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**DIRECTORATE-GENERAL INTERNAL POLICIES OF THE UNION
- DIRECTORATE A -
ECONOMIC AND SCIENTIFIC POLICIES**

Workshop

International Monetary Fund (IMF)

7 December 2005
European Parliament, Brussels

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Responsible Administrator:

BAHR, Christine
Policy Department Economy and Science
DG Internal Policies
European Parliament
Rue Wiertz 60 - ATR 00L044
B-1047 Brussels
Tel: +32 (0)2 284 07 22
Fax: +32(0)2 284 90 02
E-mail: christine.bahr@europarl.europa.eu

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**DIRECTORATE-GENERAL INTERNAL POLICIES OF THE UNION
- DIRECTORATE A -
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**Workshop on the IMF
*Programme***

7 December 2005
European Parliament Brussels
9.00h – 17.30h

9.00 - 10.45 Session 1

Coordination of EU Member States in their representation to the IMF and the World Bank

- Why is there a perceived need for change? – Deficiencies of current representation
- What possibilities are there for better coordination? – In-depth discussion of pros and cons of each possibility:
 - Single seat
 - Grouping of EU-countries, one constituency for all EU Member States? Grouping of EU Member States in constituencies with non-EU Member States?
 - Eurozone versus EU involvement?
 - Representation of smaller and bigger Member States – do smaller and bigger Member States that are now grouped in different constituencies influence if a single seat or a different grouping system would apply?
 - Does more influence for the EU mean less influence for some Member States? What influence can individual Member States have at all in today's economic world?
 - Coordination of EU Member States prior to G7? How does it work at present, what could be changed?
 - Representation of EU common interest: Who can best do this? Commission, ECB?
 - Could the EP be represented at preparatory meetings of the EU representatives similarly to its representation in the WTO delegations?

Guest speakers: Daniel Daco (European Commission Working Group on the IMF), Dennis Leech (Warwick University), Isabella Lindner (Austrian National Bank)

11.00 - 13.00

Session 2

Democratic Accountability of the IMF

- Role of the EP in democratic accountability – How can the EP play a role?
- Could the EP be involved in coordination meetings, at least before the big annual meetings (Spring meeting and Autumn meetings)?
- Could the EP ask the European Presidency to answer questions on EU coordination and priorities of the EU or Eurozone with regard to the IMF and possibly also G7 and the World Bank?
- Should Parliament invite the European executive directors of the IMF to explain their activities and the IMF's policy and priorities?
- How is the IMF held responsible by other Parliaments? (EU Member States national parliaments, Switzerland, US)
- What influence does Congress have? If this is an issue, how can it be addressed?
- Accountability towards donor nations and receiving nations – what is the difference, how should it be developed?
- Does the IMF take into account sovereign decisions of national parliaments on economic policy when negotiating with national governments?
- Could there be an international coordination role for the EP in assuring democratic accountability both in donor and recipient countries? Which body (committee, plenary, ad-hoc committee or World Bank and IMF Parliamentary Network) should be taking care of this?
- What areas of IMF work should be falling under democratic accountability vis-à-vis the EP?

Guest speaker: Charles Wyplosz (Graduate Institute of International Studies, Geneva)

15.00 - 17.30

Session 3

Tasks, mission and effectiveness of the IMF in today's global economy and division of tasks and cooperation with other international institutions

- Are the tasks and the founding philosophy of the IMF still valid half a century after its foundation? Is the Washington consensus dead? – To be evaluated in connection with recent developments (debt relief, Millennium goals)
- What is the content of IMF policy and how are the policies implemented?
- Is the institutional division of task between the IMF and other international bodies efficient?
- Were past interventions by the IMF efficient and effective? (Examples of perceived successes and failures)
- How to learn from past negative experiences such as the "One size fits all recipes" of the IMF?

Guest speakers: Jean Pisani-Ferry (Bruegel, Brussels), Kunibert Raffer (Vienna University), Charles Wyplosz (Graduate Institute of International Studies, Geneva)

Curricula Vitae

Dennis Leech

Dennis Leech is a Senior Lecturer in Economics and Director of Studies for the MSc in Economics at Warwick. His research interests focus on the governance of international economic institutions, such as the IMF/ World Bank and the EU Council of Ministers, which employ weighted voting systems, and the associated questions surrounding distribution of power. His work is both applied and methodological, centring on formal methods of analysing voting power deriving from co-operative game theory. He believes there are currently real possibilities for furthering this area of research in international relations which can lead to the development of normative rules which could be applied, for example to the allocation of votes to countries in the expanding EU. He is also actively working on corporate governance where he has previously done pioneering work on the analysis of shareholder voting power and control of the corporation, as well as aspects of empirical game theory. His work has been published in a range of journals including the Economic Journal, Econometrica, Public Choice, Management Science, European Journal of Political Research and other economics journals.

