



# The IMF and the World Bank

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## **International Financial Institutions: The IMF and the World Bank**

### **Introduction**

Toward the end of the Second World War, in July 1944, representatives of the United States, Great Britain, France, Russia, and forty other countries met at Bretton Woods, a resort in New Hampshire, to lay the foundation for the post-war international financial order. Such a new system, they hoped, would prevent another worldwide economic cataclysm like the Great Depression that had destabilized Europe and the United States in the 1930s and had contributed to the rise of Fascism and the war. Therefore, the United Nations Monetary and Financial Conference, as the Bretton Woods conference was officially called, created the International Monetary Fund (the IMF) and the World Bank (also known as "the Fund" and "the Bank" respectively) to prevent economic crises and to rebuild economies shattered by the war.

The Bretton Woods strategy addressed what were considered to be the two main causes of the pre-war economic downturn and obstacles to future global prosperity—the lack of stable financial markets around the world that had led to the war and the destruction caused by the war itself. The IMF would be aimed at stabilizing global financial markets and national currencies by providing the resources to establish secure monetary policy and exchange rate regimes, while the World Bank would rebuild Europe by facilitating investment in reconstruction and development.

Although intended to benefit the global economy and contribute to world peace, however, the Bank and the Fund, collectively referred to as international financial institutions (or "IFIs"), have become primary targets in the anti-globalization movement. In many countries, they are resented and are viewed as imposing Western-style capitalism on developing countries without regard to the social effects.

The following Issue Brief is designed to help you understand the history, purpose, structure, and activities of the IFIs and to describe both benefits and concerns that surround the Bank and the Fund.

### **The Origins of the IFIs**

At the time of Bretton Woods, there was serious concern about the stability of global economic markets. The world-wide depression of the 1930s had been deepened by the instability of international currency markets and the contraction of international trade, so that stabilization of those markets and promotion of trade were considered crucial to avoid another crisis. Likewise, the widespread destruction of Europe and uncertainty about its future also threatened to cause economic and political disruption. The countries allied to fight Nazi Germany and Japan believed that a similar collaborative effort was the only way to stabilize their economies and those of their soon-to-be-defeated enemies and to provide funds to rejuvenate the countries destroyed by the war.

The Bretton Woods conference therefore gathered together some of the world's most prominent minds in economic policy and some of its most powerful policy-makers in order to chart a new course. Representing the United States and serving as chairman of the conference was Henry Morgenthau, the U.S. Secretary of the Treasury, assisted by Harry Dexter White, the Assistant Secretary of the Treasury, who had laid the groundwork for the conference and originated the key ideas and policies to be discussed. Along with them was Dean Acheson, then the Under Secretary of State, who later became Harry Truman's influential Secretary of State



during the first years of the Cold War, and a number of Senators and Congressmen. Leading the British delegation was the famed economist John Maynard Keynes. Other delegations of notables

came from China, India, Russia, and France. Some leading economists from smaller nations were also quite influential at the conference, such as Louis Raminsky of Canada, Kyriakos Varvaressos of Greece, and Johan Beyen of the Netherlands. Morgenthau opened the conference by telling his fellow participants, "What we do here today will shape to a significant degree the nature of the world in which we are to live."

The aim of the conference was to draw up plans for the International Monetary Fund and World Bank (as well as a proposed International Trade Organization, which never got off the ground as a result of concerns among many countries over their economic sovereignty). The conference was controversial, however, with the public, politicians, and media in many of the countries—especially the United States—wary about international control of their sovereign economic policy. Even the U.S. and British delegations, the leading countries at the conference, commented to each other that their plans had to be politically amenable to their home governments in order to be ultimately approved. At the same time, the conference was largely opaque to the public. The prominent American commentator Walter Lippman said, "It has been impossible for the general public to obtain any idea of what the Bretton Wood conference is about. Though it is concerned with questions which will affect men's lives deeply, the language of monetary policy is understood by very few men in any country."

