



## **Background**

On 13<sup>th</sup> January 2010, the Irish government decided in principle to provide the International Monetary Fund (IMF) with a loan facility of approximately € 2 billion from Irish Central Bank resources.<sup>1</sup> The loan facility is part of a wider EU contribution to the IMF as a result of a G20 agreement made in April 2009 to empower the IMF to provide loans to countries affected by the global financial crisis.<sup>2</sup> This includes a commitment of up to US\$ 500 billion, tripling the total pre-crisis lending resources of the IMF to US\$ 750 billion.<sup>3</sup>

The legislation which may enable the Irish loan facility was included in the Finance Act 2010 based on an amendment to the Finance Bill which proposes amending the Bretton Woods Agreement Act 1957.<sup>4</sup> It appears that final approval of this amendment will be required by the Dáil due to the international nature of the Bretton Woods Agreement Act. Minister for Finance Brian Lenihan indicated that the legislation, if approved, will enable Ireland to provide a € 2 billion loan facility to the IMF to support all IMF member countries with balance of payments or financing needs, irrespective of income group.<sup>5</sup> In September 2009, EU Heads of State agreed that the total EU contribution to the IMF increase would be € 125 billion. Ireland's contribution will be approximately € 2 billion calculated based on its quota share at the IMF. Minister Lenihan proposes to make the commitment in 2 steps: through the creation of a bi-lateral loan facility to the IMF of € 1.3bn; followed by a further provision through joining, for the first time, the New Arrangements to Borrow (NAB) facility at the IMF.<sup>6</sup>

It appears that the loan facility functions as a loan 'promise' or 'reserve', to be drawn down and transferred if the IMF requests it. It is possible that the loan may not be required by the IMF, yet recent developments in Greece and elsewhere may cause it to be drawn down due to renewed financial stress on the institution. In practice, it is possible that the resources from this type of loan will feed into the IMF's general

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<sup>1</sup> Response to Parliamentary Question: PQ 6962/10 9<sup>th</sup> February

<sup>2</sup> The agreement was subsequently endorsed by the International Monetary and Financial Committee, and the European Council and Ecofin Ministers

<sup>3</sup> See commitments already made to this fund at:

<http://www.imf.org/external/np/exr/faq/contribution.htm>

<sup>4</sup> Referenced in the *Fourth List of Amendments, Finance Bill 2010, Section 160 'Amendment of Bretton Woods Agreement Act'*, p.4.

<sup>5</sup> Response to Parliamentary Question: PQ 9487/10 24<sup>th</sup> February 2010

<sup>6</sup> Response to Parliamentary Question: PQ 9487/10 24<sup>th</sup> February 2010. The NAB is a set of credit arrangements between the IMF and member countries and institutions to provide supplementary resources to the IMF in a situation of instability in the international monetary system. Negotiations are currently underway to expand the NAB in the context of the global financial crisis.

resources to fund its three major non-concessional lending arms.<sup>7</sup> These funding arms are generally utilised by ‘Middle Income’ developing countries. But as the terms and conditions of the loan have not been finalised, who the end users will be remains unclear. Minister for Finance Brian Lenihan has indicated that if the loan is drawn down, there is ‘*a potential indirect loss to the exchequer of up to €15 million on the occasion the IMF draws down the entire amount*’.<sup>8</sup>

## **DDCI Opposes the IMF Loan Facility as Currently Proposed**

DDCI opposes the loan facility as it is currently proposed because:

- 1. The IMF has seriously damaged the lives of people living in developing countries through the application of policy conditions and all the signs show that it will continue to do so.** Up-to-date research on the IMF’s response to the current financial crisis demonstrates that the institution is continuing to apply much the same framework in its policy conditions to Low and Middle Income Countries as it has in the past.<sup>9</sup> Despite some new levels of flexibility, the conditions being applied show that the IMF is largely continuing to promote its usual pro-cyclical measures including strong limits to public expenditure, excessively strict monetary policies and an over preoccupation with ensuring debt repayments. This represents the same short-sighted framework applied by the IMF over many years, which fails to take into account the specific needs of developing countries, especially in Low Income Countries, as outlined further below. Despite this bad track record, the IMF continues to act as a gatekeeper for financial flows into developing countries. This means that the IMF may halt badly needed ODA (Official Development Assistance) to developing countries if they are not viewed as ‘on track’ with their IMF arrangements.
- 2. Extending the loan facility in its current form, would represent an enormous missed opportunity for Ireland to advocate strongly for IMF reform.** If the loan facility is made in the current form it would undermine key areas of Irish development policy including:
  - **Ireland’s support for developing country-led responses to fighting poverty and Ireland’s commitment to partnership and coherence in**

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<sup>7</sup> Including the IMF Stand-By Arrangements (SBA), the Flexible Credit Line (FCL), and the Extended Fund Facility (EFF).

<sup>8</sup> Response to Parliamentary Question: PQ 6962 /10, 9<sup>th</sup> February 2010: Minister Lenihan: ‘*If there is no drawdown of the facility, there will be no impact on the Exchequer. If there is a drawdown, the impact would only arise indirectly in terms of a potential reduction in the surplus income remitted to the Exchequer by the Central Bank - which at current interest rate levels is estimated at €15 million per annum, based on a drawdown of the full amount of €2bn. If the drawdown is less, the indirect impact would be less*’.

<sup>9</sup> Mulina, Nuria, *Bail-out or blow-out? IMF policy advice and conditions for low-income countries at a time of crisis*, Eurodad, 2009; Van Waeyenberge, Elisa, Bargawi, Hannah and McKinley, Terry, *Standing in the way of development? A critical survey of the IMF’s crisis response in low income countries*, Eurodad & Third World Network report in cooperation with the Heinrich Böll Foundation, April 2010

**development** as outlined in the White Paper on Irish Aid.<sup>10</sup> This is because country-led, anti-poverty strategies are fundamentally weakened by the application of IMF economic policy conditionality.

- **Ireland's support for total debt cancellation for the poorest countries** as the IMF focuses on ensuring debt repayments through its policy conditions, and further conditional credit to developing countries as the primary solution to the financial crisis.

## 1. The IMF: Damaging Developing Country Economies

### *A Disastrous History*

The IMF has caused serious damage to the lives of people in developing countries. This is due to its application of stringent macroeconomic policies without due consideration of their impacts in impoverished contexts. IMF economic policy conditions have followed a clear pattern of market liberalisation, privatisation, capping public expenditure, and strict monetary policies, such as keeping inflation in low single digits, irrespective of whether these are appropriate policy actions in the context of impoverished and vulnerable states.<sup>11</sup> These kinds of policies have been described by UN economist Jeffery Sachs (a previous advocate of policy conditionality) as, ‘.. *belt tightening for people who cannot afford belts*’.<sup>12</sup>

### *Ruining Livelihoods and Education Opportunities*

Take the example of Mali, one of the poorest countries in the world where 90% of the population live on less than US\$ 2 per day. As part of its lending conditions, the IMF promoted the privatisation of the electricity sector and the liberalisation and privatisation of the cotton sector. Oxfam International and Malian civil society organisations highlight that the devastating results of these conditions included:

- Dramatic price increases in electricity costs (making Malian electricity the most expensive in the region) with limited additional coverage. The few Malians who had been able to access electricity in the first place (for example teachers in urban areas) either had to stop using electricity or were forced to reduce other basic consumptions to meet the price increases;

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<sup>10</sup> Government of Ireland, *White Paper on Irish Aid*, 2006, p.9