More detailed description of Prof Leech's research interest by himself:

Current research is mainly in the following areas. Voting power analysis, with special reference to better understanding weighted voting systems through the use of power indices. This is an emerging field. I have made substantial original contributions to the field both in methodology and in application. I have analysed voting power in international organisations which use weighted voting systems, particularly the IMF and the European Union council of Ministers. Share ownership and corporate governance. I have studied voting power of shareholder blocs and shown that many large companies are effectively controlled by a small number of shareholders, holding a minority of voting shares, voting as a bloc. I have also recently, studied the incentives of many leading investors to be active in corporate governance by voting their shares and in other ways. The research suggests that shareholders can make substantial net gains from improvements in the performance of their portfolio companies even when their holdings represent only a small fraction of the equity, in contrast to the conventional view.

Charles Wyplosz

Charles Wyplosz is Professor of International Economics at the Graduate Institute of International Studies in Geneva where he is Director of the International Centre for Money and Banking Studies. Previously, he served as Associate Dean for Research and Development at INSEAD and Director of the PhD program in Economics at the Ecole des Hautes Etudes en Science Sociales in Paris. He also has been Director of the International Macroeconomics Program of CEPR, the leading European network of economists.

His main research areas include financial crises, European monetary integration, fiscal policy, economic transition and current regional integration in various parts of the world. He is the co-author of a leading textbook on Macroeconomics and of a textbook on European economic integration. He was a founding Managing Editor of the review Economic Policy. He serves on several boards of professional reviews and European research centers.

He is a regular columnist in such newspapers as the Financial Time, Le Monde, Liberation, Le Temps, Finanz und Wirtschaft, and Handelsblatt. Currently a member of the "Conseil d'Analyse Economique" which reports to the Prime Minister of France, of the Group of Independent Economic Advisors to the President of the European Commission President, of the Panel of Experts of the European Parliament's Economic and Monetary Affairs Committee and of the "Bellagio Group", Charles Wyplosz is an occasional consultant to the European Commission, the IMF, the World Bank, the United Nations, the Asian Development Bank, and the Inter-American Development Bank. He has been a member of the French Finance Minister's "Commission des Comptes de la Nation" and has advised the government of the Russian Federation. Charles Wyplosz holds degrees in Engineering and Statistics from Paris and a PhD in Economics from Harvard University.

Kunibert Raffer

Associate Professor at the Department of Economics of the University of Vienna
1979-80 and 1983-84 consultant to UNIDO

1986-89 visiting lecturer and visiting professor, University of Klagenfurt

1989 Visiting Fellow of the Institute of Development Studies (IDS) at the University of Sussex [academic sponsor: Sir Hans (H.W.) Singer]

1990-93 Honorary Research Fellow, Department of Commerce, University of Birmingham (UK)

1998 participation in the UNDP's research project "International Development Cooperation and Global Public Goods"

Since 2002 Senior Associate of the New Economics Foundation, London (Think Tank of the Year 2002)

Winter Term 2002-03 Visiting Professor at the Centre for the Study of International Institutions (CSI), SOWI Faculty, University of Innsbruck

Present Research Interests:

International Trade, International Finance & Debts, Aid

More Detailed Description of Prof Raffer's Main Present Research Focus by himself: Sovereign Insolvency