Negotiations at the conference were, therefore, contentious. Although White had drawn up plans for the proposed organizations, many details, especially regarding financial contributions to the new institutions, were still to be worked out. Countries were concerned about the balance of power within the organizations as reflected in their proportions of contributions of gold to the Fund and their concomitant ability to draw from the Fund (their "quotas"). There was much horse-trading regarding how to divide the total amount of money the Fund would have among the forty-four participants. India insisted on having as high a quota as China, for example, while France insisted on having more than India and more than the three Benelux countries (Belgium, the Netherlands, and Luxembourg), who were coordinating their monetary policy. The Russians insisted on a quota of not much less than the British and argued that they should have to contribute less gold to the fund than other countries because of their suffering in the war, but be able to draw a higher proportional quota than other countries. At the same time, they refused to publish accurate economic statistics.

Other disputes concerned the governance of the organizations, such as how many permanent seats the major contributors would hold and where the organizations would be located; the British unsuccessfully lobbied for the Fund to be in London. Another significant dispute revolved around whether the dollar would serve along with gold as the standard for exchange rates, which, in the end, the American delegation successfully insisted on. Meanwhile, Keynes, leading the committee that drew up plans for the Bank, dominated the drafting process and forged the institution largely along his preferred lines and implementing his key economic idea—that government should spend their resources to stimulate their economies during slowdowns.

With the diplomatic wrangling completed, the conference's Final Act was signed on July 22, 1944, although the institutions did not actually start operations until the following year. In a letter read to the delegates, U.S. President Franklin Roosevelt said that they had "prepared two further foundation stones for the structure of lasting peace and security." How did such hope at the time result in such opposition today? The rest of this Issue Brief explains the current operations of the Bank and the Fund and why they are so controversial.



## The International Monetary Fund

### Governance, Organization and Purposes

#### *Governance*

The IMF is controlled by its 184 member-countries, each of whom appoints a representative to the Fund's Board of Governors. The Board of Governors, most of whom are the finance ministers or heads of the central bank of the members, meet once per year to discuss and is possible achieve consensus on major issues. In the meantime, day-to-day operations are managed by a 24-person Executive Board. The world's major economic and political powers-the United States (the IMF's largest shareholder), Great Britain, Japan, Germany, France, China, Russia, and Saudi Arabia-each have permanent seats on the Executive Board, while the sixteen other directors are elected for two-year terms by groups of countries divided roughly by geography, e.g., Caribbean, African, Southeast Asian, etc. The Executive Board, in turn, is run by the Managing Director, who is elected for renewable five-year terms.

The Fund also has an International Monetary and Financial Committee of 24 representatives of the member-countries that meets twice yearly to provide advice on the international monetary and financial system to the Fund's staff.

In all of its operations, voting power is weighted based on the size of the economy and therefore the quota allocation of each country. Decisions are usually taken by consensus, but the United States, as the Fund's major shareholder, has the most influence in the institution's policy-making.

#### *Organization*

The Fund's current Managing Director is Horst Koehler of Germany, who took office in the fall of 2001. Each members of the Executive Board runs a particular department of the Fund, offices devoted to a) particular regions of the world, such as Europe, Africa, Middle East, Western Hemisphere, and Asia/Pacific; b) functions, such as finance, technical assistance, fiscal planning, capital markets, research, and statistics; and, c) administrative functions of the Fund itself. The Fund has a total of 2,800 employees, mostly based in its Washington, D.C. headquarters.

#### *Purposes*

The Bretton Woods Conference set out six goals for the Fund in its Articles of Agreement. Those goals, as shown in the accompanying box, remain the guiding principles of the Fund today.

- (i) To promote international monetary cooperation through a permanent institution which provides the machinery for consultation and collaboration on international monetary problems.
- (ii) To facilitate the expansion and balanced growth of international trade, and to contribute thereby to the promotion and maintenance of high levels of employment and real income and to the development of the productive resources of all members as primary objectives of economic policy.
- (iii) To promote exchange stability, to maintain orderly exchange arrangements among members, and to avoid competitive exchange depreciation.
- (iv) To assist in the establishment of a multilateral system of payments in respect of current transactions between members and in the elimination of foreign exchange restrictions that hamper the growth of world trade.