<sup>11</sup> See: Centre for Economic and Policy Research, *The Scorecard on Globalisation 1980-2000: 20 Years of Diminished Progress*, CEPR, 2001; Jubilee Debt Campaign (UK), “*Cut the Strings: Why the UK government must take action now on the harmful conditions attached to debt cancellation*,” London, October 2006; Jubilee USA, *Are IMF and World Bank Economic Policy Conditions undermining the Impact of Debt Cancellation?*, February 2008 Briefing Note; Oxfam International, *Kicking the Habit: How the World Bank and the IMF are still addicted to attaching economic policy conditions to aid*, Briefing Paper 96, Oxfam International, November 2006; Joint NGO Briefing Note, *Blind Spot, The Continuing Failure of the World Bank and IMF to Fully Assess The Impact of their Advice on Poor People*, Sept 2007; Education for All Campaign & ActionAid International, *Contradicting Commitments, How the achievement of Education for All is Being Undermined by IMF*, Sept 2005; Action Aid International, *What Progress? A Shadow Review of World Bank Conditionality*, 2006

<sup>12</sup> Quoted in Jubilee Debt Campaign, *Cut the Strings: Why the UK government must take action now on the harmful conditions attached to debt cancellation*, 2006, p. 9

- A 20% drop in cotton price for 3 million Malian farmers as a result of liberalisation of the cotton price in a highly distorted international market due to rich-country subsidies to their cotton farmers. According to an unpublished study by the World Bank this was viewed as likely to increase poverty by 4.6 per cent across the country.
- The blocking of Official Development Assistance (ODA) to the tune of US\$ 72 million by the World Bank when the Malian government failed to privatise its cotton industry as part of World Bank and IMF policy conditions. Oxfam estimated that this money could have been used to pay the salaries of 5,000 teachers for the next ten years, in a country where only 17 per cent of women between 15 and 24 are literate.<sup>13</sup>

It is not surprising that in response to these disastrous outcomes in 2005, President Amadou Toumani Touré of the Republic of Mali noted at an opening speech of a development cooperation forum in Washington:

*‘True partnership supposes autonomy of beneficiary countries in requesting aid and in determining its objectives... Often programmes are imposed on us, and we are told it is our programme... People who have never seen cotton come to give us lessons on cotton... No one can respect the conditionalities of certain donors. They are so complicated that they themselves have difficulty getting us to understand them. This is not a partnership. This is a master relating to his student.’<sup>14</sup>*

Many social sectors key to development have been negatively impacted by IMF policy conditions. The outcomes have caused many developing countries to question the IMF’s definition of macroeconomic stability which historically has focused on ‘current account and fiscal balances consistent with low and declining debt levels, inflation in the low single digits, and rising per capita GDP’.<sup>15</sup> ActionAid and the Education For All Campaign show how tight macroeconomic policies promoted uniformly by the IMF across different countries - despite unique and specific challenges in each country - have prevented many Low and Middle Income developing countries from investing in education.<sup>16</sup> They highlight how the IMF has made it ‘difficult or impossible to provide education for all citizens. Many [governments] are therefore unable to meet their obligation to fulfill the fundamental right of free, basic education for all children, despite their commitment to do so in international agreements such as the Millennium Development Goals and under their own constitutions.’<sup>17</sup> Their report highlights the real life impact of this on children’s education including:

- a 2004 ban on hiring teachers in Zambia as a result of an IMF policy condition on the public sector wage bill, at a time when Zambia was highly indebted (with the IMF as one of their major creditors). This meant leaving thousands

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<sup>13</sup> Oxfam International, op cit, 2006, p.3

<sup>14</sup> ibid, p.3

<sup>15</sup> ‘Macroeconomic Policy and Poverty Reduction’, PRSP Sourcebook Ch.6, International Monetary Fund, April 2001 <http://www.imf.org/external/np/prsp/source/2001/eng/chap6.pdf>

<sup>16</sup> Education for All et al, op cit, 2005

<sup>17</sup> ibid p.4

of teachers unemployed and a pupil–teacher ratio in Zambia of 100 to 1 in some schools. Conservative estimates at the time suggested that a further 6,000-7,000 teachers are needed if a basic desired student–teacher ratio of 40-1 was to be achieved;

