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The World Financial Order
International Economic Law

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A brief review…

- The terms of peace in the Treaty of Versailles
- Keynes' critique
- The Allies learnt their lesson…
- The IMF as one of the post-WWII institutions

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II. IMF and World Bank

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IMF and World Bank

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1. International Monetary Fund

Conditionality…

- …to safeguard the Fund’s financial resources.
- …to ensure that the money is used “for the right purpose”.

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1. International Monetary Fund

Types of conditionality

- Financial conditionality: interest rate and loan repayment schedule
- Macroeconomic conditionality: government budget deficit, interest rates, money supply…
- Structural conditionality: reform of domestic tax laws, privatizations, governance reforms…

1. International Monetary Fund

IMF conditionality has created much controversy…

- Legitimacy?
- Effectiveness?
- Uniformity of treatment?

- IMF as a political scapegoat?

1. International Monetary Fund

Conditionality – mission creep?

"Conditions will normally consist of macroeconomic variables and structural measures that are within the Fund's <u>core areas of responsibility</u>. Variables and measures that are outside the Fund's core areas of responsibility may also be established as conditions but may <u>require more detailed explanation of their critical importance</u>."

IMF Guidelines on Conditionality (2002)

1. International Monetary Fund

Conditionality

Core areas of responsibility?	
Macroeconomic stabilization	✔
Governance of the Central Bank	✔
Establishment of democratic political structures	✖
Observance of human rights	✖
Establishment of a deposit insurance system for banks	✔
Reduction of military spending	✖
Cooperation with international criminal tribunal	✖

1. International Monetary Fund

Conditionality – recent developments

- Increased transparency of lending operations
- Concept of "country ownership"
- More comprehensive consultations with governments and civil society
- Focus on core mandate

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2. World Bank

Why is development important today?

- Widening income disparities as a threat to "social stability within countries and (…) security on a global scale" (WEF, Outlook on the Global Agenda 2014)
- Oxfam report (2014)
  - Almost half of the world's wealth is now owned by just one percent of the population.
  - The bottom half of the world's population owns the same as the richest 85 people in the world.

2. World Bank (Group)

Institution	Mandate
International Bank for Reconstruction and Development (IBRD)	Lending to and advising of middle-income and creditworthy poorer countries
International Development Association (IDA)	Concessional lending to and advising of the poorest countries
International Finance Corporation (IFC)	Investment and advisory services to businesses and private projects
Multilateral Investment Guarantee Agency (MIGA)	Investment guarantees/insurance to foreign direct investments
International Center for Settlement of Investment Disputes (ICSID)	Impartial arbitration institution for the resolution of private investment disputes

2. World Bank

Governance

- Board of Governors: One Governor and Alternate Governor per member
- Executive Board: 25 Executive Directors, organized in “constituencies” (voting power depends on represented share capital)
- President of the WB Group

2. World Bank

Lending/Financing

IBRD and IDA → Mostly sovereign governments

IFC and MIGA → Mostly private sector entities

2. World Bank

Lending/Financing

IBRD	IDA
“hard lending”	“soft lending”
Mostly middle-income countries + “blend” countries	Poorest countries (GNI per capita < USD 1,205 in 2014) + “blend” countries
Maturities of up to 30 yrs. (typically 5-10 yrs.)	Maturities of up to 40 yrs.

2. World Bank

Financial Resources

IBRD	IDA	IFC
Bond sales in capital markets	"Replenishment rounds", i.e. member contributions	Borrowing in capital markets
Interest on loans	Virtually no interest income	Interest on loans
Return on equity	Cross-subsidies from IBRD and IFC	Loans from IBRD

2. World Bank

"Knowledge Bank"

- Global research (e.g., on poverty, trade, globalization, environment…)
- Country-specific economic and sector work (evaluation of countries' banking systems, financial markets, trade, infrastructure, social safety net...)

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2. World Bank

IMF-WB Cooperation

- IMF - World Bank Concordat (1989)
- Regular cooperation
  - IMF Managing Director – WB President meetings
  - Staff meetings
  - Routine exchange of information
  - Joint missions
- Cross-conditionality?