(v) To give confidence to members by making the general resources of the Fund temporarily available to them under adequate safeguards, thus providing them with opportunity to correct maladjustments in their balance of payments without resorting to measures destructive of national or international prosperity.

(vi) In accordance with the above, to shorten the duration and lessen the degree of disequilibria in the international balances of payments of members.

In simpler terms, the goals are, first, to facilitate the cooperation of countries on monetary policy, including providing the necessary resources for both consultation and the establishment of monetary policy in order to minimize the effects of international financial crises. Second, the IMF is supposed to assist the liberalization of international trade by helping countries increase their real incomes while lowering unemployment. Third, the IMF helps to stabilize exchange rates between countries. Especially after the global depression of the 1930s, it was considered vital to establish currencies that could hold their value, serve as mediums of international exchange, and resist any speculative attacks.

Fourth, the IMF maintains a multilateral system of payments that eliminates foreign exchange restrictions. Countries are thus free to trade with each other without worrying about the effects of interest rates and currency depreciation on their payments. Fifth, the IMF provides a safeguard to members of the Fund against balance of payments crises, i.e., when governments cannot balance the money they have with the money they owe to other countries. Fund members can have the confidence to adjust the imbalances in their national accounts without resorting to painful measures that would hamper their prosperity, such as devaluing their currency in relation to other countries'. Sixth, by trying to reduce the effects of volatility in countries' balance of payments accounts, the IMF helps assure that global trade and financial relationships can continue at a steady rate without the risks of global depressions like that of the 1930s.

When founded, the IMF also operated the system of international exchange on the basis of gold reserves that its member countries pledged to it. In 1971, however, the U.S. government under President Nixon eliminated the connection between the U.S. dollar and gold as a means to resolve a domestic monetary crisis. By allowing the dollar's value to "float" as opposed to having it pegged to gold, the U.S. government was able to adjust its monetary policy to deal with changes in the American economy. Subsequently, the IMF eliminated its use of gold, and all other members were allowed to "float" their currencies as well.

### **How Does the IMF Achieve Its Goals?**

The IMF has three main activities: surveillance, financial assistance, and technical assistance.

#### *Surveillance*

Each year, the IMF sends economists to each of its member countries to analyze the country's economic situation. The team examines fiscal and monetary policy, exchange rate, general macroeconomic stability, and any related policies, such as labor policy, trade policy, and social policy (such as the pension system). This process is known as an Article IV consultation, after the section authorizing it in the Articles of Agreement. The purpose of such consultation is to provide an outside check on national decisions that might have an affect on the international economic system. After the team finishes its analysis, the IMF Executive Board discusses the report and gives it to the leaders of the country in question as the official opinion of the Fund. A version of the report is also published and available as an IMF Public Information Notice (PIN). The Fund also performs similar reviews of regional policy by such organizations as the European Union (EU), the West African Economic and Monetary Union, and the Eastern Caribbean Currency Union. On a global level, the IMF also publishes its analysis of the world economic system in its



World Economic Outlook twice per year and the Global Financial Stability Report, which focuses specifically on the international capital markets, also twice per year.

### *Financial Assistance*

The central activity undertaken by the IMF is financial assistance to national treasury departments. Member countries with balance of payments problems can receive credits and loans in order to pay off their obligations and readjust their economic policies so that they will not face another crisis or near-crisis. In order to receive assistance, however, the member-country must agree, through a "letter of intent," to implement changes in its fiscal and monetary policies that IMF experts have determined are necessary. These conditions, as explained below, are the cause of some of the most vociferous resentment toward the IMF because they often involve very detailed changes in national policies. Nevertheless, the IMF assistance is considered so essential to national economic health that countries generally agree even when they have strong reservations. The loans are disbursed in phases in order to ensure that the receiving country moves forward with the reforms required of it. Loans are generally granted for relatively short periods of time, for just a few months, or for as long as ten years, depending on the type of loan. The receiving country must pay back loans on time, on a rigorous schedule, because the loans are intended to be temporary assistance. Countries are discouraged from becoming dependent on IMF loans, and, in fact, may face extra charges if too much of their government funding comes from the IMF. Rather, the IMF hopes to play a role as a catalyst for private banks to lend to governments, because the extension of an IMF loan is intended to express confidence that the receiving country is getting its financial house in order.