- The privatization of 20% of pre-primary and primary school education in Guatemala as a policy condition to reduce the fiscal deficit resulting in low quality education due to an inappropriately reduced role for the state, high transfer of costs to local communities and poor quality of teaching due to the use of unprofessional teachers;
- A knock-on effect of hiring cheaper, unqualified teachers in developing countries that are struggling to keep public sector wage bills low as part of IMF programmes. The result in India, for example, is the employment of up to 500,000 ‘parateachers’ around the country which has entrenched a parallel labour market where children have access to different qualities of education depending on where they live. In some West African countries, qualified teachers are shockingly estimated to comprise less than 30% of the teaching population;
- A lack of resources to support free education in Kenya resulting in only half of children who register finishing primary school and out of that number only half accessing secondary education. This is largely due to fiscal and monetary pressures resulting from IMF policy conditions, which in 2005 included keeping inflation below 5%; downsizing the civil service by 15% and freezing employment of teachers; liberalising key industries such as tea and coffee; privatizing telecommunications and power generation; and keeping the fiscal deficit below 1.5% of GDP.<sup>18</sup>

After nearly 20 years of satisfying IMF demands on inflation in 2002, finance ministers of the Highly Indebted Poor Countries (HIPC)s declared their desire to see ‘*more flexible growth-oriented macro-economic frameworks...to think more closely about ways to increase growth and employment rather than further reducing inflation*’.<sup>19</sup> Unfortunately this freedom was not available to them as many dissenting developing countries, were blocked from receiving ODA flows – as per the example of Mali mentioned above. And many others had their debt cancellation processes delayed as they were declared ‘off track’ in their implementation of IMF policy conditions. These include Honduras - declared ‘off track’ when the government increased teachers’ wages when it was chosen as one of the first recipients of the ‘Education for All’ Fast Track donor initiative.<sup>20</sup> And Malawi - declared ‘off track’ when the government borrowed money from domestic banks to prevent its citizens from dying during an acute drought.<sup>21</sup> Countries such as Ethiopia continue to raise concerns about the role of the IMF in this regard.<sup>22</sup>

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<sup>18</sup> *ibid* pgs 22, 19, 24, 34

<sup>19</sup> *ibid* p.34

<sup>20</sup> *ibid*, p. 31

<sup>21</sup> <http://www.jubileedebtcampaign.org.uk/Response%20to%20the%20Liberal%20Democrats%20International%20Development%20Consultation%20Paper+5289.twl>

<sup>22</sup> Mulina, Nuria, *Bail-out or blow-out? IMF policy advice and conditions for low-income countries at a time of crisis*, Eurodad, 2009, p.5

## *Change at the IMF?*

Given the damning evidence, has the IMF changed in the face of sustained criticism and policy failures? Most up-to-date research on the IMF in Middle Income and Low Income countries shows that while it may have become more flexible in the short term, especially with Middle Income Countries, this flexibility has had a short life-span and is virtually non-existent for Low Income Countries.<sup>23</sup> Recent IMF communications have acknowledged that the recent period '*lulled macroeconomists and policymakers alike into the belief that we knew how to conduct macroeconomic policy. The crisis clearly forces us to question that assessment.*'<sup>24</sup> The IMF acknowledges that it has focused too narrowly on inflation and debt sustainability. But it does not fundamentally address the damage done to developing economies by the full set of stringent fiscal and monetary policies it promoted.

In practical terms, the IMF has introduced a number of changes in an attempt to demonstrate new flexibility. However, these changes do not go nearly far enough. For example, the new IMF Flexible Credit Line (FCL), which provides precautionary credit with very low levels of conditionality, is only available to countries the IMF calls 'strong performers' (meaning Middle Income Countries with approved IMF policies). The IMF also recently reformed some features of the Exogenous Shocks Facility (ESF) to ease Low Income Countries' access to IMF resources in the event of external shocks. However, the ESF still remains too expensive for Low Income Countries to access. In March 2009, the IMF phased out Structural Performance Criteria, one type of condition attached to their loans. Although overdue, this leaves unchanged other macroeconomic policy conditions.<sup>25</sup>

