who has the largest say in the organisation. This is misleading. The largest shareholders in the IMF enjoy the lion's share of the votes but the actual expenses of running the institution are paid for out of income. The IMF's income is mainly made up of the charges it levies on borrowers. A very small income is generated from other accounts. It bears noting that these charges have been increased substantially since the 1970s, putting a high burden on borrowing countries."[115]

Figure 3:
Rich countries versus the rest of the world in the IMF



As Figure 3 shows, although rich countries have about two thirds of the voting power in the IMF, they contribute about a quarter of its income, have less than a quarter of the world's population and are subject to none of the IMF's programmes.

The situation in the IBRD arm of the World Bank is slightly different with a much closer relationship between country contributions of the IBRD's equity capital and their voting shares. With the IDA, the most concessional

lending arm of the World Bank, rich countries contribute directly to the institution's income but, with the exception of UK and France, the voting shares are well out of proportion with their contribution (see table 3).

Table 3:
Selected contributions towards, and voting shares in, the IDA

Country	Contributions towards IDA income (%)	Voting share in IDA (%)
USA	**5.5**	**15.09**
UK	**5.3**	**4.97**
Japan	**4.9**	**10.86**
Germany	**3.3**	**6.99**
France	**3.8**	**4.24**

So even the crude 'dollars for votes' relationship that is commonly perceived to operate in the World Bank, is only partially implemented in the IDA.

And where 'the dollars for votes' system is operating more fully (in the IBRD) it has to be questioned as a basis for decision-making in a public interest development institution. Rather than reflecting this international public interest remit, the situation in the IBRD broadly equates to that of a commercial lender with shareholders. However, whereas in the commercial world shares can be bought and sold as financial interests change, contributions towards IBRD equity (ie, shares) can only be changed by a vote at the board (on which the US has a veto) where voting strength is the result of the original share carve-up dreamt up in the 1940s.

In terms of the day to day operating costs of the IMF and World Bank, as one author has pointed out, "the overheads and running costs of the institutions are paid for out of income which derives mainly from payments by developing and transition country members who borrow money from the institutions. In fact, their payments amount to a considerable inward investment into the economy of Washington DC."[116]

The undemocratic make-up of the IFI boards is compounded by a lack of transparency in their operation. Still beyond the reach of the public is any knowledge of *how* decisions have been reached and what the process and reasoning was behind the decisions.

For example, at the IMF, executive board documents are published after

five years, executive board minutes are released after ten years, and other archived material is available after 20 years. The time lag means no decisions can be scrutinised until well after they have been implemented. Even when documents are released, they are only available at the IMF's offices in Washington DC.[117] This effectively makes even the archives inaccessible to most politicians, groups and individuals outside of the United States, an appalling situation for a global institution.

Normally there is no formal vote on decisions taken by executive directors. The UK Treasury states that instead they "are taken on the basis of consensus".[118] In practice this does not mean that all executive directors come to agree on the decision to be taken. In reality, once the chair of the board meeting informally senses a majority of votes has been found on an issue, executive directors in opposition to the informal majority have little choice but to 'join the consensus'. Those countries with dominant voting positions on the board can collectively impose decisions, whilst claiming a 'consensus' had been reached on the issue. And individual executive directors cannot be held accountable for their role in decisions that are taken.

Formal votes are held by the IMF board of governors, but only on a small number of organisational and administrative decisions. The UK Treasury proudly states that it publishes the UK position on these votes. However, this adds little to knowledge on the UK's role in IMF decision-making and its input into IMF policy toward specific countries. In 2003, the five issues voted on were: closure of the twelfth general review of quotas; direct remuneration of executive directors and their alternates; financial statements, report on audit, and administrative capital budgets; amendments of the rules and regulations; 2004 annual meetings change in date.[119] The fact that the UK is only willing to publish the UK's position on decisions of little significance is clearly no great boost to democratic scrutiny of the IFIs. It is possible to discover whether the UK government supported or opposed a shift in the date of a meeting, but not whether they supported the many examples of democracy being undermined in debtor countries which this report has outlined.

Similarly untransparent and outdated is the way the president of the World Bank and managing director of the IMF are appointed. For their entire history, managing directors of the Fund and presidents of the Bank have been selected through an agreement between the US and European states. a US national has always been president of the World Bank, a European has always been managing director of the IMF. Their respective voting

powers have allowed the rich western states to maintain a stranglehold over the nationality of the top positions in the two institutions.