The IMF provides the assistance through several lending programs, which are called "facilities."

- Stand-by arrangements are loans granted for specific amounts over 12 to 18 months to deal with short-term problems.
- The Extended Funds Facility is used to help a member-country deal with what are called "structural" economic problems resulting from a history of poor economic planning. The IMF attaches strong conditions to loans through this facility, which are granted for three to four year terms.
- The Poverty Reduction and Growth Facility is granted at low interest rates to poor countries.
- The Supplemental Reserve Facility grants short-term loans during crises, but adds a surcharge to discourage too much borrowing.
- Contingent Credit Lines are granted during waves of crises that can spread from one country to another, called "contagions."
- Emergency Assistance is granted to countries facing military conflicts or other sudden disasters.

### *Technical assistance*

The Fund provides technical assistance on fiscal and monetary policy, regulatory procedures, tax policy, and collection of statistics, among other issues. These programs are aimed at strengthening developing countries' abilities to reform and properly manage their macroeconomic policies. The Fund dispatches its own experts and private consultants on training missions to educate government officials and also runs the IMF Institute in Washington to provide courses for officials.



In addition to these three main activities, the IMF has also instituted various programs to ensure the stability of financial system management on a global scale. For example, the Fund, along with the World Bank and other institutions, has drafted voluntary standards and codes for countries

and financial institutions to adapt in order to increase accountability and transparency and to limit corruption. The Fund has also developed two systems of collection and dissemination of statistical information in order to help assess the economic viability of the domestic and international financial systems.

## Why Is the IMF Controversial?

After the collapse of the Soviet Union, the Western approach to market liberalization, privatization, fiscal austerity, and free trade that had produced economic growth in the developed countries-especially in the United States-was exported to developing countries through the IFIs. Since they were headquartered in Washington, the IFIs' strategy was called the "Washington Consensus." As summarized by the World Bank, it had ten basic points:

1. Fiscal discipline (that is, not too much government spending).
2. Redirection of public spending toward education, health, and infrastructure.
3. Tax reform (that is, broadening the tax base and cutting tax rates).
4. Market-determined interest rates.
5. Competitive exchange rates.
6. Trade liberalization (that is, eliminating quotas and tariffs).
7. Openness to foreign direct investment.
8. Privatization of state enterprises.
9. Deregulation.
10. Legal security for property rights.

The success of industrialized nations when following these practices in comparison to Communist countries' lack of economic development caused Western economists and politicians to assume their infallibility and enticed many developing countries into following them. However, the way in which the Washington Consensus was uniformly proselytized to a wide range of national economies is said by critics to have contributed to serious problems.

Critics attack four interrelated aspects of the implementation of the Washington Consensus:

First, the conditions placed on loans are too intrusive and compromise the economic and political sovereignty of the receiving countries. For example, Joseph Stiglitz, a winner of the Nobel Prize in economics and former chief economist of the World Bank, writes that those conditions, often referred to as a whole as "conditionality," are not just the typical requirements that anyone lending money might expect the borrower to fulfill in order to ensure the money will be paid back. Rather, says Stiglitz, "Conditionality" refers to more forceful conditions, ones that often turn the loan into a policy tool."

The IMF has used conditionality to exact major changes, called "structural adjustments," in borrowing countries' fiscal and monetary policies, including such issues as banking regulations, government deficits, and pension policy. He cites the example of the Fund's insistence that the Korean Central Bank focus on fighting inflation during the 1997 Asian Financial Crisis, not



because monetary policy was a cause of the crisis, but rather because the IMF believed that fighting inflation should be the primary purpose of a central bank. According to Stiglitz, many of these changes are simply politically impossible to achieve because they would cause too much

domestic opposition. Even in the United States, he points out, the Federal Reserve Bank is not charged with just fighting inflation, but also with promoting employment and economic growth and an attempt by a powerful senator in the mid-1990s to refocus its charter just on inflation was beaten back by the White House.

