A SYMPOSIUM OF VIEWS

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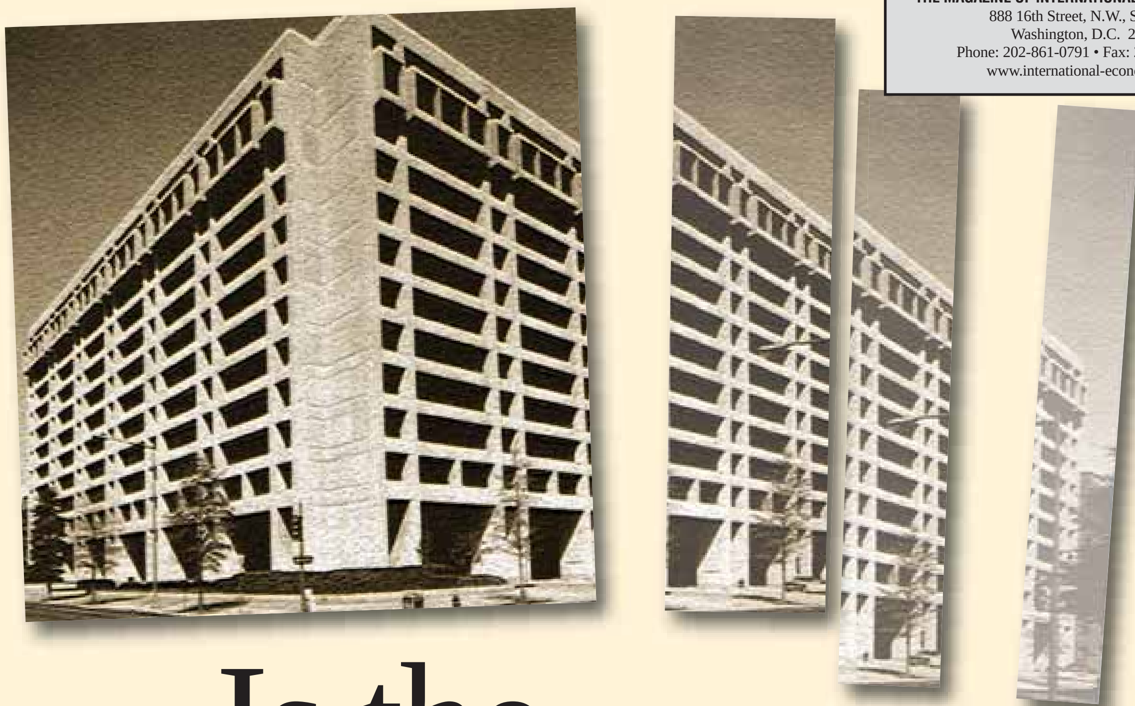


Is the IMF Obsolete?

Several years ago, even asking such a question would have seemed absurd. Yet today, with the narrowing of risk spreads in an era of increasingly interconnected markets and more efficient risk management, is the IMF's role still relevant? Has the rise of Asia, with its reliance on self-insurance by reserve accumulation since 1998, shown the Fund the door?

The institution already once in its history, after the United States went off the gold standard, redefined its mission. Is there a need for a second round of mission redefinition? If so, what's the next mission? Some have suggested the IMF become a technical assistance institution, helping the developing world set up better financial systems, but that would require market specialists, not the predominantly academic staff currently in place. Others have suggested the institution take on a new central role in multilateral surveillance, including of rich countries. The absence of volunteers, though, may make that idea stillborn. Still others suggest gains from consolidation by merging together the World Bank and the IMF. But that might make for conflicting irrelevant missions.

Never in the history of the world has a bureaucracy on its own shut itself down. Could this be the first time? Should it be?

No, recent developments simply make adapting to the new challenges all the more important.

JACQUES DE LAROSIÈRE
Advisor to the Chairman, BNP Paribas, and former Managing Director, International Monetary Fund

Financial developments have not, in my view, made the IMF obsolete. On the contrary, they have made its adaptation to the new challenges all the more important.

Three major developments have occurred. One is the mounting economic and financial power of a number of emerging countries that were formerly Fund borrowers and who are now the largest holders of international reserves of the world. How to better integrate those countries in the financial system?

The second challenge is that monetary stability is today more vulnerable in an environment of excessive indebtedness, asset bubbles, and underpriced risk. How can the Fund contribute to more stability?

The third factor is the present functioning of the exchange rate system. The Fund's Articles of agreement call for an active role for this institution in terms of multilateral "surveillance," which means a strong influence in the way underlying policies and interventions shape up exchange rates. How to achieve that aim?

These three major challenges will not be resolved only by a fairer distribution of quotas. They will also—and in my view more importantly—require a true political willingness of major countries (advanced and well as emerging), to abide by the policy recommendations of a strong and objective IMF.

The IMF has thrived by reinventing itself.

KENNETH ROGOFF
Thomas D. Cabot Professor of Public Policy, Harvard University, and Former Chief Economist and Director of Research, International Monetary Fund

The IMF has thrived over the years by constantly reinventing itself to meet the evolving needs of global financial governance. The fact that it now needs to do so again should inspire creativity rather than panic.