This process was most recently repeated in 2004, with the selection of Rodrigo de Rato as the new head of the IMF. In the spring of 2004, a recruitment process for managing director of the IMF was unexpectedly initiated when Horst Kohler resigned in order to stand for the German presidency. The G24 group of developing countries called for a "democratic and participatory process based on merit regardless of nationality".[120] The G-11 group of countries in Asia, Africa, Latin America, and the Middle East issued a joint statement with Russia, Australia and Switzerland saying that the process for selecting a new managing director should be open and transparent.[121] IMF staff even expressed concern over the process. Jack Boorman, head of policy development and review, wrote an email to other staff members stating: "The Fund cannot preach transparency, good governance and other virtues to the membership and to the international community more broadly unless it is willing to apply those virtues in its own decision-making."[122]

Despite all these concerns, governments of the European Union (EU) took it upon themselves to select the managing director from Europe. In its 2000 'White Paper on Globalisation', the UK government had stated, "the UK favours open and competitive processes for the selection of top management [of the IMF and other international financial institutions]. This could include a definition of the competencies for the post, selection and search committees and a clear process for taking the final decision, in which competence would be put above consideration of nationality."[123]

However, when it came to the actual recruitment process, the UK supported the continuation of appointing a candidate from the EU, and engaged in horse-trading between EU governments to ensure it was the European that they wanted. Reports throughout the process indicated that the UK Treasury, led by Gordon Brown, was backing Spanish Finance Minister Rodrigo Rato for the post.[124] Mr Rato duly won the EU nomination after UK support helped see off candidates from Italy and France. With the EU agreed on one candidate between themselves, the US maintained the *quid pro quo*, leaving the rest of the world unable to influence the decision. The process was far from transparent, open or democratic.

As the Financial Times commented: "The puff of white smoke has appeared from the conclave of European finance ministers … Despite the

attempts of some European ministers to portray their deliberations as a broad and transparent consultation among the Fund's member countries, in reality it was barely changed from the same old closed-door stitch-up that has disfigured past appointments." [125]

The unwillingness of European countries to abandon this anachronistic charade in 2004 returned to haunt them in 2005 with the appointment of Paul Wolfowitz – well known 'hawk' of the Bush administration – as the president of the World Bank. Although the UK government was quick to support the US administration's nomination of Wolfowitz as James Wolfensohn's replacement, several other European governments were reported to be unhappy. However, they were in no position to demand an open and transparent selection process given US support for Rodrigo Rato in 2004.

While the selection process for the heads of these institutions is not as important as the make-up and operation of the boards, the fact that it remains a political carve-up rather than an open and transparent process is symbolic of EU and US hypocrisy in preaching good governance and democracy to the rest of the world but refusing to practice it themselves.

As for the UK government, despite its six year old commitment to an open and transparent selection processes, and despite a similar recommendation being made by Tony Blair's Africa Commission, it has remained unwilling or unable to influence either Europe or the USA on this matter. The UK is left desperately pointing towards elements of transparency it claims are creeping into the process as signs of progress, while most other governments do not even bother trying to defend the current system, preferring instead to maintain an embarrassed or belligerent silence.

3.5 Different names: same old policies

In May 2004, the World Bank sponsored a conference in Beijing, China, aimed at examining successful development policies and practices. In his keynote address, then World Bank president James Wolfensohn claimed that the Washington Consensus no longer exists. This latest proclamation is hard to take seriously because it is just the latest in a long line of grand rhetorical statements and superficial public relations manoeuvres emanating from the World Bank and IMF.

For example, in the late 1990s, the IMF's Enhanced Structural Adjustment Facility (ESAF), formerly the Structural Adjustment Facility (SAF), changed

its name to the Poverty Reduction Growth Facility (PRGF). However, the content of PRGF loans is little, if any different from ESAF loans.

Similarly, in the late 1990s the World Bank changed the name of the Enhanced Structural Adjustment Credit (ESAC), formerly the Structural Adjustment Credit (SAC), to the Poverty Reduction Support Credit (PRSC). However, the content of PRSC loans is little if any different from ESAC loans.

The World Bank is no longer using the term 'adjustment lending' to define its involvement in programmes (as opposed to projects) but has instead changed the name to 'development policy lending'. And perhaps the flagship initiative was to change National Development Plans into 'country-owned' Poverty Reduction Strategy Papers (PRSPs).

Yet, despite all these name changes, the reality on the ground remains little changed. Poor countries are faced with an international financial landscape where loans, debt relief and aid are all subject to meeting economic policy conditions determined by the IMF and World Bank and their political masters in the developed world. To obtain low-interest loans from the Bank and Fund, a country has to agree a programme with economic conditions attached. To receive debt relief through the HIPC Initiative or the new debt cancellation scheme, countries must have an IMF programme in place, implement further conditions contained in their 'decision point' document which are agreed with the Bank and Fund, and create and implement a PRSP. And many donors often require a country to be 'on-track' with an IMF programme before they will disburse aid.

Economic policy conditionality can also be more subtle. The IDA allocates its lending on the basis of Country Policy and Institutional Assessments (CPIAs). This works as a scorecard that ranks countries on the basis of the policies a country follows. 'Good' policies that give a high rating include: an average trade tariff of 10 per cent or less; no foreign exchange restrictions on long-term capital inflows; equal treatment of foreign and domestic investors; and the bulk of government revenues coming from 'low-distortion' taxes such as VAT and property tax.[126] By allocating money on the basis of already implemented economic policy reforms, policy scorecards are a form of conditionality in disguise.

