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The International Monetary Fund, Criticized. The International Monetary Fund Response to Critics

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Abstract: After more than half a century since the creation of the International Monetary Fund (IMF), this paper analyzes the extent to which this institution fulfilled its mission. The IMF admits that, in general, failed in the activities which it proposed, that is raising funds for countries with economic problems and their redistribution to ensure long term growth and development. This institution did nothing towards reducing poverty and financial disparities, increasing transparency, accountability and improving management, and creating a more efficient loan system. The main objective of this paper is to present arguments for and against the strategic effect, the policy and methodology of the financial institution, with the purpose of justification for IMF membership to the global financial system.

Keywords: failure; success; wrong management; the IMF in developing countries

JEL Classification: F33; F34; F35

1. Introduction

The IMF is, undoubtedly, the most important financial organizations in the world. In its 67 years of operation, the IMF has encountered ups and downs. The IMF critics say that, instead correcting its failures, this institution tends to cause more problems (McQuillan, 2010). The IMF has been glorified, but also criticized because of the importance granted to the market economy, the Fund being defined as a supporter of financial globalization. Countries that rely on the financial aid from the IMF have to implement standard programs of economic reforms which, often, have significant consequences on the population. Basic criticism of the IMF, from a theoretical point of view, is based on the commitment to neoclassical doctrine, often called market fundamentalism (Davis, 2007).

The toughest critics of neoclassical doctrine were made by George Soros, founder of the Open Society Foundation, and expert in functioning of financial markets. The theoretical core of this issue is that the strategic operation of the MF is contained in the economic relations explanation, which becomes guideline for developing countries and for those with problems, countries that are dependent on the aid from the international financial institutions. The IMF imposed this limited development concept to all of the countries that asked for help.

After the failure of the idea of central planning economy and social development, the main task of modern economists is to release the invisible hand of market forces around the world, eliminating barriers to free flows of natural resources, goods, services and money, which should ensure greater prosperity. The economy protected by the IMF defenders is based on the belief that the private sector is more efficient and more dynamic than the public sector, and it reacts better to the market conditions

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(Sheppard, Weidner and Wendt, 2011). In academic and political discussions, many blame the IMF because its dogmatic approach, this causing inflation and payments deficits in developing countries.

2. The International Monetary Fund, Criticized

Criticism of the IMF's role is centered on four core issues (Goldsbrough, 2006):

1. Macroeconomic frameworks underlying the IMF programs are said to be "too rigid", restraining, therefore, the expenditures that would be made, since they are very conservative in terms of macroeconomic stability. This might be because their goal is to achieve low inflation rates or to target fiscal deficits which are lower that what is necessary for stability. There are two aspects of criticism on macroeconomic frameworks: first, that programs aim at achieving too low inflation targets, exceeding the available evidence on inflation thresholds that are harmful for economic growth and poverty reduction; secondly, in spite the declaration made at the time the Facility for poverty reduction and growth was introduced, the programs still present insufficient fiscal flexibility, especially in terms of expenditure financed by aid.
2. In his role as "keeper", it is said that the IMF goes beyond the available evidence to make decisions on issues such as absorptive capacity, risk of "Dutch disease" or debt sustainability. To a considerable extent, the community of the lenders contracted from the IMF assessments of the countries' macroeconomic policies, based on its signals on the opportunity of the macroeconomic framework when making decisions on aid. While creditors' answers to these signals may be nuanced, the IMF assessments are likely to influence the level of aid flows. So, the question is how the IMF makes its decisions on macroeconomic framework for an environment where there is a considerable uncertainty about how the economy will respond to the aid. Some critics of the IMF argue that it exceeds the available evidence in making such judgments, relying unduly on the caution side by strong emphasizing of macroeconomic risks. IMF response is that this is a more flexible approach to macroeconomic challenges, but that many of the involved countries went through long periods of macroeconomic instability, with high costs, so caution is justified in order not to undermine the recent gains.
3. The IMF is criticized for not having a more detailed approach of members' needs when determining the macroeconomic framework and the requirements of the aid to help countries to achieve the Millennium Development Goals – or any other targets related to these goals. They say that the IMF does not act as a catalyst and it can tell creditors that a medium term framework based on low expectations is acceptable when a more ambitious scenario would be feasible. IMF response is that in the formulation of the spending programs, the government must take account of budgetary constraints, including expectations of available aid and is not in favor of poorer countries to claim that they would receive more help than they do – in a world where commitments still exceed payments.
4. Developing programs do not sufficiently take into account the cost of achieving short term macroeconomic adjustments. It is very important the framework in the medium term, which underpins the programs developed by the IMF. But the schemes involve more than this framework. They are detailed accords of how macroeconomic policies will be implemented in the short term. For many programs, some aspects of the detailed design were controversial.