Some of the required reforms are manifestly clear and widely agreed upon. First and foremost, voting shares need to change to fully reflect the changes in the balance of global financial power. Asia should gain votes at the expense of Europe to a far greater degree than is currently being contemplated.

Second, Europeans need to relinquish their absurdly anachronistic prerogative of appointing the Fund's Managing Director. (Parenthetically, the United States should immediately and forever forfeit its right to appoint the head of the IMF's sister institution, the World Bank.)

Third, the Fund's governing board needs to put the Institution's financing on a sustainable basis by securely endowing it with the funds needed to pay for the IMF's surveillance and technical assistance activities, supplemented possibly by charges for the latter. Selling off a portion of the Fund's massive—and vestigial—gold supply would be a fine way to accomplish this.

After that, there is less agreement. I personally believe the Fund should phase out of the emerging market bailout business completely. The broad shift to stable macroeconomic policies, and especially to flexible exchange rates (a move the Fund fully embraced only well after the Asian crisis), has done far more to make the world less crisis-prone than any change in Fund bailout policies might have accomplished. Too often, adjustment is postponed and debt renegotiation is delayed when debtors and creditors believe official bailout money might be forthcoming. Stanford Professor Jeremy Bulow and I first highlighted this moral hazard problem in a series of papers some twenty years ago, albeit our concept was broader than the one sometimes used in popular discussions. The problem still seems central to me, even though some people close to bailout negotiations profess to be blind to it.

The IMF should be busy on two fronts.

GARY HUFBAUER
Reginald Jones Senior Fellow, Peterson Institute for International Economics

For many years the IMF hasn't had the financial or political muscle to shape up the big boys. The United States, European Union, Japan, and China can do pretty much as they please—in terms of fiscal stance, interest rates, or exchange rates—either cooperating or not as suits their tastes. For the big boys, the IMF can be no better than a scholarly scold. A useful role, to be sure, but not a task that justifies a staff of thousands.

But there is a vital dimension of the world economy where the IMF still has the brains and clout to make a difference. To be done right, this alternative task does require thousands of capable and experienced financial economists and computer wizards.

In his recent Ph.D. thesis, Hyun Koo Cho demonstrated that U.S. banking deregulation in the 1990s accentuated the volatility of bank lending to emerging markets. Since then, we have witnessed vast new waves of financial deregulation centered on hedge funds and private equity. Add to that the overwhelming evidence of herd behavior among financiers and crisis contagion between countries and the conclusion is inevitable. Anyone who thinks that the emerging market crises of the 1990s are a thing of the past is living in a dream world. The global financial shock in early March, emanating from a 9 percent drop in the Shanghai stock exchange, should awaken even the soundest sleeper.

Faced with this reality, the IMF should right now be busy on two fronts. First, it should create a real-time surveillance system for monitoring, on a confidential basis, the financial flows of the top players—the top two hundred banks, the top one hundred insurance companies, the top one hundred hedge funds. The emphasis should be on money flows in and out of emerging markets. This information can be used to warn financial players and countries of unusual buildups. It can also be used, in times of crisis, to counsel against herd behavior, and make proactive emergency loans.

Second, the IMF should augment its own financial war chest. Right now the Fund falls well short of the Pentagon's old readiness standard—an ability to fight two wars at the same time. Financial markets have been well-behaved for the past five years. But an era when global finance reaches new records every year is not a time for the Fund to be winding down its own resources. Instead, the Fund should be negotiating substantial unconditional swap lines with the major central banks, along with the flush central banks of nations such as Saudi Arabia, Singapore, and Switzerland. When the next financial firestorm rages, the last thing the world needs is a fireman with an empty hose.

We need a leaner and meaner IMF with a different kind of staff.

EDWIN M. TRUMAN
Senior Fellow, Peterson Institute for International Economics

The IMF is not obsolete. It is one of the principal institutions of global governance. Those who associate the Fund with financial rescue operations ignore the fact that less than 20 percent of its administrative expenses are associated with lending activities. The balance is involved in the provision of public goods in the form of surveillance of global economic and financial developments and vulnerabilities.

Benign conditions over the past five years have lulled many into the mistaken view that the bad old days of the 1990s are behind us forever. It is regrettable that the management of the institution and its principal shareholders have not been more proactive in putting in place needed reforms to reposition the IMF. Those reforms should start with governance reforms including the realignment of quota and voting shares with members' relative weights in the global economy as they have evolved over the past three decades in which no such adjustments have been made. The United States and Europe should also abandon their hold on the CEO positions at the World Bank and Fund. The Fund's role in surveillance of economic and financial policies should be upgraded. The Fund's capacity to provide high-access financing to members contingent on their strong policies should be further developed. Finally, as recommended in the Malan Report on Bank-Fund Collaboration, the Fund's engagement with low-income members needs to be scaled back and refocused.

All this may well require a leaner and meaner IMF with a different type of staff. It is not consistent with shutting down the Fund.

The IMF has lost a clear sense of purpose and must reorganize.

ALLAN MELTZER
Visiting Scholar, American Enterprise Institute, and Chairman, International Financial Institution Advisory Commission (1998–2000)

The IMF has lost a clear sense of mission and purpose, and it has lost the support of many members. Members have built reserves and made other arrangements to avoid borrowing from the IMF. Leadership of the IMF has been unwilling to reduce spending by closing the Poverty Reduction and Growth Facility.