'Country-owned' PRSPs must therefore be seen in a broader context of the mechanisms, both overt and more subtle, that donor institutions and donor governments use to influence the policies of poor countries. It is

nevertheless worthwhile examining whether PRSPs and the donor rhetoric on country ownership and participation stand up to close scrutiny.

WDM's own analysis of the first four full PRSPs and twelve interim PRSPs in 2001 demonstrated that the policy content of these strategies did not constitute a major change from the past. The report concluded: "The core macro-economic elements have changed little from the old SAPs with a continued adherence to privatisation, liberalisation and a reduced role for the state."[127] A similar conclusion was reached by Jubilee 2000 Zambia which stated that, "there is actually no major change in the shift by the two financial institutions. The move of renaming ESAF as PRGF is only an attempt to add poverty reduction into SAPs without changing the actual policy conditions."[128]

Subsequently, civil society organisations in three countries – Bangladesh, Pakistan and Sri Lanka – rejected their countries' PRSPs because consultation procedures were inadequate. In April 2003 it was reported that campaigners slated the Sri Lankan PRSP because it had "been drafted without any consultation of civil society and differs very little from previous IMF recommendations."[129] Similar criticisms of World Bank and IMF-dominated processes; lack of real civil society involvement and little consideration of alternative policies; were levelled at the PRSP processes in Malawi,[130] Benin,[131] Mali,[132] Uganda,[133] Mozambique[134] and Tanzania.[135] As one study looking at a range of PRSPs concluded, "PRSPs from wildly divergent countries reveal great universality in vocabulary, process, form, content and even prescription."[136]

In 2003, WDM's analysis of the decision point documents for the 26 countries that had progressed under HIPC was revealing, if not particularly surprising. Of these 26 documents, all mentioned a previous privatisation programme and an ongoing/future privatisation process. 15 specifically mentioned planned privatisation in public utilities or basic services such as energy, telecommunications, water and transport.[137] 23 mentioned past efforts to liberalise trade and 11 indicated a continuing trade liberalisation process.

WDM has subsequently analysed the 50 PRSPs signed-off by the IMF and World Bank and made publicly available by the end of August 2005, 28 of which are in HIPC countries and 22 in non-HIPCs. The analysis looks at nine fairly standard policy prescriptions that have comprised a major part of the so-called 'Washington Consensus' imposed on poor countries by the IFIs during the 1980s and 1990s: strict monetary policy,

strict fiscal policy, trade liberalisation, privatisation (generally), water privatisation/greater private sector involvement in water supply (more specifically), investment deregulation, capital account/financial liberalisation, agricultural liberalisation and increased labour market flexibility. WDM has assessed whether each policy was clearly mentioned in the PRSP, not mentioned in the PRSP or whether what could be considered an 'unorthodox policy' or a review of the policy had been included in the PRSP. While not intended as an exact guide to all the economic policies of PRSP countries, this exercise has yielded some striking results.

If countries were really free to promote their own choice of poverty reduction strategy in PRSPs, we would surely expect significant variation between countries and adaptation of policies to suit local circumstances rather than a high degree of similarity. We would surely expect a range of 'alternative' approaches rather than an adherence to the narrow confines of the Washington Consensus. However, this is not the case. The main findings of WDM's research are:

- There are further trade liberalisation measures in 72 per cent of the PRSPs on top of the significant trade liberalisation that has already happened in many of these countries. In only two cases is what might be considered an 'alternative trade policy' included in the PRSP; Laos recognises a need for protection of certain sectors,[138] while Ghana talks of holding a review of trade liberalisation policy[139] As already mentioned, even though Ghana then implemented an alternative policy, it was pressured by the IMF to revert back to trade liberalisation.[140]

- 90 per cent of the PRSPs include privatisation and 62 per cent specifically include water privatisation/greater private sector involvement in water supply services. The persistent failure of the private sector to deliver better water and sanitation to the poor has led UN-Habitat, international experts on urban development, to conclude: "[Increasing private sector involvement] is not a 'solution' that should be promoted internationally in the name of those who currently lack adequate water and sanitation."[141] Again, despite this evidence, none of the PRSPs include a review of any privatisation policies or a specific goal to keep water and sanitation under public management.