Second, the IMF imposed the policies of the Washington Consensus on countries without understanding the distinct characteristics of the countries that made those policies difficult to carry out, unnecessary, or even counter-productive. According to Stiglitz, for example, the economists of the IMF had a "one-size-fits-all" policy based on their academic training, which focused on economic models with unrealistic assumptions about how real-life economies work. They do not generally specialize in the economies of the countries whose policies they oversee, often do not live in those countries and mostly work from Washington, and have little appreciation for the political circumstances under which the governments operated. When crises arise, therefore, says Stiglitz, the IMF instinctively blames the governments of the countries suffering the crises.

Third, the policies were imposed all at once, rather than in an appropriate sequence. For example, the IMF demands that countries it lends to privatize government services rapidly—that is, sell them to private investors rather than operate the services itself—such as water supply and utilities. According to Stiglitz, this is a result of the IMF's "market fundamentalism," a blind faith in the free market, that ignores the fact that the ground must be prepared for privatization. Private owners are most interested in operating a company efficiently, which often means letting go of staff. But, says Stiglitz, if a country's unemployment program and other social safety nets are not sufficiently developed, those fired staff will have no way to support their families. "Privatization needs to be part of a more comprehensive program, which entails creating jobs in tandem with the inevitable job destruction that privatization often entails. Macroeconomic policies, including low interest rates, that have help create jobs, have to be put in place. Timing (and sequencing) is everything."

Fourth, the IMF was not open to criticism or public oversight when working on these policies, leading to arrogance and a lack of connection to the reality on the ground in the affected countries. For example, Stiglitz points out that the agreements between the IMF and borrower countries were always kept secret from the general public in those countries. Sometimes, he says, the agreements were kept even from him and his colleagues at the World Bank when working on joint projects with the Fund. At the same time, the government officials of borrowing countries often felt powerless to question the Fund's policies, believing that just to ask a question would be viewed by the Fund as a challenge to its authority and jeopardize the loans it was offering. A great lack of trust, therefore, characterized relations between the Fund and its borrowers, as the public and governments of its borrower countries felt out of the loop on the decisions that would shape their economic future.

Some opponents of the IMF, and globalization in general, go even further. They claim that the entire international financial system is corrupt and unfair. They criticize not just the implementation of the Washington Consensus, but its very existence. One group, for example, called 50 Years Is Enough, argues that the IMF, World Bank (discussed below), and the World Trade Organization (WTO) are anti-democratic institutions, responsible for the impoverishment of the developing world and benefiting only rich countries and multinational corporations. According to 50 Years Is Enough, "Only when the well-being of all, including the most vulnerable peoples and ecosystems, is given priority over corporate profits can we achieve genuine sustainable development and create a world of justice, equality, peace, and ecological values, where fundamental human rights, including internationally-recognized social, cultural, environmental,



and economic rights, are respected." This group wants an immediate end to the IMF's policies, a cancellation of all outstanding government debts in the developing world (discussed in more detail below), and reparations for the damage, in their view, that the Fund and Bank's policies have caused.

Three views, then, of the IMF's role are possible. First, the IMF views itself as committed to sound financial management, lending money and providing surveillance and advice to help countries avoid economic collapse. Second, however, IMF critics claims that the Fund's policies are often poorly planned, and even counter-productive. Third, the most radical critics of the IMF contend that the whole international finance system, of which the Fund is one of the leading institutions, should be dismantled for the benefit of the worlds poor.

## **The World Bank**

### **Structure**

The World Bank is the name that has come to be used for the International Bank for Reconstruction and Development (IBRD) founded at Bretton Woods. As the Bank expanded beyond its initial scope and purpose of rebuilding Europe after the Second World War, the World Bank grew through the creation of four additional organizations. Together, these five financial organizations comprise the World Bank Group, namely the International Bank of Reconstruction and Development (IBRD), the International Development Association (IDA), the International Finance Corporation (IFC), the Multilateral Investment Guarantee Agency (MIGA), and the International Center for Settlement of Investment Disputes (ICSID).