The IMF should reorganize to achieve three tasks: first, prevention of systemic crises; second, improvements in the quality and quantity of information; and third, provide incentives for prudent financial behavior and open financial markets.

No, because success in dealing with the China currency issue requires international cooperation and multilateral surveillance.

JEFFREY A. FRANKEL
James W. Harpel Professor of Capital Formation and Growth, Kennedy School of Government, Harvard University

The IMF is by no means obsolete. That its resources are dwarfed by the magnitude of international financial markets is nothing new. It has redefined its mission not just once, with the break-up of the Bretton Woods system, but repeatedly: by switching emphasis to the balance of payments problems of developing countries who ran up large debts in the late 1970s, by adding to the problems of the transition economies after 1991, and by adding above-quota rescue packages and structural conditionality in its response to the emerging market crises of 1995–2002.

The Fund has always evolved with the times. This is appropriate and not primarily an example of mission creep. It is foolhardy to think, just because emerging market spreads have been very low recently, that there will be no more crises in the future; the international debt cycle tends to take fifteen years to repeat itself. It is likewise foolhardy to let the absence of outstanding business dictate the scope of operations—by all means sell gold if necessary to finance the institution.

That said, the Fund was handed a new mandate in the spring of 2006, both by its governing body and by the G7, that could restore it to central importance in the management of the world monetary system. But it would have to seize the opportunity more aggressively than it has, while continuing to navigate the treacherous big-power politics carefully. The mandate was to reconsider the 1977 Decision on Surveillance, and thereby look into the issue of global current account imbalances through a multilateral consultation process. In practical terms, this means that the U.S. Treasury in early 2006 passed the Chinese renminbi hot potato on to the IMF, giving that institution a rare potential opportunity to help midwife or broker a multilateral agreement over the Chinese currency and also G7 imbalances. Many economists identify the large U.S. current account deficit as far more a result of deficient U.S. national saving than of China's support of the dollar against its own currency. A cooperative agreement might entail concrete steps by the U.S. government to raise national saving, together with a decision by China jointly with other Asian countries—and oil exporters who are running even larger surpluses—to allow their currencies to appreciate simultaneously. Negotiations over such an agreement cannot take place in the G7 because China, Korea, Saudi Arabia, and the others are not members. The IMF is the logical place.

Agreeing on such multilateral cooperation will not be easy. Neither side can be dictated to, and both will be reluctant to make the necessary concessions voluntarily. The United States will not give up easily on the politically attractive idea of China as scapegoat for its trade imbalance, represented numerically by the bilateral deficit. China for its part will not give up easily on its sovereign right to move as slowly on currency reform as it deems in its interest. But the idea need not be stillborn. Both sides also have something important to lose if the issue is not settled. China's leaders run the danger of losing free access to the largest and most important export market. American leaders run the risk of the political momentum behind the scapegoat strategy backfiring, in the form of either self-inflicted protectionist legislation or a hard landing for the dollar and U.S. securities in global financial markets, or both. The renminbi/dollar rate and associated imbalances is a better subject for multilateral surveillance and international cooperation than any subject to come along in many years, and it is more likely to be amenable to progress in the forum of the IMF than anywhere else.

We should modernize the IMF.

RICHARD N. COOPER
Maurits C. Boas Professor of International Economics, Harvard University

All institutions need to adapt to evolutionary changes in economy and society. The operational question for the IMF is whether major financial disturbances are gone forever, and of interest from now on only to historians. Despite—or perhaps because of—low risk premiums today, the answer is assuredly negative. During the last several years the world economy has performed well, with high growth and low inflation, and primary product prices have risen from their lows early in the decade. These financially favorable conditions are not likely to last forever, and when economic activity and prices slacken, some countries will find themselves in financial trouble. Bankers love to lend to highly credit-worthy customers, but not to those in financial difficulty. Thus, private capital markets are no substitute for the IMF in times of financial distress, any more than they are substitutes for national central banks. We do not abolish fire departments just because we have had a run of time with no fires.

We should use this quiet period to modernize the IMF, including its governance. That implies the need to update member quotas and voting rights, and representation on the Executive Board, over one-third of whose directors are European. Total quotas need to be increased, reflecting the much larger size of the world economy, but differentially, to reflect relative changes in the world economy. East Asia, in particular, is badly under-represented, as well as some other emerging markets. Edwin Truman and I have made some concrete suggestions in a recent policy paper for the Peterson Institute for International Economics.

Technical assistance to developing countries on economic and financial management is an important by-product of the lMF's activities. Indeed, the training of past and future officials as members of its staff and in its seminar programs may well be its most important and durable activity. But such training is a by-product of its on-going monitoring of national economic activity, and assistance to countries in financial difficulty.

The IMF could be a natural leader in this brave new world, but isn't selling the moment.