- 64 per cent of PRSPs include investment deregulation and none mention the need to regulate investors to ensure reinvestment of profits in the country, joint ventures with local companies, technology transfer or

employment of local people, all of which are policies recognised by development policy analysts as potentially useful in creating spillover benefits for domestic economies from FDI.[142]

- 96 per cent of PRSPs include fiscal stringency; normally that the government should not resort to borrowing from the domestic economy. Vietnam's PRSP does not have detail on its fiscal policy,[143] while Tanzania's is the only one that explicitly says a fiscal deficit is allowed, stating it should be maintained "at a modest level"[144] Yet, as Cambridge economist Ha-Joon Chang argues, "Historically, periods of rapid economic growth in Continental Europe, the USA and Japan were associated with large programmes of public expenditure and even large budget deficits."[145] Denying governments the ability to borrow domestically seriously hinders their ability to manage the economy.

The homogeneity of PRSPs across such a range of widely differing countries, and the dearth of alternative policy approaches on these key economic issues, suggests that ownership of the economic policies in such countries is still a pipedream.

There are three reasons why it has been extremely difficult, if not impossible, for the poorest countries to truly determine their own development strategies. First, the content of PRSPs is influenced by pre-existing World Bank and IMF programme conditions. Rather than start afresh, these IFI determined policies are generally 'cut-and-pasted' into the PRSP with no further analysis or scrutiny. For example, in the Gambia, Ghana, Guinea, Malawi, Mali, Mozambique, Nicaragua, Sierra Leone and Yemen, water privatisation was already a condition of a Bank and/or Fund programme *before* being included in the PRSP. These countries had little choice but to include water privatisation within the document. In theory then, IMF and World Bank policy conditions are determined by the content of PRSPs, but in practice, in many cases the PRSP content is determined by already existing IMF and World Bank conditions.

Second, even in the absence of previous conditions, representatives of the World Bank and IMF tend to have significant influence over the content of the PRSP. There are numerous examples of IFI staff telling country officials of policies that need to be included, and changes that need to be made, in the final PRSP document.[146]

Third, and perhaps most tellingly, the final PRSPs are signed-off by the

boards of both the IMF and World Bank. If country directors on the board do not like the content of a PRSP, they can just reject it. The PRSP will then need to be redrafted to meet the board's expectations, and debt relief, aid and new loans will be withheld until it is.

However, the IFI boards may not need to take such drastic steps. The requirement for sign-off already ensures the government produces a document likely to be acceptable to the Bank and Fund, and after a decade or more of structural adjustment in most countries, governments are fully aware of what the IMF and World Bank expect. As one Finance Minister has revealed: "We don't wish to second guess the Fund. We prefer to give them what they want before they start lecturing us about this and that. By doing so, we send a clear message that we know what we are doing – ie, we believe in structural adjustment."[147]

The World Bank's Operations Evaluation Department (OED) has itself concluded: "The Bank management's process for presenting a PRSP to the board undermines ownership. Stakeholders perceive this practice as 'Washington signing off' on a supposedly country owned strategy."[148]

In conclusion, all we have really seen in response from the Bank and Fund is a series of worthy statements and name changes aimed at conveying the impression that these institutions are listening and learning. This year, there is talk of tinkering with the IMF's voting structure to keep some larger developing countries happy but this will not in any way tackle the fundamental inequities in decision-making. The lesson is clear: the World Bank and IMF are pass masters at presenting old wine in new bottles; but lasting and meaningful change has been more difficult to come by.

4 WDM's agenda for change

"You will not hear anybody argue that if the IMF and World Bank were to be created now, they would be formed in the same way."
Nancy Birdsall, Centre for Global Development, 2004.[149]

It is clearly time to rethink the IFIs. After so many problems and so much rhetoric backed by minimal action, a radical agenda is needed. This chapter firstly sets out some broad principles on which WDM believes IFIs should be based, and then provides a set of more concrete suggestions that could make these principles a reality.

Box 2:
The case against the World Bank summarised

- The World Bank is clearly undemocratic in the way it operates (eg, vote weighting, choice of president etc).
- The World Bank is clearly untransparent in the way that it operates (eg, detailed minutes are not made public, votes are kept secret).
- The World Bank is not poverty-focused but instead is corporate-focused (eg, providing finance to companies through the IFC and MIGA and pushing policies that benefit multinationals rather than poor people).
- The World Bank's economic conditionality has been unsuccessful, undemocratic and unfair. Many countries have suffered and the World Bank has ignored public protest.
- The World Bank has been involved in a series of environmental and human rights disasters (eg, loans for dam building, pipeline building, mining, logging etc).
- The World Bank has been unable to reform effectively – changing names rather than policies or practices.
- Developing countries that have achieved poverty reduction have often been those that have ignored the standard policy prescriptions of the World Bank.
- The World Bank has ignored evidence and recommendations produced by its own commissions.