The IBRD and the IDA focus mainly on public sector monetary policy and provide low-interest loans, interest-free credit, and grants to developing countries. Additionally, they work to affect the policies of governments by providing macroeconomic policy advice, research, and technical advice. The remaining three institutions that belong to the World Bank Group focus more on private market interactions, providing funding, insurance, and dispute resolution for private sector projects. The sections below deal with each part of the World Bank Group in turn.

### **Governance**

The governance of the World Bank is almost identical to that of the IMF. It is directed by a Board of Governors composed of one representative from each member country, and the governors direct the IBRD based on weighted voting rights that are determined by each country's agreed annual contributions to the Bank. As in the IMF, the United States is the largest contributor and has the most weighted voting power, though as a practical matter decisions are made by consensus. Twenty-two executive directors oversee the daily operations of the Bank, including five permanent spots given to the United States, Japan, Great Britain, Germany, and France. The remaining 17 directors are elected by all member-nations. The Bank is led by its President, currently James Wolfenson of Australia, a retired investment banker. Vice presidents manage Bank affairs in six regions-Africa, East Asia & Pacific, Europe & Central Asia, Latin America & the Caribbean, Middle East & North Africa, and South Asia-and in other functional units such as Finance, Poverty Reduction, Infrastructure, and Private Sector Development. The World Bank also operations a World Bank Institute for training of officials in development related topics. In total, the Bank has almost 10,000 employees, spread out over 100 offices around the world and headquartered in Washington, D.C.

### **The IBRD**

The mission statement of the IBRD states that it "aims to reduce poverty in middle-income and creditworthy poorer countries by promoting sustainable development, through loans, guarantees,



and non-lending-including analytical and advisory-services." The Bank aims at issues such as building infrastructure (roads, dams, power plants), natural disaster relief, humanitarian

emergencies, poverty reduction, infant mortality, gender equality, education, and long-term development issues. Furthermore, the Bank tries to foster social reforms in order to promote economic development, such the empowerment of women, building schools and health centers, provision of clean water and electricity, fighting disease, and protecting the environment.

Since 2000, the Bank has been devoted to helping implement the Millennium Development Goals (MDGs), drafted by the United Nations at the Millennium World Summit. The goals are as follows:

1. Eradicate extreme poverty and hunger.
2. Achieve universal primary education.
3. Promote gender equality and empower women.
4. Reduce child mortality.
5. Improve maternal health.
6. Combat HIV/AIDS, malaria, and other diseases.
7. Ensure environmental sustainability.
8. Develop a global partnership for development.

The goals also have 18 specific targets and 48 performance indicators and are considered a step forward over previous development efforts because they set specific targets and timetables for achievement, with 2015 as the major deadline.

The Bank operates by providing loans in two different ways. First, investment loans are granted for projects that will produce goods or services or public works to help economic and social development. Second, adjustment loans are granted for programs to support reforms to government policies. Like IMF loans, Bank loans are conditioned on the Bank's approval of the investment plans and schedule for the project and repayment of the loans. The Bank funds its loans by raising money on the international bond market, issuing bonds in its name to large institutional international investors, such as banks and pension funds. As a non-profit institution, however, the Bank does not take any profit on the results of its fundraising. Instead, it uses its profits to subsidize its lending back to the countries whose projects its finances. Only about half of the Bank's funding comes from grants by members, and the rest comes from the Bank's own operations.

Examples of the programs the Bank funds include the following:

- In Bangladesh, the Bank provided a \$59.8 million credit to provide medical services and nutritional supplements to children and their mothers.
- In Bosnia, the Bank helps offer "microcredit" loans, typically less than \$1,000, to individuals who wish to start small businesses and otherwise would not have access to bank credit.
- In Peru, the Bank helped finance the Peru Rural Roads Program increase the connection of rural areas to each other and to urban centers as a way to increase economic activity.
- In Brazil, the Bank has provided funds to the government to run the Rain Forest Pilot Program to reduce deforestation in the state of Mato Grosso.