JIM O'NEILL
Head of Global Economic Research, Goldman Sachs International

The one saving grace for the IMF is that they are not alone in their dilemma! In the world that has been evolving ever since the tragic events of September 11, it is not entirely clear what purpose remains for any of the post-World War II organizations. For the IMF, the World Bank, probably the United Nations, and most definitely the G7, G8, and G20, a serious reform has been years overdue. How any of these entities can hope to preside over the current and likely future world order in terms of trying to operate "optimal" policies is beyond me. China is highly likely to overtake Germany in 2007 or 2008 as the world's third-largest economy, and is placed well to challenge Japan for second largest by the middle of the next decade. India and Russia together have contributed more than half the total of the combined Eurozone to global growth since 2000. China and India are the world's most important marginal users of resources, and increasingly Brazil and Russia are the most marginal suppliers of new energy needs. Russia's foreign exchange reserves are bigger than those of all of the Eurozone countries combined!

I could go on and on. It is time for a wake up call amongst the old "industrialized elite." As far as the IMF is concerned, if it wants to be of relevance to the modern world, it needs to get noisier and stronger from within and without. If there is inertia from their old majority owners in Europe, it should say so. When asked to opine more publicly about equilibrium exchange rates, the IMF shouldn't be scared of the responsibility.

The new world order needs a credible, independent global institution to guide it, and make all the other entities—such as a revamped (and constantly reforming) G7 and G20—effective. The IMF should be a natural to lead this new world order, but unfortunately there is no sign they are really seizing the moment.

No, but the institution should further specialize.

BARRY EICHENGREEN
George C. Pardee and Helen N. Pardee Professor of Economics & Political Science, University of California, Berkeley

This question assumes that financial systems are now so strong and reserves so abundant that emergency financial assistance is redundant. I don't buy it. It is precisely when the markets are calm and commentators grow sanguine that risks build up. My own favorite early-warning indicator of financial crises is the number of newspaper articles calling for abolition of the IMF.

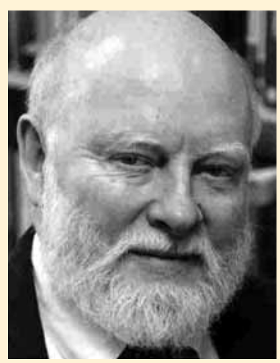
Of course, this leaves unresolved what insiders refer to as "modalities" for IMF surveillance and lending. Bilateral surveillance could usefully focus on problem countries rather than spanning the globe. Multilateral surveillance can never force rich countries to alter their policies, but the Fund could make better use of its bully pulpit. And although prequalifying countries with strong policies for a quick-disbursing high-access facility is a non-starter (how would you then un-prequalify them without precipitating a crisis?), more can be done to streamline both lending decisions and disbursement.

Should the World Bank and IMF be merged? At a minimum they should specialize further. The Bank should provide grants and technical assistance to poor countries, while the Fund should provide loans and surveillance of middle-income countries connected to international capital markets. To be sure, they should cooperate in areas like advice concerning financial markets. But merger is a bad idea: having the two institutions keeping a watchful eye on one another provides checks and balances.

No, the calm status quo of the financial sphere won't last.

JEFFREY E. GARTEN
Juan Trippe Professor of International Trade, Finance, and Business, Yale School of Management

No. The current state of the global economy, with its impressive growth, expanding trade and investment, and lack of systemic crises is not going to last. The need for strong global economic institutions will become more rather than less important in the years ahead, because national governments are increasingly ill-equipped to handle cross-border crises. In fact, for all the talk about multilateralism, we have barely begun to put in place the multilateral institutions that will be necessary to lend order to the burgeoning capital markets in the years ahead. Reforming and strengthening the IMF may be politically difficult, but it would be even more problematical to try to create a new institution.



Keep the IMF, if simply to enforce Article VIII.

RONALD I. MCKINNON
William D. Eberle Professor of International Economics, Stanford University

To explain the declining importance of the IMF in the new millennium, two features of the world economy stand out. First, the boom in primary commodities greatly improves the foreign trade positions of most third world countries. Second, the huge current account deficits of the United States have pre-empted much of the supply of private international finance that once flowed into developing countries. Both effects together now lead to net current account surpluses in lesser-developed countries—except for some African basket cases more the province of the World Bank, and smaller economies in Eastern Europe more the concern of the European Union.

This brave new world seems to be performing satisfactorily without the debt crises associated with episodes of over-borrowing in foreign exchange of the 1980s and 1990s for which the IMF was the fire fighter. Now the biggest debtor of all is the United States. Its central position in the world dollar standard allows it to go deeply into debt in its own currency with no threat of default. So the amount of foreign exchange risk in the new system overall is greatly reduced—and so is the need for IMF lending.

However, only diamonds are forever. For instance, another slump in primary commodity prices is possible. Moreover, the IMF is still an important international monitor. Although its original function of exchange rate stabilization has been undermined by the new mantra favoring exchange flexibility, the IMF is still very successful in enforcing Article VIII—the obligation of each member country to maintain current account convertibility. Without Article VIII, the world's money machine would be seriously impaired. The IMF also provides valuable advice in helping countries develop their internal financial systems.

We should keep the IMF, but how to pay for it is a story for another time.

No, there will always be problems to address.

NORBERT WALTER
Chief Economist, Deutsche Bank Group

Those who believe in the benefit of unilateral exchange rate policies—for example, the fundamentalist advocates of floating exchange rates—neither want the IMF's surveillance nor see any need for it. Now almost all those who defend pegged exchange rates—mostly to the weakening U.S. dollar—have amassed a multiple of the foreign exchange reserves needed to stabilize exchange rates. No wonder these factions' need for a lender of last international liquidity has gone out of the window. The IMF's massively reduced income from international lending, partly caused by early repayment of loans, brutally shows how the IMF has gone out of business.