## *IMF policy conditions at a time of crisis: It's Business as Usual*

Newly published research examining the impact of the IMF on Low Income Countries since the current financial crisis, demonstrates that any marginal shifts away from strict policy conditionality were reversed in 2009 - 2010.<sup>26</sup> The research demonstrates that the IMF's macroeconomic policy design shows the usual short-term and deflationary set of policy priorities that constrain countercyclical and development policies.<sup>27</sup> Despite IMF claims that it has allowed borrowers greater policy space, in reality, fiscal deficit targets were increased by less than 2.5% of GDP in 7 of the 13 Low Income Countries recently examined. While this increase provides greater policy space compared to previous IMF targets, they represent marginal adjustments to initially restrictive recommendations while the underlying short-term

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<sup>23</sup> Van Waeyenberge, Elisa, Bargawi, Hannah and McKinley, Terry, *Standing in the way of development? A critical survey of the IMF's crisis response in low income countries*, Eurodad & Third World Network report in cooperation with the Heinrich Böll Foundation, April 2010 ; Mulina, Nuria, *Bail-out or blow-out? IMF policy advice and conditions for low-income countries at a time of crisis*, Eurodad, 2009, p.5

<sup>24</sup> Olivier Blanchard, Olivier, Dell'Ariccia, G, Mauro, P, *Rethinking Macroeconomic Policy*, IMF Staff Note, February 12, 2010, p. 1

<sup>25</sup> Molina, Nuria, *IMF emergency loans for low-income countries*, G24 Briefing, July 2009, p.1

<sup>26</sup> Van Waeyenberge et al, op cit 2010

<sup>27</sup> *ibid*, p.9

approach remains in tact. The majority of countries in the study sample are facing tighter fiscal constraints in 2010 than in 2009.<sup>28</sup>

The report highlights that the IMF's programmes continue to be premised on an excessive preoccupation with monetary and financial indicators such as fiscal balances, price stability and inflation, low interest rates, and high international reserve levels. The report highlights that this focus is to the detriment of the '*performance of real variables- real levels of output, income and employment*'<sup>29</sup> and that the IMF is more preoccupied with a developing country's capacity to service external debt over the urgent need for debt cancellation and investments in public spending.<sup>30</sup> The research finds that monetary policy was tightened across most Low Income Countries with IMF programmes, exchange rate flexibility and price liberalisation were encouraged, while protectionist measures such as tariffs and quantitative restrictions on imports were discouraged. As the Bretton Woods Project highlights, '*ironically, the stimulus programmes of developed countries have entailed many of the exact policies which the IMF has discouraged in developing countries — such as significant investments in large public employment, protectionist trade policies, conscious management of the exchange rate, and subsidies for local industries*'.<sup>31</sup>

The research also demonstrates that the IMF promotes the superiority of domestic private sectors over public sectors in stimulating domestic economic recovery. This seriously limits the ability of Low Income Countries to undertake policies that could create employment, invest in public services, adopt broader social policies, and support growth and development strategies to diversify the economy and enhance its resilience to external shocks. The dangers of this approach at this time are reinforced by another recent report by a coalition of US women's and justice organisations on the importance of countercyclical policies for development. The report highlights the need to examine the impact of government responses to the economic crisis in developing countries on human rights. The authors note that, "*the lack of countercyclical policies in times of crisis often risks jeopardising hard-fought gains in housing, education, health, water and employment.*"<sup>32</sup>

## **2. Ireland's Relationship with developing countries - The need to support developing country sovereignty, debt cancellation, tax justice and grant based finance**

In April 2009 before the G20 meeting, UN Secretary General Ban Ki-moon warned G20 leaders that "*at least \$1 trillion is needed to help developing countries get through the global financial crisis*".<sup>33</sup> This will require that richer countries mobilise additional resources to help countries bridge the giant financing gaps they face and that developing countries are allowed to implement policies that allow them to boost

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<sup>28</sup> *ibid*, p.5-6

<sup>29</sup> *ibid*, p.14

<sup>30</sup> *ibid*, p.15

<sup>31</sup> <http://www.brettonwoodsproject.org/art-566168>

<sup>32</sup> Center of Concern et al, *Bringing human rights to bear in times of crisis, A Human Rights Analysis of Government Responses to the Financial Crisis*, March 2010, p.5

<sup>33</sup> <http://www.un.org/apps/news/story.asp?NewsID=30305>

their economies.