The IMF supporters respond to this criticism by saying that this approach is the direct result of free market and market economy. Also, they affirm there is a need of Washington consensus and that the countries with economic problems will soon come through. Fiscal strictness, privatization, liberalization and other macroeconomic programs elements are the basis of the IMF policies, and over time, have become rather targets than means for sustainable growth (Spruiell, 2006). These policies were pushed too hard and too fast, while neglecting other necessary policies. The IMF provided better grades to those countries with a faster privatization process.

However, rapid privatization has not brought any consistent benefit. Corrupt politicians took advantage of the IMF demand for rapid privatization and purchased power, energy and water companies in their own countries. Workers have not received anything during privatization, because they were dismissed without pay. No wonder that high unemployment rates were recorded after such measures (Hood, Kamery and Pitts, 2004). International power elite puts the IMF under its authority, to serve as regulator of national economies and as a force dealing with globalization. IMF, through stand-by arrangements, expanded its competences and imposed its attitude and its neoliberal objectives. Often, the IMF managed not only the budget of a country, but the whole set of economic policies (Gilbert, Vines, 2004). By rapid elimination of barriers and reduction of custom duties, the free market was established, causing significant damages to domestic production. It was a big mistake of the IMF and of the overall financial globalization.

The preparations for the free functioning of the market have been made in developing countries, but institutions that were needed were not established. Increasing production and productivity in domestic industry were not achieved, national industry remaining uncompetitive both in national and world markets. Foreign trade deficit of developing countries rose to a dangerously high level. The budgets were limited and the expenditures over budgets were reduced, resulting in a decreasing of social benefits, a reduction in health insurance rights and a pensions' limitation.

All these adversely affected the different classes of people, especially the poor, and caused numerous complaints and protests. These policies, based on Washington directives, brought social and private benefits, but also had many weaknesses, encouraged the instability of taking systemic risk and led to negative financial consequences. In addition to faulty design, it focused too much on limiting demand, and not on the structural policy that would influence the main causes of balance/imbalance of payments of developing countries or of those in transition (Camdessus, 1998). The IMF program did not encourage the development of agriculture, but caused a decline in agricultural activity, rising unemployment and deteriorating living conditions. However, the IMF defends its programs, claiming that they are based on demand regulation and supply increase policy, depending on the nature and the size of the period of balance/imbalance of payments.

Moreover, the main problem of the IMF is the management, the lack of accountability and evaluation, the excessive monopolistic status, the undemocratic management system and the lack of public participation. This institution is dominated not only by the richest countries, but also by commercial and financial interests of these countries (Schwartz, 2005).

Experts that are involved in the process of decision making of the IMF adapt their analysis and suggestions to their superiors' ideas. The IMF is often criticized for its politics and secret programs. Lately, an important step has been made towards publishing additional info about its activity. Though, more actions are needed in order to increase the transparency of the IMF and its citizen approach. Increasing public pressure may lead to changes in the politics of the international institutions, bringing benefits to citizens all around the world. Moreover, the leading structure and the way of making decisions have been the main problem of IMF activity.

The most developed countries make decisions within the IMF, not only due to the way of vote rights allocation, but also due to the division of competences between certain domains within the organizational hierarchy and the vote of qualified majority, exceeding 2/3 in the total number of votes. Nowadays, most of IMF and World Bank activity within the emerging countries are lead by representatives of the industrialized countries. It is well known that the leading staff of the IMF is always from Europe and the one of the World Bank (WB), from the United States. The elections are always made behind closed doors, and global development experience is not a prerequisite. The principle of liability demands that decision makers are responsible for their own actions and for the consequences of their elections.

This activity includes the principles of transparency and evaluation. Transparency ensures information access to individuals that are not members of the institution. Evaluation allows citizens to express their opinion about the decisions quality. The IMF has failed in achieving the criteria of responsibility. The main reason is the lack of a systemic and independent evaluation mechanism. As long as there are no consistent, independent and continuous evaluation and criticism of the IMF, one can see that the IMF tries to hide the results of its activity. Commercial interests must be replaced with preoccupation with the living standards, democracy, human rights and social justice. Institutions representing the global civil society demand individuals to involve in developing economic growth programs, though, very often, the IMF makes the plans by itself, behind closed doors and then sends them to the countries in order to be signed, without letting them know that they have the possibility to develop their own plans. As global communication turns the world into a very strong linked system, more and more individuals are capable of examining the costs and benefits of economic policies.