Box 3:
The case against the IMF summarised

- The IMF is clearly undemocratic in the way it operates (eg, vote weighting, choice of managing director etc).
- The IMF is clearly untransparent in the way that it operates (eg, minutes are not made public, votes are kept secret).
- The IMF has failed time and time again both to anticipate, and then to successfully intervene in financial crises.
- The IMF is not a 'development institution' yet is increasingly involved in lending to, and dictating the policies of, the poorest countries.
- The IMF has consistently failed to secure a sustainable exit from balance-of-payments problems in the poorest countries.
- The IMF's economic conditionality has been unsuccessful, undemocratic and unfair. Many countries have suffered and the IMF has ignored public protest.
- The IMF has been unable to reform – instead changing names rather than policies or practices.
- Developing countries that have achieved poverty reduction have often been those that have ignored the standard policy prescriptions of the IMF.

4.1 Broad principles for international financial institutions

Before attempting to set out more detailed proposals on how IFIs might work, it is worth taking a step back and considering the broader principles on which the remit and functioning of these institutions should be based. WDM suggests that the following principles would be a good starting point.

- They should be democratically accountable to member countries with decision-making processes that minimise the potential for political bullying and ensure no country or small group of countries can operate a veto.
- They should support economic democracy ensuring countries have full ownership over their economic strategies, enabling different economic policies to be pursued.
- They should not create the potential for unpayable debts.
- They should act according to need.
- Decision-making should be transparent to enable accountability to parliaments and the public and recruitment of all employees should meet equal opportunities best practice.

4.2 Scrap the World Bank: create a new body to fund development

WDM believes there is a need for an international institution, or series of regional institutions, to provide grants and highly concessional loans for poor countries. Although not addressed in this report, the international aid system has been severely criticised for unwieldy bureaucracy and incoherence. While it is up to individual industrialised countries to decide whether to have their own development agencies, it would certainly make more sense to disburse a higher proportion of overall aid through a single institution.

The World Bank, in its current form, cannot make the above principles real. WDM proposes to replace it with a completely different institution, for the purposes of this report we will call it the World Development Fund (WDF), whose remit and ways of working could include the following.

Creating a system of independent financing
Currently, the income of IDA can be a little unpredictable as it depends on donors making commitments every few years. At the same time the direct relationship between donor aid budgets and IDA, although for most countries out of proportion with their voting share, at least creates the perception that donors should have a right to decide how IDA operates.

A system based on globally-levied taxes to finance a WDF could reduce both problems. Potential for taxes on the arms trade, financial transactions, air tickets and air fuels have all been considered by the technical group on innovative financing mechanisms set up by several governments including Brazil and France.[150] The findings of this group are that there are few if any technical reasons why one or more of these taxes could not be created.

Such a system is not intended to rebalance the funding for development between rich and poor countries. Clearly any of these taxes would generate a larger share of the overall revenue from the industrialised world. The idea is to reduce the direct link between donor aid budgets and funding the institution in order to facilitate a fairer decision-making structure (see below).

Altering the system of grants and loans
Ideally, a WDF should be solely a grant-giving institution when it comes to low income countries. A possible derogation from this might be to provide low or no-interest loans to the poorest countries to fund development projects with a very good potential rate of return.

Depending on its level of financing, a WDF could also provide loans to middle income countries on more favourable terms than the IBRD currently does.

Seeing aid as global social security: redistribution as a right
Part of the problem with the aid system and its bureaucracy is the amount of effort that goes into determining who should qualify for aid and then reporting back on how aid money has been spent.

A different way of looking at the disbursement of grants by a WDF would be as an entitlement based on need. In the same way that poor people in many countries are entitled to social security payments with no strings attached relating to how the money is used, poor countries could be entitled to a basic allocation of aid depending on the degree of poverty. The CPIA criteria and conditionality could simply be dispensed with.

In addition to this basic budget support, a WDF could also still dispense some of its funding through particular targeted programmes (eg, The Global Alliance for Vaccines and Immunisation).

Of course, this approach comes up against the problem of giving money to corrupt or undemocratic regimes. However, neither bilateral donors nor the World Bank have a particularly exemplary record at defining and targeting 'good governments' and/or using aid as a tool to achieve greater transparency and democracy.

One possible way to address this, which has had some experimental success, is disbursing aid directly to individuals. This could always be considered as part of the WDF's way of working.

Alternative systems that use the above as a basic premise but include varying degrees of complexity and intervention are as follows.

- The same system as above but also involving the denial of grants to countries currently subject to UN sanctions.
- A basic unconditional entitlement of grant funding for all countries either based on need or as a flat rate for all. In addition, extra funding available to be disbursed to governments that are already meeting certain transparency/democracy criteria determined by the WDF or by a UN body.[151]

- A basic unconditional entitlement of grant funding for all countries either calculated based on need or as a flat rate for all. In addition, extra funding available to be disbursed to governments that agree to implement transparency and democracy reforms aimed at ensuring greater public and parliamentary scrutiny of how money is spent. The reforms in question could be determined and monitored by the WDF and thus ultimately scrutinised by its board.

