Economic Commentaries

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The world needs a strong IMF

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"Finance ministers and central bank governors from around the world will gather in Washington on 25–26 April to attend the spring meetings of the International Monetary Fund (IMF) and the World Bank. Whereas a year ago they may have questioned the IMF as an institution, many member countries are now standing in line to borrow money from the Fund. Not since the IMF was created in 1944 has it been so sharply in focus as it is today. A central issue at this year's spring meetings will be to ensure that the IMF has sufficient funding to meet the increasing borrowing needs in connection with the global financial crisis. Another important issue relates to how the influence of the member countries within the IMF should be allocated. The financial crisis has entailed increased pressure to give emerging markets more influence. This will in turn increase the pressure on the member states of the EU to relinquish some of their influence. It is vital to ensure that both of these issues are dealt with in a reasonable way in the period ahead," writes the Governor of the Riksbank, Stefan Ingves.

As the financial crisis has worsened, more countries have turned to the IMF for financial assistance. The members now support moves to increase the Fund's resources from USD 250 billion to USD 750 billion. It is, however, not entirely clear how this tripling of the resources should be achieved. The process can be viewed from three perspectives. In the short term, there is in principle only one option available, namely that the member countries provide short-term loans to the Fund. Here, the EU countries have agreed to lend EUR 75 billion in all to the IMF. The Riksbank has already decided to contribute Sweden's share of this amount; that is EUR 2.47 billion, or approximately SEK 27 billion. In the longer term, financial resources can be provided using the so-called New Arrangements to Borrow, or the NAB, which at present amount to approximately USD 50 billion. The NAB can be regarded as the IMF's "reserve tank" for lending when its own resources are not sufficient. Now that there is a need to extend the NAB it is important to involve more countries in the system and some emerging markets, for example China, have large foreign currency reserves that could be useful. However, increasing the resources and the number of member countries in the NAB will take some time as this requires negotiations between several countries. At present, Sweden's and the Riksbank's share in the NAB amounts to approximately SEK 10 billion. Any increase in Sweden's commitments would require parliamentary approval. In the even longer term, there may be a need to increase the resources of the IMF by increasing the member countries' capital contributions to the Fund; that is their so-called quotas. This is the normal way of increasing the Fund's resources. However, this also takes a long time and, like the NAB, would require parliamentary approval in Sweden's case.

It is clear that the IMF needs more money. The Fund has recently set up a Flexible Credit Line facility which implies a sort of insurance from the IMF for countries that conduct sound economic policies. Over a short period of time, Colombia, Mexico and Poland have applied for such loan pledges amounting to a total of USD 85 billion. Applications can be expected from more countries. Previously, such countries could only get insurance of this type by turning to central banks, which entailed the risk that the countries would be treated differently. It is therefore welcome that a multilateral institution like the IMF has instead taken over such an insurance role. This type of insurance is also something that the emerging markets have been demanding for a long time and by setting it up the IMF has shown that it takes the needs of the member countries seriously.

The financial crisis has also led to a renewed interest in the issue of the influence of the emerging markets within the IMF. It is reasonable that as the emerging market economies grow they should have more say in the IMF. Low-income countries must also be guaranteed fair representation. This will increase the legitimacy of the IMF, but at the same time means that the influence of other countries will lessen. The European countries, in particular, are being subjected to heavy pressure to reduce their representation, and this may eventually happen, especially for the countries that have adopted the euro as their common currency. However, decisions concerning the consolidation of the EU must be made by the European countries themselves. Nor should it be forgotten that the European countries still constitute a considerable share of the world economy and that they contribute major resources to the IMF. In the next steps of the process we must make sure that the small countries retain a reasonable degree of representation. The smaller European countries must not be absorbed by the representation of the large European countries. If the small countries are unable to retain a reasonable level of influence there is a risk that the IMF will eventually lose legitimacy, which will probably reduce the willingness of the countries to contribute financially to the Fund. Taxpayers in all the member countries must be able to see that they have some influence over where the money is used.

The IMF has demonstrated its ability to quickly adapt to the needs of the member countries and to provide assistance to countries as the financial crisis has worsened. The financial crisis has shown that the global community needs a strong IMF that has stable funding in order to deal with the borrowing requirements of the member countries. The IMF must also have legitimacy in the eyes of all the member countries. The stronger and more legitimate the IMF is, the greater is the likelihood that multilateral discussions on the financial crisis will be conducted among the 185 countries belonging to the IMF and not in other, more limited forums. The meeting in Washington this weekend will therefore be an unusually important one.