The IMF has restricted individuals' access to its economic programs of adjustment. Though, it is believed that it gives financial help and short term macroeconomic guidance. As a judge within the negotiations, the IMF usually limits itself to the Ministries of Finance and the national banks. Involvement of individuals in decision making is ethic compulsory. Citizens in the emerging countries have protested for years due to the beamy social and economic statuses. What is now different is the fact that a new wave of protests starts in the developed countries. They have occurred in Geneva, Seattle and other cities where meetings of the IMF, WB and World Trade Organization occurred. High public pressure may contribute to the changing of the policies of the international financial institutions towards individuals' interests.

The professor and winner of the Nobel Prize, J.E. Stiglitz has criticized in a public manner the mechanism of this institution when he saw the way the IMF and other global players operated (Dawson, 2009). According to Stiglitz, the IMF programs caused hunger and disorders in many countries, though the results had not been fatal. The rich often become healthier, while the poor ones become poorer. Moreover, he emphasized that there is no doubt that certain distress were necessary, but the distress in the emerging countries, caused by globalization and development, lead by the IMF and other financial international institutions, are more than unnecessary. In fact, Stiglitz is against the way globalization is lead and does not hide his social sensitivity regarding the victims of the cruel process of globalization (Ambrose, 2002). The principles of the global financial orders are always attacked.

Globalization turned over the night into an important topic, decreasing the feeling of isolation, connected the national economies and influenced the development of international trade. It also hollowed the difference between the developed and underdeveloped countries. The process of globalization itself and the implementation of a trade based economy did not have positive effects in the emerging countries. The West promised great improvements if the countries adopted the new economic system. The new system caused a rising degree of hunger instead. International financial institutions have not had the leading role in a global ruled system without global leadership. Stiglitz claims that the IMF has made two mistakes in its actions. The first one was accepting the theory of liberalization, drawing the map according to the theory and by diagnosing the problems in the emerging countries in a wrong way. Moreover, this scheme and this model have been applied to all the states, neglecting national features. The problems can be described in four steps. First step is privatization. Some politicians have sold public water and electricity companies without negotiating, interested by the remittances. These politicians have used the demands of the World Bank in order to justify its actions. The second step was liberalization of the capital flows.

Unfortunately, in the case of Indonesia and Brazil, money usually moves because of the real estate sector and currency speculations. The state reserve can lose currency in just a few days. When such things happen, the IMF demands these countries to raise the interest rate by a considerable percentage. The effects are predictable. High interest rates can destroy the value of the real estate sector and industrial production, and clear the national reserves. The IMF then leads the weaken country towards the third step, represented by the liberal stabilization, at the market level, of the prices of water, food and gas. This action leads to the fourth step, the so-called IMF protest, which is also predictable (Davis, 2007).

Jeffrey Sachs, economist and professor at Harvard University, is one of the critics of international financial organizations. He claims that Western countries must devote more financial resources to programs against poverty. He adds that past project failed because US pressure to give money to allied governments, no matter that they were incompetent or corrupt. Sachs emphasizes the growing influence of Wall Street bankers on these institutions.

Many economists believe the criticism is justified, but this does not give poor countries the right to set conditions and amount of loans. Also, it is normal for the IMF to protect the bankers interests because, unprotected, they will not invest, which is contrary to the interest of developing countries (Rogoff, 2003). The WB and IMF have both good and bad ideas.

As mentioned above, it can be deduced that more and more economists believe that the IMF is not needed (Hood, Kamery and Pitts, 2004). These statements are based on three arguments. First, the IMF is institutionally unable to be an effective so-called “last lender in case of emergency”. The IMF does not succeed in creating valuable money and in reacting quickly enough to prevent liquidity crises. Also, the Fund lacks information on insolvency and illiquidity of the banks. The IMF has not demonstrated effectiveness in promoting economic policies necessary to avoid future crises. The IMF, established for helping in the short term, evolved into an international economic consultant for development, using loans to persuade developing countries governments to implement policies that are in interest. However, the IMF has not shown effectiveness in this role. Differences in living standards between rich and poor countries continued to grow. The power and the frequency of crisis deepened. Negotiations for receiving the IMF loans take too long and threaten transformation of liquidity crises into one of solvency.