Thus, while I agree that technical help to establish and/or improve financial systems in many countries is a much-neglected task, I would not allocate much of a micro and/or regulatory task to a unit basically learned in only macroeconomics. The Bank for International Settlements would perform such a role much better. I certainly do not favor an incursion by the IMF into World Bank territory. Some special facilities have gone much too far towards soft lending in the past and should be scaled back, if not abolished.

So should we close down the IMF? A clear "no" is my verdict. First, I am pretty sure that quite traditional balance of payment crises will reoccur and ought to find an institution on alert. Second, I am pretty sure macro policy surveillance including the exchange rate policies of rich countries and not just of the emerging and developing nations is of the essence. Deviations of exchange rates from fair value as unilateral means of solving domestic issues should only be accepted if they do not cause bigger trouble for the countries confronted with the unwelcome fallout of "the other guy's" exchange rate policy!

No, but the IMF must change.

HORST SIEBERT
President-Emeritus of the Kiel Institute for the World Economy

In no way have financial developments made the IMF obsolete. Currency crises are sure to stay. It is most likely that government policies will not always be able to prevent a widening gap between the real and the nominal exchange rate with a real appreciation driving up the current account deficit. This is what we have witnessed in the Mexican peso crisis in 1994, the Asian crisis in 1997, the Brazilian crisis in 1999, and the Argentine crisis in 2001–02. We cannot rule out surprises in the future. Remember how surprised we all were by the Asian crisis as a new phenomenon? And we also cannot rule out national banking crises. Just imagine a problem in the fragile Chinese banking system. In such financial crises, the exchange rate has to give. Financial market innovations in the last few years such as the rise of hedge funds have increased the systemic risk of the international financial system.

The experience with past currency crises shows severe repercussions: Savings and assets melt away and countries lose 20 percent of their real GDP in one or two years. Real wages and other incomes fall by a similar percentage. The real economy experiences a major disruption.

Consequently, there is no question that the world economy needs the IMF. Of course, the IMF has to change. Besides adjusting quotas, its mission has to focus on the task of preventing currency crises, its instruments have to be orientated towards this *ex ante* task, and it cannot be the disciplinarian of national states. Its mission cannot be overloaded with the target of promoting development of less-developed countries and reducing debt there, and it should not attempt to determine equilibrium exchange rates. This approach failed in the second part of the 1980s when the Louvre Accord and the Plaza Agreement paved the way for Japan's financial bubble.

The IMF must promote exchange rate surveillance and management of balance of payments crises.

DESMOND LACHMAN
Resident Fellow, American Enterprise Institute, former Deputy Director, Policy Development and Review, IMF, and former Chief Emerging Market Economist, Salomon Brothers

In today's world of unprecedented global payment imbalances and of major risks to the global economic recovery, there is as strong a need as ever for a multilateral institution to safeguard the international monetary system. In particular, at this time of rising protectionist pressures, one would want an institution specifically mandated to prevent a return to the "beggar-my-neighbor" policies of the 1920s and 1930s.

Sadly, today's IMF is patently not rising to that challenge. It says little about the numerous egregious cases of currency manipulation that thwart the global adjustment process. And it offers little leadership in helping to find a collaborative solution to the world's payment imbalance problem.

If the IMF is to have relevance in today's world, it needs to abandon its mantra of not wanting to be the world's exchange rate umpire. Rather, it needs to return to its original mandate of promoting international monetary cooperation through the very much more active exercise of multilateral exchange rate surveillance.

On the lending front, global capital market developments notwithstanding, the IMF will continue to have an important role to play in helping resolve emerging market balance of payment crises as they arise. It would be a mistake to assume that the remarkably benign external conditions, which emerging market economies have enjoyed over the past five years and which have allowed them to prepay the IMF, will endure indefinitely. Rather, one must anticipate that a number of emerging markets will again need major IMF support as they did in the past as international commodity prices decline and as global credit conditions become decidedly less supportive.

The IMF should lead the way on exchange rates.

MAKOTO UTSUMI
President and CEO, Japan Credit Rating Agency, Ltd.

The suspension of the U.S. dollar's convertibility with gold and the collapse of the fixed exchange rate system in 1971 shook the foundations of the IMF as the caretaker of the international monetary system.

The management of the exchange markets under the floating exchange system of the major currencies has been left to the G5 or G7, and the IMF has been excluded from the decision making.

But fundamental global changes, such as the emerging importance of many developing countries including China and some Asian countries, offer the IMF renewed importance as the caretaker of the international monetary system.

When the currencies of the G10 moved to the floating exchange system, no discussion was held in respect of currencies of the developing countries. It was taken for granted that these currencies belonging to smaller undeveloped economies would be pegged to one of the major currencies such as the dollar or pound, like satellites surrounding these major currencies.

But now China, for example, is too big to be treated as a satellite. It is the time for the international community to discuss what exchange rate systems should be adopted by the developing countries in order to contribute to the growth and sustainable equilibrium of the world economy. The system would probably vary depending on the stage of development, the importance as a stakeholder in the world economy, and so forth. This task should not be left to unilateral pressure by the United States nor the G7, but should be undertaken by the IMF. I strongly hope the IMF will take this initiative with the support of the international community.