Soon after August 1982 - which is traditionally considered the date when the debt crisis of the South started - the idea was advocated to use domestic insolvency as a model how to solve this problem. While economically feasible, however, international reorganisation pursuant to Chapter 11 of US Title 11 (Bankruptcy) or similar laws in other countries fails to address the important problem of sovereignty. As insolvency procedures for firms do, of course, not tackle the problem of governmental powers, it was rightly argued from a legalistic point of view that it cannot be applied to sovereign debtors. This argument is right as far as it goes, although emulating insolvency - as already suggested by Adam Smith - is economically feasible and indicated. In 1987 I therefore proposed to internationalise the basic features of the US Chapter 9. Designed and used for decades in the US to solve debt problems of municipalities, debtors vested with governmental powers, its essential points can be applied to sovereign borrowers immediately and without problems. In 2001 the IMF's proposal of a model of sovereign insolvency - the so-called Sovereign Debt Restructuring Mechanism (SDRM) - stimulated discussion on sovereign insolvency, not least by breaking the taboo of considering insolvency for overindebted countries at the IMF. Unfortunately it is not going to work. Totally shaped by the IMF's narrow institutional self-interest it is simply a continuation of unsuccessful debt management since 1982. Strong reservations are therefore heard from creditors, including the US Treasury, debtors and NGOs. My most recent work thus focuses on showing why the SDRM - in marked contrast to my proposal - is unlikely to work.

Slides

**Presentation by
Dennis Leech**

Voting Power Implications of a Single European Seat at the IMF

Presentation prepared by Dennis Leech for:

Workshop on Strategic Review of the IMF
European Parliament
7th December 2005

A Single European Seat in IMF:Votes

- European Countries' votes in the IMF:
EU 31.9%, Eurozone 22.9%. Compare USA 17.1%.
- So a single EU seat without quota changes would be dominant.
- Too large relative to share of world GDP:
EU 31.1%, Eurozone 22.9%, USA 29.3%.
- European quota would have to be reduced.
- But introduction of bloc vote increases voting power.

Bloc Vote plus Reduced Voting Weight

- Complex Effects:
 1. Vote redistribution to all other countries
 2. New large bloc comparable to USA will reduce US voting power and increase powers of all other members more than in 1. above
 3. EU members indirectly represented through bloc may have more or less voting power
- Need to use voting power analysis.

Voting Power Analysis

- Voting **Weight** is not Voting **Power** in systems of Weighted Voting.
- Voting Weights are *Inputs* to decision making = Number of Votes each member possesses.
- Voting Power: Capacity to influence decisions taken by majority voting, to “swing” the vote.

Power Indices

- A Power Index is equal to the **No. of Swings** divided by the **No. of possible swings**
(Penrose Index)
- Power shares: powers of all member countries add up to 100%
(Banzhaf Index)
- No assumptions about voting *behaviour*.
Constitutional power only: Voting *modalities* only not *behaviour*.
- Depends on the Decision Threshold and the Weights of all members. Analysis of voting rule.

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Scenarios for Analysis

- The Status Quo. USA 17.1%. Separate European seats.
- Single European seat, EU bloc and USA have the same weight = 371,743 votes. Analyses for both EU25 and Euro12.
- Also analyses for a **range** of number of votes for EU bloc: 140,000-500,000

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Specific Analyses and Questions

1. Analysis of IMF Governors as a Voting Body:
Comparison with the Status Quo.
How would a single European seat affect powers of other members?
2. Analysis of Powers of Individual European Countries Indirectly as Member of the European Bloc in the IMF Governors: Two Level Decision Making.
Are there power incentives to joining the European Bloc?

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Results for Analysis 1.

1. In the Status Quo the USA has more power than weight. Its share of voting power 24.5%. Powers of all other countries less than weight.
2. A European Bloc would increase the voting powers of all non-members exc. the USA.
3. A European Bloc with equal votes to USA would give all non-members exc. USA more power than weight.
4. Power of non-European or US members maximised when two blocs are equal.
5. Both large blocs have veto power over 85% majority decisions.

Assumptions about the Voting System in the European Bloc: Euro12 Case

1. IMF Current weights: the Euro12 uses weighted majority voting based on the actual current weights determined by the IMF quotas;
2. GDP weights: a system of weighted voting based on the economic size of each country;
3. Population weights: a voting system based on population as an alternative measure of a country's size;
4. One Country One Vote: all members have an equal voice; this is the basis on which the European Central Bank currently works.

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Assumptions about the Voting System in the European Bloc: EU25 Case

1. IMF Current Weights.
2. Nice: the system of Qualified Majority Voting in the Nice Treaty currently in use in the Council of Ministers.
3. Draft Constitution to replace the Nice system.
4. GDP Weights.
5. Population with a simple majority decision rule.
Both Nice and the Draft Constitution systems based on populations but require supermajorities, which means low power to act and low absolute voting power of members.
6. Population Square Roots: more equitable basis for EU voting weights. Penrose square root rule.
7. One Country One Vote.