- A basic unconditional entitlement of grant funding for all countries either calculated based on need or as a flat rate for all. In addition, extra funding available to be disbursed to governments that agree to implement transparency and democracy reforms aimed at ensuring greater public and parliamentary scrutiny of how money is spent. The reforms in question could be determined and monitored by the WDF and thus ultimately scrutinised by its board. The WDF could also use extra funding as an incentive to draw up national development plans although there would be no involvement in content or the final outcome.

Scrapping economic policy conditionality
Whichever of the above systems is adopted, they all entail scrapping economic policy conditionality and ensuring the WDF is not involved in determining economic policy choices in countries receiving its grants or loans.

Scrapping World Bank involvement in and sign-off on development plans
Of course a sensible government defines a development plan, but the current practice of the World Bank requiring a PRSP paper to be written and then determining whether or not the content is adequate is not a way to foster democracy and better government.

It is true that, in some cases, PRSPs have enabled greater public involvement in national development plans (often through organised civil society or parliamentarians) but even in such cases, the influence of the World Bank and IMF over the content has undermined the ultimate goal of the public contribution: to alter the outcome. It is hard to escape the conclusion that the only way around this is to ensure that there is no way for the World Bank to determine the structure or content of national development plans.

Creating a fairer decision-making system
Rather than the current outdated system of voting shares that do not bear

an accurate relationship with contributions to IBRD and IDA income, a new system should be developed.

With the funding based on an international tax perceived to be de-linked from national budget processes, there would be fewer grounds for arguing that a 'contribution measure' should be used to determine votes within the institution. Also, applying a very different approach to providing grants (eg, on an unconditional entitlement basis) would change the nature of board decision-making.

On the face of it, the most equitable decision-making structure would be 'one-member one-vote' although this would not take into account the most basic democratic unit – the individual citizen. Would it be right that a small island with a population of a few thousand had the same vote as a country that is home to tens or hundreds of millions of people? An alternative approach to organising the voting structure might be 'double majority' voting using a combination of one-member one-vote and a voting system that takes into account population. In other words, for a decision to be taken both a majority of members as well as a majority of population weighted votes would be needed. However, WDM would argue that a system would need to be developed that is consistent with the principle that no country, or small group of countries is able to veto decisions.

Rather than expand the size of the board so that all 180 or so countries have a seat at the table, the current 24 seats could be increased to 30 and each seat represent about six countries with those sharing the seat deciding how to organise themselves (eg, possibly rotating over time who occupies the seat at the board).

An alternative to the global institution with a global membership could be to create several regional development funds (eg, Africa, Asia and Latin America), also financed through a new international tax, which would comprise a regional membership and not include industrialised countries. The decision-making structures could be similarly organised along the lines of a double majority system of one-member one-vote and a population weighted system.

Creating more transparency in the institution
The convention that the World Bank does not hold formal votes. Instead the chair performs a quick back of the envelope calculation to roughly work out if a majority of voting shares is in favour or against a particular

decision should be scrapped. This is laughably referred to as 'consensus-based decision-making'.

More transparent would be to hold formal votes and to make the notes of board meetings public so that citizens can see what has been said and how their representatives have voted.

Developing a set of social and environmental criteria
Project-based loans would be the principal if not sole engagement between a WDF and middle income countries. There is potential for project lending, as distinct from budget support grants, to be subject to social and environmental criteria. The criteria could of course make the loans more 'costly' in standard economic terms so this would have to be factored into the calculation on how favourable the terms of the loan can be.

The criteria would, where possible, need to be based on international standards and they would need to be agreed by the membership. These criteria could be applied in the sense of 'selectivity' (ie, project loans would not be provided to fund the construction of munitions factories, military training facilities etc) and in the sense of 'safeguards' (ie, project loans will be provided to build a railway as long as certain social and environmental standards are met during construction).

Establishing criteria for 'selectivity' and criteria for 'safeguards' is, of course, easier said than done when it comes to politically, socially and environmentally sensitive projects such as nuclear power generation, oil extraction and large dam building. Ultimately, this would come down to decisions by the membership of a WDF.

Also, it should be remembered that there is nothing stopping a middle income country using its own domestic savings or the international private sector to finance projects if it disagrees with these policies. The question for a WDF board would be what should qualify for low-interest loans that are partly subsidised by an international tax?

Subjecting the IFC to the agreed environmental criteria – or scrapping it
There may well be a role for an institution that provides loans to companies investing in low income countries. The main question would be how is this different from the loans companies can get in the private sector?

If it is to be on more favourable terms than can be obtained in the private

sector then the social and environmental criteria mentioned above should be applied. Otherwise it may as well be scrapped.

Subjecting the MIGA to the agreed environmental criteria – or scrapping it
There may well be a role for an institution that provides risk insurance to companies investing in low income countries. On issue of loans, the main question would be how would this be different from the risk insurance that companies can get in the private sector?

If it is to be on more favourable terms than can be obtained in the private sector then the social and environmental criteria mentioned above should be applied. Otherwise it may as well be scrapped.