No, it is still needed.

JEFFREY R. SHAFER
Vice Chairman of Global Banking and Head of Economic and Political Strategies, Citigroup, and former Under Secretary for International Affairs, U.S. Treasury

The world still needs an IMF. Markets are the best allocaters of capital available, but they can become unstable. The Fund's essential role, to paraphrase the Articles in today's terms, is to avert the buildup of conditions that could undermine market stability and to help countries respond to instability in order to mitigate the economic costs.

The risks of exchange rate and other financial instability can be reduced through effective monetary cooperation through the Article IV process and multilateral surveillance. But it is not realistic to think that these processes will ever eliminate the risk of financial disruption. For one thing, not even the Fund staff is wise enough to recognize all risks and remove them. But even more important, it is ultimately the governments of member countries who are responsible for implementing economic and financial policies and in most cases are accountable to their people. The Fund staff is not.

When markets do become unstable, a lender of last resort can greatly reduce the economic costs, as history has shown. The Fund's role as a lender to countries in financial distress will continue to be critical for as far ahead as one can see. Distress is likely to come in new forms and afflict different sets of countries than in the past. It is possible that the Fund in the future will deal more with isolated country problems than systemic ones. But I do not believe that systemic financial problems are a thing of the past simply because they are not visible on the horizon today. The Latin American crisis of 1982 was not apparent in 1979, nor was the Asian crisis of 1997 foreseeable in 1995. We will need a well-funded and well-staffed IMF with flexible operating rules to respond to the unforeseen when it happens.

For the moment, the IMF is a backwater. But conditions change.

MARINA V.N. WHITMAN
Professor of Business Administration and Public Policy, University of Michigan, and former member, President's Council of Economic Advisers

The IMF is in an institutional backwater at the moment, becalmed by managed flexibility of exchange rates, creditworthy countries' access to private capital through international markets, and the buildup of superprecautionary reserve balances by many Asian countries. But current conditions are not necessarily etched in stone, and if the IMF were abolished, there is a real possibility that it would have to be reinvented at some point in the future.

The fact that there have been no payments crises in recent years, of the sort that became endemic in the 1990s, doesn't guarantee that they won't reemerge. And the very countries that are most vulnerable to such crises are in many cases the same ones whose poor or deteriorating credit standing denies them access to private capital. The IMF's apparent recognition that its one-size fits-all approach to conditionality must be modified to take account of each borrower's particular circumstances should make potential borrowers less reluctant to turn to the Fund for assistance with a balance-of-payments problem.

At the same time, the Fund is attempting to strengthen its role in multilateral surveillance of the balance-of-payments and exchange rate policies of all its members in order to alleviate the problem of inconsistent goals. The fact that the leading industrialized countries show little enthusiasm at present for modifying their policies in this regard doesn't mean that they may not take a more cooperative stance at some point in the future, particularly as the relative size of international capital flows continues to increase. Should this development occur, the Fund is well-suited to assist its members in its implementation.

The alternative of merging the IMF and the World Bank would be a move in precisely the wrong direction at a time when a clearer definition and separation of the two institutions' roles is urgently needed in order to make their activities complementary rather overlapping. Under the guise of helping countries to meet "a protracted balance-of-payments need," the Fund has increasingly been making long-term loans at concessionary rates of interest whose real purpose is to alleviate poverty and/or support economic development in poor countries, functions which more appropriately fall under the purview of the Bank. Clearer separation of missions, not consolidation of the two institutions, is what is needed.

If the Fund vanished, another institution would have to take its place.

ANNE KRUEGER

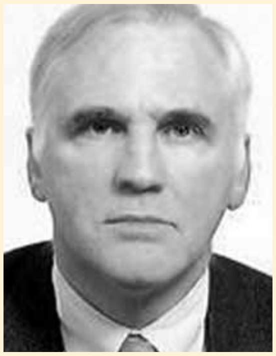
Professor of International Economics, Johns Hopkins School of Advanced International Studies, and former First Deputy Managing Director, International Monetary Fund

Throughout its history, the Fund and the international economy have had to meet new challenges. Starting with the need to achieve current account convertibility and remove quantitative restrictions under fixed exchange rates, the shift to flexible exchange rates on the part of industrial countries changed the Fund's role. In the 1970s, it was worldwide inflation and the oil price increase. The 1980s saw the debt crisis in developing countries, while the 1990s first saw the emergence of transition economies and their need for an appropriate macroeconomic framework and then capital account crises as private capital flows had increased greatly in absolute and relative importance.

The Fund's leadership in understanding and analyzing the issues through its research, technical assistance, and policy advice was a major factor in reducing the costs of these challenges. The continuing role of policy advice and technical assistance should not be underestimated.

Now that the United States no longer has such a large share of global transactions, multilateral consultations could become a significant mechanism when issues such as energy-related financial imbalances arise. The process has only just begun. It can be hoped that the process will evolve to be useful when future and perhaps urgent issues arise. But of course, it can only be as useful as the countries involved are willing to let it become.