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Results for Analysis 2.

1. Each European bloc member *could* gain (indirect) voting power from the formation of the bloc.
2. Weighted voting based on current IMF weights would give every member greater power as a member of the more powerful bloc than at present.
3. All other weighted voting schemes would benefit some but not all member countries of the bloc.

Conclusions: Possible Beneficial Effects of a Single European IMF Seat

- Powers of **all** non-European members except USA increase due to 2 effects:
 1. Reduction in European weight increases all countries' voting shares
 2. Parity of European Bloc and USA creates a bipolar situation with 2 large blocs - Voting Power Analysis
- Powers of **all** members of European bloc **can** increase compared to the status quo.

Results

Computed Power Indices

Table 1: Voting Power Analysis of the IME with a Single European Seat with Voting Parity with the USA

	Status Quo				Euro12/US Parity						EU25/US Parity					
	Votes	%	Power Indices Abs	Rel	votes	%	Power Indices Abs	Rel	Abs	Rel	votes	%	Power Indices Abs	Rel	Abs	Rel
United States	371743	17.09	0.755917	24.49	371743	18.15	0.499745	16.06	0.66	0.66	371743	20.06	0.499991	16.71	0.66	0.68
Euro12					371743	18.15	0.499745	16.06								
EU25											371743	20.06	0.499991	16.71		
Japan	133378	6.13	0.168548	5.46	133378	6.51	0.238587	7.67	1.42	1.40	133378	7.20	0.281973	9.42	1.67	1.73
Germany	130332	5.99	0.165113	5.35												
France	107635	4.95	0.138111	4.47												
United Kingdom	107635	4.95	0.138111	4.47	107635	5.25	0.18028	5.79	1.31	1.29						
Italy	70805	3.25	0.091691	2.97												
Saudi Arabia	70105	3.22	0.090793	2.94	70105	3.42	0.113549	3.65	1.25	1.24	70105	3.78	0.124767	4.17	1.37	1.42
China	63942	2.94	0.082879	2.69	63942	3.12	0.103089	3.31	1.24	1.23	63942	3.45	0.113424	3.79	1.37	1.41
Canada	63942	2.94	0.082879	2.69	63942	3.12	0.103089	3.31	1.24	1.23	63942	3.45	0.113424	3.79	1.37	1.41
Russian Federation	59704	2.74	0.077423	2.51	59704	2.91	0.09599	3.09	1.24	1.23	59704	3.22	0.105656	3.53	1.36	1.41
Netherlands	51874	2.38	0.067321	2.18												
Belgium	46302	2.13	0.060117	1.95												
India	41832	1.92	0.054331	1.76	41832	2.04	0.066669	2.14	1.23	1.22	41832	2.26	0.073370	2.45	1.35	1.39
Switzerland	34835	1.60	0.045262	1.47	34835	1.70	0.055381	1.78	1.22	1.21	34835	1.88	0.060935	2.04	1.35	1.39
Australia	32614	1.50	0.042381	1.37	32614	1.59	0.051811	1.67	1.22	1.21	32614	1.76	0.057008	1.91	1.35	1.39
Spain	30739	1.41	0.039949	1.29												
Brazil	30611	1.41	0.039782	1.29	30611	1.49	0.048602	1.56	1.22	1.21	30611	1.65	0.053473	1.79	1.34	1.39
Venezuela	26841	1.23	0.034868	1.13	26841	1.31	0.042577	1.37	1.22	1.21	26841	1.45	0.048837	1.57	1.34	1.38
Mexico	26108	1.20	0.033936	1.10	26108	1.27	0.041407	1.33	1.22	1.21	26108	1.41	0.045549	1.52	1.34	1.38
Sweden	24205	1.11	0.031465	1.02	24205	1.18	0.038373	1.23	1.22	1.21						
Argentina	21421	0.98	0.027848	0.90	21421	1.05	0.033941	1.09	1.22	1.21	21421	1.16	0.037331	1.25	1.34	1.38
Indonesia	21043	0.97	0.027357	0.89	21043	1.03	0.03334	1.07	1.22	1.21	21043	1.14	0.036669	1.23	1.34	1.38
Austria	18973	0.87	0.024667	0.80												
South Africa	18935	0.87	0.024618	0.80	18935	0.92	0.029989	0.96	1.22	1.21	18935	1.02	0.032962	1.10	1.34	1.38
Nigeria	17782	0.82	0.02312	0.75	17782	0.87	0.028158	0.91	1.22	1.21	17782	0.96	0.030967	1.04	1.34	1.38
Norway	16967	0.78	0.022061	0.71	16967	0.83	0.028864	0.86	1.22	1.21	16967	0.92	0.029544	0.99	1.34	1.38
Denmark	16678	0.77	0.021885	0.70	16678	0.81	0.026405	0.85	1.22	1.21						
Korea	16586	0.76	0.021565	0.70	16586	0.81	0.026259	0.84	1.22	1.21	16586	0.89	0.028879	0.97	1.34	1.38
Iran	15222	0.70	0.019792	0.64	15222	0.74	0.024095	0.77	1.22	1.21	15222	0.82	0.026498	0.89	1.34	1.38
Malaysia	15116	0.69	0.019655	0.64	15116	0.74	0.023927	0.77	1.22	1.21	15116	0.82	0.026313	0.88	1.34	1.38
Kuwait	14061	0.65	0.018283	0.59	14061	0.69	0.022254	0.72	1.22	1.21	14061	0.76	0.024473	0.82	1.34	1.38
Ukraine	13970	0.64	0.018165	0.59	13970	0.68	0.02211	0.71	1.22	1.21	13970	0.75	0.024314	0.81	1.34	1.38
Poland	13940	0.64	0.018126	0.59	13940	0.68	0.022062	0.71	1.22	1.21						
Finland	12888	0.59	0.016758	0.54												
Algeria	12797	0.59	0.01664	0.54	12797	0.62	0.020251	0.65	1.22	1.21	12797	0.69	0.022269	0.74	1.34	1.38
Iraq	12134	0.56	0.015778	0.51	12134	0.59	0.0192	0.62	1.22	1.21	12134	0.65	0.021114	0.71	1.34	1.38
Libya	11487	0.53	0.014937	0.48	11487	0.56	0.018175	0.58	1.22	1.21	11487	0.62	0.019986	0.67	1.34	1.38
Thailand	11069	0.51	0.014394	0.47	11069	0.54	0.017513	0.56	1.22	1.21	11069	0.60	0.019298	0.64	1.34	1.38