Re-orienting research
The 'knowledge bank' concept – with the World Bank positioning itself as a dominant voice on development – should be scrapped. While it makes sense for a WDF to do some research, the aim should be to spend the majority of research resources on funding academic and/or independent research within developing countries. Not only would this be a contribution to research capacity-building, it would likely result in a greater diversity of work than using the institutions own staff (wherever they are based).

Parliamentary scrutiny
The rather bizarre situation whereby current executive directors are employees of the IFIs rather than employees of government needs to be reversed. The rules of a WDF could also stipulate an expectation that executive directors (or their deputies) are available to periodically report back to the parliaments of countries that they represent, although it would still have to be the decision of national governments whether to make use of this.

4.3 Scrap the IMF: create a new body to 'balance the books'

Returning to the words of Edward Holloway on the IMF: "There is no point in the continuation of a system which automatically leads to unpayable indebtedness between nations …These proposals, we argued, would inevitably lead to a desperate competition for world markets … default … was certain to be the unfortunate fate of one or more of the nations concerned."[152]

And the words of Geoffrey Crowther, former editor of 'The Economist' and one of the foremost economists in the UK at the time the IMF was

created: "It is the belief of the present author that Lord Keynes was right, and that the world will bitterly regret the fact that his arguments were rejected."[153]

There is no escaping the fact that the structure and remit of the IMF means that it is incapable of properly addressing balance-of-payments problems, that it creates and perpetuates massive debt and that the two combined have caused immeasurable suffering for millions of people. That this is regrettable is an understatement. It is time for a radical change.

WDM argues that making good on the principles listed in section 4.1 would best and most simply be achieved by scrapping the IMF and returning to John Maynard Keynes's original idea of an ICU; the creation of an international body with a neutral unit of currency and the remit to bring both debtor (deficit) countries and creditor (surplus) countries into balance (see box 1, chapter 2).

As was said at the time Keynes made the proposal, "Nothing so imaginative and so ambitious had ever been discussed as a possibility of responsible government policy."[154] There is just as much need for ambition and imagination now as there was at the end of World War Two. The global economy faces the ever-growing problem of the US deficit with no way of knowing how the market will correct itself; many poor countries are stuck with seemingly permanent balance-of-payments deficits through little fault of their own; and the debt crisis persists.

Also useful would be to encourage financial re-regulation. WDM believes current instability in international finance demands that there is greater regulation of the movement of capital, in particular speculative currency trading, in order to reduce the potential for financial crises and make it easier to control them if they do occur. Aside from setting an international currency transaction tax at a level which deters short-term currency speculation, the action to combat speculative capital movement is likely to be best achieved at the national level.

And in the event of the ICU system not being able to bring all countries towards a balance of payments it would make sense to also create a fair and transparent arbitration process (FTAP) for countries to negotiate excessive debt burdens. At the moment, the legal machinery exists for companies to enter debt restructuring procedures but not countries, and recent discussions within the IMF suggest that it is certainly technically possible to create such a mechanism.

WDM firmly believes that the current international financial system makes it harder rather than easier to achieve poverty eradication, social justice and environmental sustainability. Even a shake-up of the IMF including the kind of independent financing and voting structures mentioned in section 4.2; ending the IMF's adjustment lending to developing countries; providing unconditional loans for balance-of-payments problems; creating an FTAP; encouraging financial regulation; or even regional monetary funds; while much better than the current institution, would still leave some key problems in place. For example, the dollar would still be the de facto global reserve currency with the difficulties that it brings. WDM therefore believes the ICU provides a more robust solution than a changed IMF.

5 Conclusion

Failing economic policies, a debt crisis and a gaping democratic deficit; this is the enduring backdrop to the work of the IMF and World Bank. And these problems have not just been with us for a couple of years, it is a story which has lasted over two decades.

So when problems have persisted for so long, it is increasingly important that, some people take a step back and examine afresh the mythology that has grown around the two big beasts of international aid and finance. Of course, there is a collective desire to avoid the conclusion that the IMF and World Bank are simply not working because this leads to difficult choices. But ultimately, this conclusion cannot be escaped: Not only does the 'emperor have no clothes', he is running naked, screaming at the top of his voice, down H street Washington DC.

The World Bank and IMF are out of time, both in the sense that they are a product of the politics and economics of the 1940s with little relevance to today's world, and in the sense that patience with their efforts at tinkering and reform has reached its limit. The question is not *whether* there should be change but h*ow*.

WDM does not claim to have all the answers but after assessing the evidence, cannot help conclude there is a need for something radically different. The analysis presented in this report demands a more telling response than shuffling a few votes on the board of the Bank and Fund or re-branding (again) their activities in poor countries. The ideas for change suggested in these pages are intended as a contribution to public debate on what this response could look like.