There is no assurance that the world economy will always remain as buoyant as it now is, and new challenges will arise. Consultations will improve economic performance in individual countries. As the international economy evolves, the Fund and the international community need to keep learning and adapting to new challenges. If the Fund were shut down, another institution would have to be devised to take its place, and it is unlikely that agreement could be reached on one as effective as the Fund.



The Fund is adrift, but the members bear responsibility.

DANIEL K. TARULLO

Professor of Law, Georgetown University, and former Assistant to the President for International Economic Policy

There is little question but that the Fund is adrift. But this is less the fault of its management than its members. Only the Fund's powerful members have the ability to provide direction.

With currency crises in abeyance for the last five years, the Fund's established mission has become less relevant. With no consensus among large economies on whether—much less how—to correct global financial imbalances and thereby to limit the potential for severe and disruptive exchange rate movements, an updating of its original mission of exchange rate oversight has not been possible.

The officials and staff of the Fund can do relatively little about either of these circumstances. In such a situation, the self-preservation instinct of most organizations leads to a search for new missions that it can execute, in order to validate its continued operation. This can result in misguided initiatives, a number of which have been in evidence at the IMF in recent years. The Fund's membership should stop the organization from grasping for new but inappropriate roles.

More importantly, the membership—beginning with the United States—must take responsibility first for defining the Fund's missions, and then for providing the guidance and resources necessary to achieve them. For all that has changed in recent decades, the Fund's core missions should be the two that have defined its existence to date: providing an insurance policy against possible emerging market currency crises arising from as yet undetected vulnerabilities, and providing a mechanism for safeguarding global financial stability. The latter mission must be pursued very differently than it was under the postwar par value system—at least at the outset, it is most realistic to institute multilateral surveillance and structured discussions among members on economic and exchange rate policies. Over time, a more robust set of policies may prove workable.

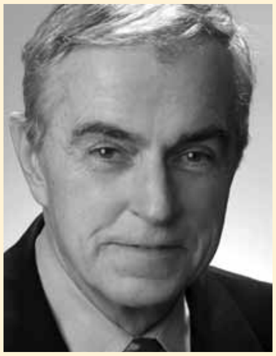
The institution, to catch up to the latest developments, needs to reform itself.

STEFAN INGVES
Governor, the Riksbank (Central Bank of Sweden)

Financial developments in the past decades have been fast, and this development is welcome. However, it also confronts us with new challenges to which the Fund must adapt. That said, it is hard to find any other organization more able to deal with the challenges posed by increased financial integration and this makes the role of the IMF more relevant than ever. When working with financial issues today one has to look across borders. International cooperation is key and the Fund's nearly universal membership, in combination with the gathering of expertise and experience among Fund staff, is a unique and indispensable asset.

What the IMF needs to do is to catch up with developments by reforming itself. The ongoing implementation of reforms in the Fund is promising. I welcome the increased focus on surveillance, in particular the efforts to better integrate financial issues with the macroeconomic aspects of Fund surveillance. Helping to build national institutions and expertise in order to assist countries in adapting to financial developments is another important task for the Fund.

When reforming itself the Fund should stick to its core mandate, which is essentially within the realm of macroeconomic and financial stability, and its performance should also be assessed against this mandate. Within these boundaries, the IMF must be responsive to the needs of all groups of members. If members are to listen to the advice of the Fund, they must also feel that they are listened to, that they have a voice. This is where the issue of IMF governance comes in and where the effectiveness and the legitimacy of the Fund come together. I remain optimistic about the Fund's ability to deliver. But actions speak louder than words and we are not quite there yet.



Don't expect more than the IMF can deliver.

RICHARD ERB
Former Deputy Assistant Secretary for Developing Nations Finance, U.S. Treasury, former U.S. Executive Director and Deputy Managing Director, International Monetary Fund, and Senior Fellow, Montana World Affairs Council

The founders clearly and succinctly defined the IMF's mission in Article I of the IMF Articles of Agreement titled Purposes. Those Purposes are even more relevant in our highly integrated global economy than they were in the balkanized world of 1945. Thus, the key question facing the international community is how to maintain and indeed strengthen the ability of the IMF to fulfill its mission.

The first Purpose established the IMF as a forum "for consultation and collaboration on international monetary problems." The IMF is the only global multilateral institution that brings officials with monetary and financial responsibilities together to monitor international developments and to respond when problems arise. It would be foolish to assume that the world has entered an "end of crises" stage in its history.

A second Purpose commissions the IMF to "promote exchange stability, maintain orderly exchange arrangements, and avoid competitive exchange depreciation." No mention is made of an exchange rate system pegged to a gold-based U.S. dollar. The underlying developments that contributed to the collapse of that regime, including the dramatic growth in multilateral trade, financial, and monetary flows, did not alter or diminish the exchange Purpose of the IMF.

In fact, the IMF's exchange mission became more demanding both for the membership and the organization. The 1976 Article IV amendment codified the economic policy obligations of IMF members and the consultation and surveillance activities of the IMF organization. It is in this area where there is more than a little room for improvement.

For one thing, member governments need to do a better job in fulfilling their Article IV economic policy obligations. In that context, annual Article IV consultations provide an opportunity for IMF staff to analyze and provide policy advice to member governments.

The IMF staff also is expected to judge when a country is pursuing a policy of "competitive exchange rate depreciation." But those staff roles conflict.