Both absolute and relative power indices are given (Penrose and Banzhaf indices). Ratios for both allow before and after comparisons. Calculations have been done using the program *ipmlic* in Leech and Leech (2005). Workshop on the IMF

Table 2: Voting Power Comparison for the Euro12 Member Countries Assuming Euro12/USA Voting Parity

	Status Quo			Current IMF Weights			GDP Weights			Population Basis			Equality					
	Votes	%	power	Weight%	power	2-stage ratio	power	2-stage ratio	power	2-stage ratio	power	2-stage ratio	power	2-stage ratio				
Germany	130332	5.99	0.1650	26.14	0.5723	0.2860	1.73	29.37	0.6201	0.3099	1.88	26.97	0.6162	0.3079	1.87	0.2256	0.1127	0.58
France	107635	4.95	0.1381	21.59	0.4160	0.2079	1.51	21.38	0.3799	0.1898	1.38	19.51	0.3565	0.1781	1.29	0.2256	0.1127	0.82
Italy	70805	3.25	0.0917	14.20	0.2949	0.1474	1.61	17.93	0.3604	0.1801	1.96	18.83	0.3486	0.1742	1.90	0.2256	0.1127	1.23
Netherlands	51874	2.38	0.0673	10.40	0.1904	0.0952	1.41	6.26	0.0889	0.0444	0.66	5.30	0.0986	0.0493	0.73	0.2256	0.1127	1.67
Belgium	46302	2.13	0.0601	9.29	0.1709	0.0854	1.42	3.70	0.0518	0.0259	0.43	3.38	0.0635	0.0317	0.53	0.2256	0.1127	1.88
Spain	30739	1.41	0.0399	6.16	0.1006	0.0503	1.26	10.23	0.1357	0.0678	1.70	13.43	0.1787	0.0893	2.24	0.2256	0.1127	2.82
Austria	18973	0.87	0.0247	3.81	0.0703	0.0351	1.42	3.08	0.0518	0.0259	1.05	2.63	0.0420	0.0210	0.85	0.2256	0.1127	4.57
Finland	12858	0.59	0.0168	2.58	0.0518	0.0259	1.54	1.98	0.0264	0.0132	0.79	1.70	0.0361	0.0181	1.09	0.2256	0.1127	6.73
Portugal	8924	0.41	0.0116	1.79	0.0332	0.0166	1.43	1.83	0.0264	0.0132	1.14	3.33	0.0596	0.0298	2.57	0.2256	0.1127	8.72
Ireland	8634	0.40	0.0112	1.73	0.0313	0.0156	1.38	1.82	0.0264	0.0132	1.17	1.29	0.0263	0.0142	1.26	0.2256	0.1127	10.04
Greece	8480	0.39	0.0110	1.70	0.0313	0.0156	1.42	2.12	0.0303	0.0151	1.37	3.49	0.0635	0.0317	2.88	0.2256	0.1127	10.23
Luxembourg	3041	0.14	0.0040	0.61	0.0117	0.0059	1.48	0.32	0.0029	0.0015	0.37	0.15	0.0029	0.0015	0.37	0.2256	0.1127	28.52
TOTAL	498627	22.92		100.00				100.00				100.00						