There has to be a rethink of the international aid and financial systems, and it is time politicians of all persuasions recognised this. Continuing to tinker will needlessly condemn millions to a life of misery. As we said at the outset, we call on anyone who is interested in their own future and the future of others to understand the history, consider the evidence and demand change.

Appendix 1:
Remit of various organs of the World Bank Group

International Bank for Reconstruction and Development (IBRD)[155]
The IBRD was created in 1944 during the Bretton Woods Conference. 45 governments participated. It currently has 184 members. To become a member of the IBRD, a country must first be a member of the IMF. The IBRD is officially run by its board of governors, one from each country. 24 executive directors exercise powers delegated to them by the governors. These are elected by the board of governors, and so those countries with more than 4 per cent of votes are able to elect one each, whilst the rest represent groups of countries. The executive directors meet as often as the Bank requires.

The IBRD raises its finance through selling bonds on international markets. It then finances these bonds through the interest payments from countries it loans the money on to. The IBRD effectively acts as an intermediary, allowing middle income countries access to loans at its AAA credit rating, plus administrative costs, who do not have an AAA credit rating in capital markets themselves. In practice, the rates countries borrow at are similar to those they would pay in the market, but they get longer periods in which to repay, normally 15 to 20 years. In 2002, US$11.5 billion was lent to 40 countries. A small proportion of the IBRD's capital is generated from donor countries, who are mainly industrialised countries, although they do not make additional contributions towards its income.

International Finance Corporation (IFC)[156]
The IFC was created in 1956 to invest in private sector projects in the developing world. There are currently 176 members. To qualify for membership, a country must already be a member of the IBRD. The IFC has an authorised capital of US$2.45 billion. The IFC operates commercially and has made a profit in every year since its creation. It charges market rates on its loans and does not accept government guarantees. There are limits to the extent of investment provided to an individual project. Therefore, for every $1 of IFC financing, other investors provide on average $5.

The IFC also gives technical assistance to companies in the developing world, especially in helping to get finance from international markets. The IFC is officially run by its board of governors, comprising one governor from each member state, but this delegates most of its powers to the

executive directors. Votes are allocated on the basis of the share capital each country holds in the IFC. The president of the World Bank Group serves as IFC president.

International Development Association (IDA)[157]
The IDA was created in 1960, in order to provide low or interest free loans with 35 to 40 year maturities, and ten year grace periods. It currently has 164 members. To gain membership a country must first be a member of the IBRD. Countries are only eligible to borrow from the IDA if they have: a GNP per capita below an established threshold, currently US$865; a lack of creditworthiness to borrow on market terms and; implement economic and social policies acceptable to the World Bank. There are currently 81 countries eligible to borrow from the IDA.

The IDA allocates its finances amongst eligible countries on the basis of the perceived soundness of a country's policies, and its per capita income. Each year the IDA ranks all eligible countries under its country performance criteria, which enables the Bank to compare countries and determine the allocation of resources.158 A PRSP also has to have been formulated and agreed with both the World Bank and the IMF. In 2002, the IDA gave US$8.1 billion in loans and grants to 62 countries. The IDA's funds come from replenishments every four years by donor countries and the IBRD, in addition to the paying back of interest free loans. IDA financing is normally one third of that of the IBRD. Outside of donations to IDA, little funding for the rest of the World Bank Group comes from donor countries.

International Centre for Settlement of Investment Disputes (ICSID)[159]
The ICSID was created in 1966 to help facilitate the settlement of investment disputes between governments and foreign investors. 140 states have ratified the Convention on the Settlement of Investment Disputes between States and Nationals of Other States, making them full members of the ICSID. The costs of the ICSID's administration are paid by the World Bank Group (presumably from the IBRD); the costs of individual proceedings are paid by the parties concerned. The ICSID is overseen by an administrative council chaired by the World Bank Group president, and one representative from each member state, normally its IBRD governor.

Provision for the ICSID to be used as a forum for settling disputes is commonly found in investment contracts between a government and the

foreign investor. Advanced consent by governments to submit investment disputes to the ICSID arbitration can also be found in over 900 Bilateral Investment Treaties (BITs). Once a party has consented to resolve a dispute through the ICSID they are bound to carry out their undertaking and, in the case of arbitration, to abide by the award.

Since 1972 there have been 84 cases concluded at the ICSID, 21 cases have concluded since the turn of the millennium.

Multilateral Investment Guarantee Agency (MIGA)[160]

The MIGA was created in 1988 as a member of the World Bank Group. There are currently 164 members. To qualify for membership, a country must already be a member of the IBRD. With the aim of increasing the amount of FDI going to countries that investors would otherwise deem to be politically risky, the MIGA offers insurance on non-commercial risk to private investments and lending flows from one MIGA member country to another. The MIGA also offers technical assistance to developing countries to help them develop strategies to gain FDI.

The MIGA has a capital base of US$3.5 billion, and currently has issued insurance covering US$12 billion.

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