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2. World Bank

IMF-WB Cooperation

- Joint initiatives
  - Heavily Indebted Poor Countries (HIPC) Initiative
  - Poverty Reduction Strategy Paper
  - Global Monitoring Report
  - Financial Sector Assessment Program (FSAP)
- High-level meetings
  - IMF and WB Boards of Governors Annual Meetings
  - Development Committee semi-annual meetings

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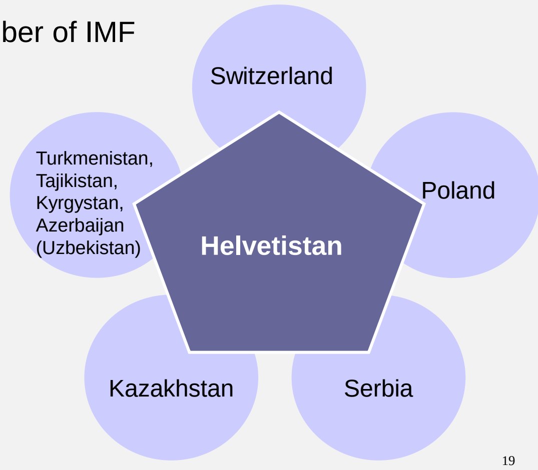
2. World Bank

Switzerland as a Member of IMF and WB

- IMF (1992)
- IBRD & IDA (1992)
- IFC (1992)
- MIGA (1988)
- ICSID (1998)



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Which institution(s)…

- …would likely hire a nutrition specialist?
- …deal(s) with the poorest countries in the world?
- …offer(s) concessional financial assistance?
- …cannot borrow in capital markets?
- …is/are mandated to finance government deficits?
- …conduct(s) Financial Sector Assessments?

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III. International Monetary Policy

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International Monetary Policy

1. Gold Standard (1879-1914)

- Currency is convertible into a preset, fixed quantity of gold
- Fixed exchange rates among participating countries
- Advantage: Limits the power of governments to inflate prices through excessive issuance of paper currency
- Disadvantage: Highly inflexible, as money supply is determined by the amount of gold production

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2. Bretton Woods System (1944-1973)

- Replaced gold with the USD ("dollar standard")
- System of fixed but adjustable exchange rates anchored on a gold-convertible USD
- Adjustments of >10% required IMF approval and was contingent on a fundamental disequilibrium in a country's balance of payments

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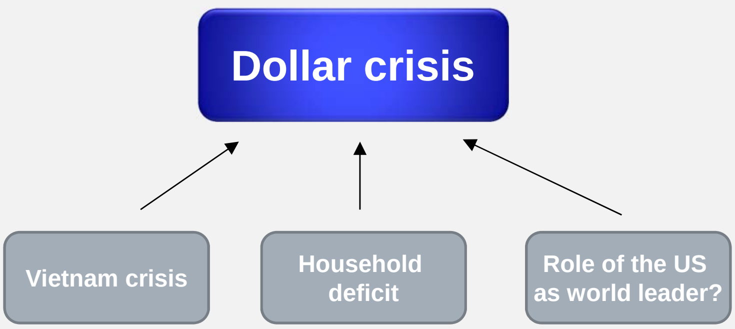
3. Transition to Floating Exchange Rates



3. Transition to Floating Exchange Rates

- Dollar’s fixed value against gold became increasingly overvalued
- August 1971: Nixon “temporarily” suspends USD-gold convertibility
- Attempts to revive the Bretton Woods system failed

3. Transition to Floating Exchange Rates

- Since 1978, members are free to choose their exchange-rate regime (except pegging to gold)

“The IMF allows each member country to choose its own method of determining the exchange value of its money. The only requirements are that the member no longer base the value of its currency on gold (which has proved to be too inflexible) and inform other members about precisely how it is determining the currency’s value.”

4. Overview of Exchange-Rate Regimes

- Floating exchange rate
- Peg to another currency (or basket)
- Adoption of another country's currency
- Participation in a currency bloc
- Participation in a monetary union

IV. Responding to the Financial and Economic Crisis

1. Pre-crisis Developments

Is the IMF still needed?

- Large accumulation of foreign exchange reserves in emerging markets
- Reorientation towards regional arrangements (EU, ASEAN, Mercosur)
- Massive drop in the Fund's lending activities

2. European Debt Crisis

Country	Duration	IMF contribution	Total aid
Hungary	11/2008-10/2010	EUR 12.5 bn	EUR 20 bn
Latvia	12/2008-12/2010	EUR 1.7 bn	EUR 7.5 bn
Romania	5/2009-6/2011	EUR 13.6 bn	EUR 20.6 bn
Greece	5/2010-3/2016	EUR 48.1 bn	EUR 245.6 bn
Ireland	11/2010-12/2013	EUR 22.5 bn	EUR 67.5 bn
Portugal	5/2011-5/2013	EUR 26 bn	EUR 78 bn
Spain	7/2012-12/2013	--	EUR 100 bn
Poland	1/2013-1/2015	EUR 25.2 bn	EUR 25.2 bn
Cyprus	5/2013-3/2016	EUR 1 bn	EUR 10 bn
Total	**11/2008-3/2016**	**EUR 154.2**	**EUR 574.4**