Analysis assumes voting parity between the USA and Euro12. The power index for Euro12 is 0.499745. The power indices are the Penrose indices. Status quo refers to the present IMF. Two stage is the two-stage Penrose index: the product of the power index in the Euro12 with the power of the Euro12 bloc in the IMF governors (0.499745). The Status Quo is the current IMF board of governors. The ratio is the ratio of the power index to the status quo power index of the country. GDP and population figures are for 2003. Calculations of power indices for the members of Euro12 have been done using the program *ipdirect* in Leech and Leech (2003).

Table 3: Voting Power Comparison for the EU25 Members Assuming EU25/USA Parity

	Status Quo			Current IMF weights			Nice system			Draft Constitution system					
	votes	%	power	weight%	power	2-stage ratio	weight	pop%	power	2-stage ratio	power	2-stage ratio			
Germany	130332	5.99	0.1651	18.79	0.4855	0.2428	1.47	29	18.21	0.0551	0.0275	0.17	0.158	0.0790	0.48
France	107635	4.95	0.1381	15.52	0.3803	0.1902	1.38	29	13.09	0.0551	0.0275	0.20	0.113	0.0565	0.41
United Kingdom	107635	4.95	0.1381	15.52	0.3803	0.1902	1.38	29	13.15	0.0551	0.0275	0.20	0.114	0.0570	0.41
Italy	70805	3.25	0.0917	10.21	0.2273	0.1136	1.24	29	12.79	0.0551	0.0275	0.30	0.111	0.0555	0.61
Netherlands	51874	2.38	0.0673	7.48	0.1750	0.0875	1.30	13	3.5	0.0272	0.0136	0.20	0.058	0.0290	0.43
Belgium	46302	2.13	0.0601	6.68	0.1537	0.0769	1.28	12	2.27	0.0251	0.0126	0.21	0.050	0.0250	0.42
Spain	30739	1.41	0.0399	4.43	0.1000	0.0500	1.25	27	8.75	0.0522	0.0261	0.65	0.098	0.0490	1.23
Sweden	24205	1.11	0.0315	3.49	0.0795	0.0398	1.26	10	1.97	0.0210	0.0105	0.33	0.048	0.0240	0.76
Austria	18973	0.87	0.0247	2.74	0.0622	0.0311	1.26	10	1.79	0.0210	0.0105	0.43	0.470	0.2350	9.53
Denmark	16678	0.77	0.0217	2.40	0.0546	0.0273	1.26	7	1.18	0.0148	0.0074	0.34	0.044	0.0220	1.01
Poland	13940	0.64	0.0181	2.01	0.0456	0.0228	1.26	27	8.58	0.0522	0.0261	1.44	0.083	0.0415	2.29
Finland	12888	0.59	0.0168	1.86	0.0422	0.0211	1.26	7	1.15	0.0148	0.0074	0.44	0.043	0.0215	1.28
Hungary	10634	0.49	0.0138	1.53	0.0348	0.0174	1.26	12	2.24	0.0251	0.0126	0.91	0.050	0.0250	1.81
Portugal	8924	0.41	0.0116	1.29	0.0292	0.0146	1.26	12	2.22	0.0251	0.0126	1.08	0.050	0.0250	2.15
Ireland	8634	0.40	0.0112	1.24	0.0282	0.0141	1.26	7	0.83	0.0148	0.0074	0.66	0.042	0.0210	1.87
Greece	8480	0.39	0.0110	1.22	0.0277	0.0139	1.26	12	2.34	0.0251	0.0126	1.14	0.051	0.0255	2.31
Czech Republic	8443	0.39	0.0110	1.22	0.0276	0.0138	1.26	12	2.28	0.0251	0.0126	1.14	0.050	0.0250	2.28
Slovak Republic	3825	0.18	0.0050	0.55	0.0125	0.0062	1.25	7	1.2	0.0148	0.0074	1.49	0.044	0.0220	4.42
Luxembourg	3041	0.14	0.0040	0.44	0.0099	0.0049	1.25	4	0.1	0.0085	0.0043	1.08	0.037	0.0185	4.88
Slovenia	2567	0.12	0.0033	0.37	0.0083	0.0042	1.25	4	0.44	0.0085	0.0043	1.27	0.039	0.0195	5.84
Lithuania	1692	0.08	0.0022	0.24	0.0055	0.0028	1.25	7	0.82	0.0148	0.0074	3.37	0.041	0.0205	9.32
Cyprus	1646	0.08	0.0021	0.24	0.0054	0.0027	1.25	4	0.17	0.0085	0.0043	1.99	0.038	0.0190	8.87
Latvia	1518	0.07	0.0020	0.22	0.0049	0.0025	1.25	4	0.54	0.0085	0.0043	2.16	0.040	0.0200	10.13
Malta	1270	0.06	0.0017	0.18	0.0041	0.0021	1.25	3	0.08	0.0064	0.0032	1.92	0.037	0.0185	11.20
Estonia	902	0.04	0.0012	0.13	0.0029	0.0015	1.25	4	0.32	0.0085	0.0043	3.63	0.038	0.0190	16.20
Total	693582	31.88		100.00				100.00							
IMF Total	2175345														