- In China, the Bank supported the Chinese government's National Iodine Deficiency Elimination Program by providing aid for upgrading physical plants for iodized salt production, packaging, and distribution, by establishing effective quality control in the salt industry, and funding the training of laboratory staff and the improvement of laboratory facilities.

### **International Development Association (IDA)**

The IDA was organized by the World Bank in 1960 in order to provide additional financial assistance to the poorest developing countries. In order to provide resources on better terms than those that are available from the Bank the IDA provides special "credits." These credits are zero-interest loans that have longer payment periods of 35 to 40 years and a grace period of 10 years. These types of loans are offered to the poorest countries to help them pursue their development goals, sometimes despite disease and conflict.

To help developing countries with these issues, the IDA has established a framework that emphasizes six core principles. First, the IDA seeks to promote growth through macroeconomic policy, especially in rural and private sector development. Second, the IDA concentrates on social issues such as gender equality and public health. Third, the IDA works to improve governance by assisting in public management and in combating corruption. Fourth, the IDA strives for sustainable development projects that help protect the environment. Fifth, the IDA fosters recovery efforts in post-conflict countries. Sixth, the IDA promotes economic integration through regional trade.

Examples of IDA projects include the following:

- In Chad, the IDA sponsored a \$41.5 million Health Sector Support Project to support the country's National Health Strategy.
- In Bhutan, the IDA gave a 10-year, \$31 million credit for construction of rural schools and curricula development.

### **International Finance Corporation (IFC)**

The IFC was established in 1956 and is now the largest public source of financial investment for private sector projects in developing countries. Unlike the grass-roots development efforts pursued by the IBRD and IDA, IFC investment is often used for projects such as building hotels or power plants, where finance and trade are more heavily involved. IFC provides private sector investment, helps companies acquire additional financing in international markets, and provides technical advice and assistance.

Examples of IFC work include the following:

- In Colombia, the IFC is financing the first stage of development of oil fields in Middle Magdalena Valley, providing loans totaling \$30 million from its own account and organizing a combined loan of \$25 million for a number of other private participants.
- In Azerbaijan, Georgia, and Turkey, the IFC is helping finance the construction of an oil pipeline to move up to a million barrels of oil per day from Baku, in Central Asia, to Ceyhan, on Turkey's Mediterranean coast.



### **Multilateral Investment Guarantee Agency (MIGA)**

MIGA created in 1988 to provide risk-balancing insurance services to foreign direct investment projects in developing countries. The typical service offered by MIGA is political risk insurance, which insulates investors against government expropriations, consequences of conflict, terrorism, and similar threats. This allows both investors and lenders to undertake commitments to such projects without the overwhelming downside risk that would otherwise exist. It also enables developing countries to attract and maintain private investment in their countries, which is essential to sustained development.

Membership in MIGA is offered to all member countries of the World Bank Group and currently numbers 161 countries. MIGA is operated by a Council of Governors, who recently voted to double the agency's capital stock from the current \$1 billion, to \$2 billion. A small amount of that (\$150 million) came in the form of limited financial assistance from the World Bank, and the remaining \$850 million increase was due to a capital increase.

Since it was established in 1988, MIGA has insured more than \$41 billion of foreign direct investment in 78 developing countries-investment that may not have otherwise happened. The result of all of MIGA's activities is that, with the potential reduction of risks through insurance, developing countries are encouraged to adopt policies that promote investment. This combination of reform at the domestic level and insurance coverage for investors is another important tool in the drive to reduce poverty by the World Bank Group.

Examples of MIGA projects include the following:

- In Azerbaijan, MIGAs provided insurance to protect Turkish investors in a project to expand and modernize a flourmill to produce and distribute flour sold in Azerbaijan and Georgia.
- In Ecuador, MIGA is supporting investors in the construction of a new airport to serve the capital of Quito in order to improve and expand economic development and trade.

### **International Center for Settlement of Investment Disputes (ICSID)**

The World Bank established ICSID in 1966 in order encourage both investors and governments to undertake and receive foreign direct investment by providing a neutral dispute resolution system. The ICSID provides arbitration services, which are entered into on a voluntary basis, but once two parties agree to submit issue resolution to ICSID, they are required to follow ICSID procedures until the verdict is rendered. Furthermore, all member countries of ICSID are bound to recognize and enforce the rulings that are made.