3. IMF and the Global Financial Crisis

In a recent paperwork of the Center for Economic and Policy Research (CEPR), economists argue that countries currently involved in the IMF loan agreements are subject to "pro-cyclical" macroeconomic policies, which tend to aggravate the economic slowdown. Economists argue that the IMF failed to learn valuable lessons from the past economic crises, and continues to be based on overly optimistic growth forecasts for debtor countries. Managing these policies wrongly, the authors argue that the IMF may have increased or prolonged financial crisis in many countries that it have borrowed (Center for Economic and Policy Research, 2009).

CEPR and other analysts have criticized the IMF for failing to anticipate the crisis in the United States. Since the IMF releases regularly the World Economic Outlook every six months - in order to assess current economic trends - some economists argue that the Fund should have recognize the growing bubble and to anticipate the consequences. Critics urge the IMF to reassess the criteria, assumptions and economic analysis used to prescribe macroeconomic policies in developing countries (Inter Press Service, 2009).

In many Eastern European countries, both leaders and citizens see the IMF loan conditions as factors that have aggravated the crisis. In Romania (who negotiated a loan of 20 billion with IMF), opposition political party called for a vote of no confidence against the elected government because of the controversial reforms imposed by the IMF. In Hungary, people know of the IMF loans and conditions attached to them, and "The IMF is not very pleasant".

4. IMF Response to Criticism

1. Crisis always creates difficulties.

Because the IMF fights against the economic crisis, regardless of policy that offers, it is likely to experience difficulties. Trying to balance the balance of payments is not possible without some painful readjustments.

2. The IMF had some successes.

The IMF failures tend to be highly publicized. But its successes, less. Also, critics tend to focus on short-term problems and ignore longer-term prospects (Hivos and the Mott Foundation, 2003).

3. Safety

The fact that there is a lender of last resort provides a boost to investor confidence. This is important during the current financial crisis.

4. Countries are not obliged to resort to the IMF loans.

Countries are those that seek help from the IMF. The fact that many countries turn to the IMF suggests that there are benefits in this respect.

5. The IMF is an easy target.

Sometimes, countries decide to make painful adjustments in the short term, but it lacks political will. An IMF intervention causes governance to borrow from the Fund, and later on, if difficulties arise, to blame the IMF (Bryant, Guh, 2008).

5. Conclusions

Traditional criticism of those who oppose the market system and globalization of trade says that a combination of financial liberalization, opening of economies and recipes of macroeconomic development of the IMF creates a dangerous cocktail for small, open and dependent countries. Recently, these views were shared also by the officials who implement these policies.

Although there is a growing awareness of the problem of organization and management of this institution, compensatory programs are modest today.

The key issue of whether institutions will help to increase or decrease poverty in developing countries has not been solved. The IMF will continue to represent the rich international financial institutions, bankers and investors who show interest for the case of the poor. There is also the problem of indications adequacy in determining the international institutions to change their behavior to developing countries in order to promote development and social welfare.

Since this subject is vast, it is necessary to point out some proposals. First, it must be admitted that neo-liberalism and privatization did not lead to prosperity and development. Liberalization and privatization should be introduced gradually and in a controlled manner. Certain pre-conditions are necessary for market liberalization. Privatization program should be protected from adverse effects, and social programs must be implemented to solve social problems arising from privatization. It is necessary to introduce quality rules for the privatization process, in order to make privatization policies serve in achieving development. Appropriate financial institutions such as banks and regulated financial markets are necessary for successful operation of liberalization and privatization.

Moreover, all the above must be followed by appropriate macroeconomic policies. These policies should be based on an accurate analysis of state of the economy and must take into account that a weak economy cannot survive the competition with developed countries, having to protect by custom duties and other methods. Macroeconomic policy must contain a special social program and a program to reduce poverty, problem encountered in most in transition and developing countries. The IMF must observe the specific conditions of each country and adapt its development models and macroeconomic policies to these conditions.

There is no doubt that the IMF violates human rights, destroys physical and social environment and extends the misery and poverty in poor countries. Despite criticism, the international financial institution must continue to allocate funds to less developed countries, maintain the international monetary system stability and promote the economic development and prosperity. This means that the IMF should support liquidity, convertibility of currency and monetary and fiscal stabilization.

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