The analysis assumes voting parity between the USA and EU25. The power index for the EU25 is 0.499991. The power indices are the Penrose indices. Status quo refers to the present IMF. Two stage is the two-stage Penrose index: the product of the power index in the EU25 with the power of the Euro12 bloc in the IMF governors (0.499991). The Status Quo is the current IMF board of governors. The ratio is the ratio of the power index to the status quo power index of the country. GDP and population figures are for 2003. Calculations of power indices for the members of EU25 have been done using the program *ipdirect* in Leech and Leech (2003).

Table 3 (continued): Voting Power Comparison for the EU25 Members Assuming EU25/USA Parity

	GDP weights				Population weights			Population Square Root weights				Equality		
	GDP %	power	2-stage	ratio	power	2-stage	ratio	power	2-stage	ratio	power	2-stage	ratio	
Germany	21.88	0.5332	0.2666	1.61	0.4962	0.2481	1.50	4.267	0.3544	0.1772	1.07	0.1612	0.0806	0.49
France	15.93	0.3432	0.1716	1.24	0.3203	0.1602	1.16	3.62	0.2938	0.1469	1.06	0.1612	0.0806	0.58
United Kingdom	16.36	0.3548	0.1774	1.28	0.3219	0.1610	1.17	3.63	0.2945	0.1473	1.07	0.1612	0.0806	0.58
Italy	13.36	0.2652	0.1326	1.45	0.3121	0.1561	1.70	3.58	0.2900	0.1450	1.58	0.1612	0.0806	0.88
Netherlands	4.66	0.1102	0.0551	0.82	0.0820	0.0410	0.61	1.87	0.1469	0.0734	1.09	0.1612	0.0806	1.20
Belgium	2.75	0.0621	0.0310	0.52	0.0534	0.0267	0.44	1.51	0.1178	0.0589	0.98	0.1612	0.0806	1.34
Spain	7.62	0.1908	0.0954	2.39	0.2063	0.1031	2.58	2.96	0.2363	0.1181	2.96	0.1612	0.0806	2.02
Sweden	2.74	0.0618	0.0309	0.98	0.0463	0.0232	0.74	1.40	0.1096	0.0548	1.74	0.1612	0.0806	2.56
Austria	2.29	0.0516	0.0258	1.05	0.0421	0.0210	0.85	1.34	0.1045	0.0522	2.12	0.1612	0.0806	3.27
Denmark	1.94	0.0436	0.0218	1.01	0.0278	0.0139	0.64	1.09	0.0847	0.0423	1.95	0.1612	0.0806	3.72
Poland	1.91	0.0430	0.0215	1.19	0.2008	0.1004	5.54	2.93	0.2338	0.1169	6.45	0.1612	0.0806	4.45
Finland	1.47	0.0331	0.0166	0.99	0.0271	0.0135	0.81	1.07	0.0836	0.0418	2.49	0.1612	0.0806	4.81
Hungary	0.75	0.0169	0.0085	0.61	0.0527	0.0263	1.90	1.50	0.1170	0.0585	4.23	0.1612	0.0806	5.83
Portugal	1.36	0.0307	0.0153	1.32	0.0522	0.0261	2.25	1.49	0.1165	0.0582	5.02	0.1612	0.0806	6.94
Ireland	1.35	0.0305	0.0152	1.36	0.0195	0.0098	0.87	0.91	0.0709	0.0355	3.16	0.1612	0.0806	7.18
Greece	1.58	0.0355	0.0177	1.61	0.0550	0.0275	2.49	1.53	0.1196	0.0598	5.42	0.1612	0.0806	7.31
Czech Republic	0.78	0.0175	0.0087	0.80	0.0536	0.0268	2.44	1.51	0.1181	0.0590	5.38	0.1612	0.0806	7.34