Ireland has committed to a set of key principles in support of developing countries. These include partnership and coherence in development, a commitment to the provision of grant-based finance to the poorest countries in the world<sup>34</sup> and support for total debt cancellation for the poorest countries.<sup>35</sup> Therefore, in the limited instances when Ireland provides loan-based finance through multi-lateral institutions, it bears a very serious responsibility to ensure that the outcomes significantly improve peoples' lives in developing countries. Despite bearing this responsibility, the Irish government has not responded to the significant evidence available of the damage caused to developing countries as a result of IMF policy conditions.<sup>36</sup> In addition, given the high emphasis by the IMF on lending as a solution to the crisis, Ireland has not outlined a clear position on the implications of this massively scaled up credit in the context of low levels of availability of other forms of more independent finance. DDCI is especially concerned about the area of global tax injustice. Tax revenue is the most independent and sustainable source of development finance for developing countries. Yet tax evasion by multi-national corporations costs developing countries at least US\$ 160 billion per year in lost income. The human impact of these losses is disastrous as ending such illicit capital flight could save the lives of 350,000 children under the age of 5 each year, based on present health spending patterns in impoverished countries.<sup>37</sup>

#### *Recommendations to the Irish Government*

**The Irish government should use the opportunity of engaging with the IMF on its resource needs to ensure greater economic justice for developing countries. The Irish government should not approve the loan facility to the IMF in its current form. The loan should be extended based on strong commitments from the IMF to:**

- Discontinue its practice of attaching economic policy conditions to its loans;
- Reform its governance structure to include far greater voice and vote for developing countries (for example through introducing a double majority voting system),<sup>38</sup>
- Recognise the need for debt cancellation for all developing countries that need it based on human rights measurement criteria, and the need to tackle illegitimate debts;

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<sup>34</sup> Government of Ireland, op cit 2006 p.9 & p.85

<sup>35</sup> Government of Ireland, *Policy on Developing Country Debt*, 19 July 2002

<sup>36</sup> Currently, Ireland has no clear position on policy conditionality at the international financial institutions. A new position may be outlined in Ireland's current work on revising the '*Policy on Developing Country Debt*' (2002).

<sup>37</sup> Christian Aid, *Death and Taxes, The True Toll of Tax Dodging*, Christian Aid, 2008

<sup>38</sup> Chowla, Peter, *Bridging the democratic deficit, Double majority decision making and the IMF*, Bretton Woods project, Feb 2007, p. 1

- Restrict future IMF lending to developing countries to short term needs, such as balance of payments shocks, and discontinue long term lending given the IMF's lack of mandate and expertise in the area of long term development and poverty eradication.

**In addition, the Irish government should:**

- Provide strong support to developing countries to access policy advice from a wide range of sources which could include UN agencies, regional or national think tanks and academia in the Global South;
- Delink bilateral ODA allocations to the existence and status of IMF programmes;
- Support Irish Aid funded research into alternative macro-economic policy designs in developing countries;
- Promote the mobilisation of domestic taxation in developing countries to ensure greater access to debt-free finance through supporting country-by-country financial reporting on taxation by multi-national companies and automatic information exchange between jurisdictions on taxation.

**Key Sources**

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*Debt and Development Coalition Ireland is a national network focusing on challenging Ireland's role in any exploitation of Southern countries by Northern countries and Northern dominated institutions through unjust flows of resources between the South and the North; and particularly through injustice in the international lending system. [www.debtireland.org](http://www.debtireland.org)*

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