To eliminate that conflict, a small independent body of experts should be established in the IMF to serve as an exchange rate judge in controversial cases. It should be up to the IMF Executive Board to decide if penalties are merited. Unless the IMF performs these two functions, there is a danger that posturing politicians may assume these roles.

It often is asserted that the breakdown of the Bretton Woods fixed exchange rate system led the IMF, in good bureaucratic fashion, to redefine its mission and embark on a major lending program to developing countries. As I recall the events of the 1970s, that interpretation of history is backwards.

By the 1970s, many developing countries with balance of payments problems had become members of the IMF and vigorously sought access to IMF balance of payments financing in accordance with the Purposes of the IMF. Foreign ministries, development agencies, and early versions of non-governmental organizations also pressed the IMF to lend to developing countries. Finance ministries, who should have been more cautious, also pressed the IMF to lend to developing countries in support of Paris Club agreements.

On the other hand, I recall that many IMF "bureaucrats" were reluctant lenders of temporary finance to developing countries. Yes, developing countries needed macroeconomic policy analysis and advice, but the IMF's capital structure did not fit their balance of payments financing needs, especially among the low-income countries. What the IMF needed and still needs is a financial facility capable of providing long-term finance on grant terms to low-income countries. The finance would be dedicated to enhancing a country's reserves, a need that is neglected by all other sources of development assistance.

IMF management and staff should work to improve the performance of the IMF. But given that economic policies remain firmly in the hands of member governments as they should, and given that member governments determine IMF policies and decisions, it is a mistake to expect more from the IMF than its member governments allow.

No, the IMF could be the coordinator of liquidity.

CHARLES W. CALOMIRIS
Henry Kaufman Professor of Financial Institutions, Columbia University Graduate School of Business

The IMF has a legitimate mission, but it has not focused on that mission or restructured its lending policies or governance to achieve it. The IMF should not be a policy coercer. Its efficacy in that role has been mixed at best, and it is no longer obvious how coercion would be applied. Are Japan, China, Brazil, Mexico, India, Korea, Russia, the United States, and the European Union likely to agree on what sort of coercion should be applied to Pakistan or Turkey?

The IMF could play an important role as a coordinator of liquidity to prevent and mitigate emerging market crises. But the IMF today lacks the size and structure to provide meaningful liquidity. The key impediment is political. Because member countries have not agreed on this narrow focus they have not created the rules necessary to implement it. Instead, the IMF drifts with an ineffectual structure, undefined mission, and limited resources.

The IMF should create one assistance mechanism to replace all others. This new line of credit should be supplied under credibly enforced rules, defined in advance, that would limit the abuse of the line by constraining discretion in determining the terms on which credit could be supplied. IMF governance reform is the first step toward achieving these objectives. Governance reform does not mean broadening political control through changes in members' voting rights. It makes little sense for the IMF to be governed by finance ministers who can be relied upon to resist any rules that limit their discretionary interventions. It makes more sense to empower G7 central bankers to take the lead in establishing new rules for the IMF and in implementing them. They are familiar with the challenges of managing liquidity crises, have control over the supply of liquidity, and are relatively insulated from political pressures.

We need the right IMF more than ever.

WOLFGANG ROTH

Former member, German Parliament, and former Vice-President, European Investment Bank

After some years without a crisis, public opinion is apt to shift towards the notion that the future will be stable. Again and again such dreams arise. We seem to be in such period. Older people recall fondly the idea of secular growth. Globalization and the increase of mutual interdependence are trusted to produce international self-regulation. With less intervention in international markets, the invisible hand is thought to have a chance to produce worldwide stability. All these illusions have become popular again.

The opposite might be true. Interdependence could mean that worldwide waves could come in the same direction and magnitude—such as down. The possibility of economic tsunamis can't be excluded. Not only can governments make mistakes, but markets can also fail. How many bubbles do we need to learn this? The sheer volume of monetary and speculative movements could create systematic dangers. Naturally, nobody knows the dangers waiting in the future exactly, but fears of a worldwide bubble cannot be ignored.

Some say the best policy to guard against dangers is to produce market optimism. That is good guidance for the world of real investments in research and development, in tangible assets and infrastructure. But it is not the right mood in the world of volatile monetary capital.

We need in the future an international body of special control. Is that the IMF? Not really. They watch over national budgets and balance of payments and some other important things.

We need the right IMF more than ever. We need the IMF as a body of surveillance of international capital movements, of controlling the impact of new financial products. Who else besides an IMF-like organization could monitor inherent speculative risks and systemic dangers?

This idea looks naive. But I am sure after the next financial crisis new responsibilities for the IMF will be discussed seriously. History shows that politics means learning not by doing, but by learning through mistakes and disasters.

The IMF is not obsolete, but outdated.

MARC LELAND

President, Marc Leland and Associates, Co-Chairman, German Marshall Fund of the United States, and former Assistant Secretary for International Affairs, U.S. Treasury

The IMF as it presently operates is not obsolete, but outdated. The developed world, however, cannot let it go out of business because an organization with its voting structure could not be recreated. The World Bank has already excessively expanded its mission so a merger would only make matters worse. Technical assistance plus Article III reviews should be the IMF's mission. That probably means a staff with different expertise, but that would reinvigorate the institution.