2. European Debt Crisis

Facility	Aim	Possible beneficiaries
Balance of Payments (BoP) assistance	Easing of external financing constraints	Only non-euro area countries
European Stability Mechanism (ESM)	Financial stability	• Euro area governments • Banks established in euro area countries
ECB Outright Monetary Transactions	Price stability	Euro area governments (purchases of sovereign bonds on secondary markets)

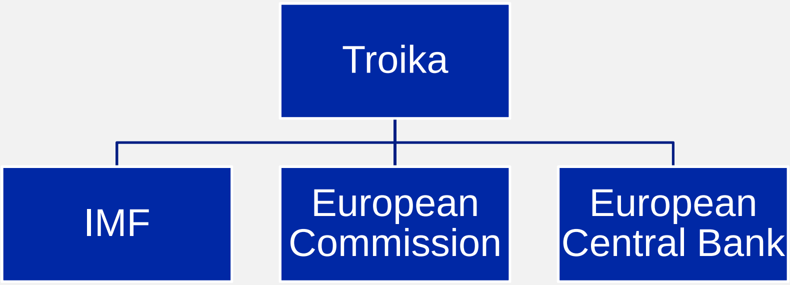
2. European Debt Crisis

IMF participation in…

- …providing financial assistance
- …designing economic adjustment programs
- …monitoring the adjustment in quarterly reviews

2. European Debt Crisis

The Emergence of “Troika”



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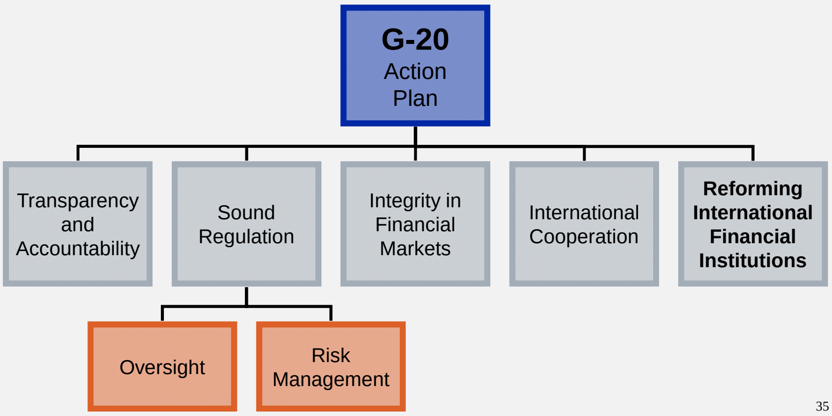
2. European Debt Crisis

Advantages and disadvantages of IMF participation

+	-
Experience and credibility	Overstepping the mandate?
Conditionality and moral hazard	Sufficiency of Fund resources?
Additional source of funds	Disproportionate focus on Europe?

3. Governance Reform

G-20 Summit Washington, 15 November 2008



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3. Governance Reform

The G-20 Agenda

- Sufficient resources for IMF and World Bank to overcome the crisis
- IMF and World Bank to adapt their lending facilities in the light of the crisis
- Help emerging and developing economies regain access to finance
- Increased focus of surveillance on the financial sector

3. Governance Reform

The G-20 Agenda – Additional Resources

- Increase IMF resources by USD 250 bn through immediate contributions from some members
- Use additional resources from sales of IMF gold to provide USD 6 bn in additional financing for poor countries
- General SDRs allocation equivalent to USD 250 bn to boost global liquidity
- Special SDRs allocation to make the allocation of SDRs more equitable

3. Governance Reform

The G-20 Agenda – Quota Review

"We are committed to advancing the reform of the Bretton Woods Institutions so that they can more adequately reflect changing economic weights in the world economy in order to increase their legitimacy and effectiveness. In this respect, emerging and developing economies, including the poorest countries, should have greater voice and representation."

Declaration, Summit on Financial Markets and the World Economy, 15 November 2008

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3. Governance Reform

14th General Review of Quotas

- Doubling of quotas from approx. SDR 238.5 bn to SDR 477 bn
- Shift of more than 6% of quota shares from over-represented to under-represented member countries
- China will become 3rd largest member in the IMF
- BRIC countries among the 10 largest shareholders in the Fund
- Preservation of the voice of low-income countries
- 15th General Review postponed in January 2014

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