Although it is technically a separate entity ICSID is chaired by the president of the World Bank, and the two organizations are well integrated, with their annual meetings being held in concert, and with ICSID's operating expenses coming from the World Bank Group's budget.

### **Why is the World Bank Controversial?**

Like the IFM, the World Bank has been criticized for its part in promoting the Washington Consensus through its close participation with the IMF in lending only to programs that were heavily conditioned. For example, according to 50 Years Is Enough, the Bank's policies are



"indistinguishable" from the Fund's in that they often go to "austerity plans that 'reform' economic policies by suffocating the poor and inviting corporate exploitation."

In addition, several unique factors contribute to dislike and distrust of the Bank. The Bank is often accused of ignoring the environmental and social impact of projects it supports. For example, the Bank helped fund Brazil's Polonoroeste development program, inaugurated in the Amazonian state of Rondonia in 1981. By improving the main highway into the forest, subdividing the land, and granting ownership of the land to settlers, the program caused an intense migration and land rush that resulted in the wide-spread destruction of the rainforest. The Bank also funded a dam-building project in India that resulted in the forced resettlement of people the Narmada River Valley between 1978 and 1993. As dams were built on the river, territories that have been populated since pre-historic times were lost to man-made reservoirs, causing resentment and social turmoil, for which the Bank was blamed. Similarly, the Bank has been attacked for funding the Western Poverty Reduction Project in China that opponents of Chinese control of Tibet say will resettle 37,000 ethnic Chinese in the territory of Tibet.

Most recently, the Baku-Ceyhan pipeline mentioned above has garnered opposition because, its critics say, it will increase pollution in the region and world-wide through further use of fossil fuels, contribute to oil dependency in the economies of the countries involved, damage the forests and water supplies in the region, and contribute to human rights abuses.

Another major complaint about the Bank (as well as the Fund) is its role in causing high debt among developing countries. Although the Bank's loans are intended to help countries, they also cause those countries to take on debt that they must pay interest on and remain under the conditions of the institution. Over the last twenty years, these debts have piled up so much that, critics say, they amount to "perpetual debt" that the poor people of world are saddled with. According to 50 Years Is Enough, "External debt per capita for sub-Saharan Africa (not including South Africa) is \$365, while GNP per capita is just \$308." Many countries, say these critics, spend more on servicing their debt obligations than on basic social services.

To remedy this problem, a campaign has begun to get international banks-both the public development banks such as the World Bank and private banks-to eliminate the debt. According to the Jubilee movement (named after the Biblical practice of forgiving debts every fifty years), the campaigners "want to put an end to this system of deliberate exploitation which generates external debts for our countries, impoverishes billions of people and degrades our environment. It is a system which does not allow our communities, societies and nations to develop on their own terms, democratically, without domination and exploitation by foreign interests, and dictates from the OECD [Organization for Economic Cooperation and Development, countries who are the world's major economic powers] governments, the IMF, the World Bank and the WTO." Naturally, the Fund, the Bank and their private-sector allies oppose this campaign.

## Conclusion

The IFIs are pillars of globalization. Designed to help manage the international financial system, they have taken on major roles as drivers of closer economic integration of all the worlds countries, from the advanced to the last developed. They have provided funds and advice to assist countries with their economic development and policy-making. At the same time, they are subject to criticism on many levels-for their intrusiveness into the economic and political sovereignty of nations dependent on their aid, for their lack of transparency, and for the impact of their policies on societies and the environment.



The IFIs have responded with new programs to address these critiques. For example, the Fund has begun publishing Public Information Notices (PINs) regarding their Article IV consultations with governments. Also, the Fund has emphasized "ownership" by client countries of the policies it recommends. Finally, the Bank and the Fund are cooperating in the Heavily Indebted Poor Countries (HIPC) initiative to provide debt relief.

Whether or not these new policies will serve to mollify the IFIs critics remains to be seen. Protests continue against the IFIs, and it is likely that controversy about both them and globalization in general will continue for some time.