Slovak Republic	0.29	0.0065	0.0032	0.65	0.0282	0.0141	2.84	1.10	0.0854	0.0427	8.58	0.1612	0.0806	16.20
Luxembourg	0.24	0.0054	0.0027	0.68	0.0024	0.0012	0.30	0.32	0.0246	0.0123	3.11	0.1612	0.0806	20.38
Slovenia	0.24	0.0054	0.0027	0.80	0.0103	0.0052	1.55	0.66	0.0516	0.0258	7.73	0.1612	0.0806	24.14
Lithuania	0.17	0.0037	0.0019	0.85	0.0193	0.0096	4.38	0.91	0.0705	0.0353	16.02	0.1612	0.0806	36.63
Cyprus	0.10	0.0023	0.0012	0.54	0.0040	0.0020	0.93	0.41	0.0320	0.0160	7.48	0.1612	0.0806	37.64
Latvia	0.09	0.0020	0.0010	0.50	0.0126	0.0063	3.19	0.73	0.0571	0.0286	14.47	0.1612	0.0806	40.82
Malta	0.04	0.0008	0.0004	0.24	0.0019	0.0009	0.58	0.28	0.0220	0.0110	6.65	0.1612	0.0806	48.78
Estonia	0.08	0.0017	0.0009	0.73	0.0075	0.0037	3.20	0.57	0.0440	0.0220	18.73	0.1612	0.0806	68.70
	2.2511				2.455			20.58						

The analysis assumes voting parity between the USA and EU25. The power index for the EU25 is 0.499991. The power indices are the Penrose indices. Status quo refers to the present IMF. Two stage is the two-stage Penrose index: the product of the power index in the EU25 with the power of the Euro12 bloc in the IMF governors (0.499991). The Status Quo is the current IMF board of governors. The ratio is the ratio of the power index to the status quo power index of the country. GDP and population figures are for 2003. Calculations of power indices for the members of EU25 have been done using the program <http://www.ecb.int/press/pr/2003/030401.htm> (2003)

Power Indices

Hypothetical and Illustrative Examples

Power Indices Example (1)

- Voting Body with: 1 member with 20 votes, 80 members with 1 vote each,
majority threshold = 51 votes
- One dominant bloc
- He has *more* power than weight
- All others have *less* power than weight

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Power Indices Example (1)

Votes	Power Index (Penrose Index)	Power Share (Banzhaf Index)	Weight Share
20	0.97	62%	20%
1	0.0073	0.47%	1%

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Power Indices Example (2)

- Voting Body with: **2** members with 20 votes each, 60 members with 1 vote each,
winning threshold = 51 votes
- A Bipolar situation: Two Independent Blocs
- Each 20-vote member has *less* power than weight
- Each other member has *more* power than weight

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Power Indices Example (2)

Votes	Power Index (Penrose Index)	Power Share (Banzhaf Index)	Weight Share
20	0.50	12%	20%
1	0.0504	1.27%	1%

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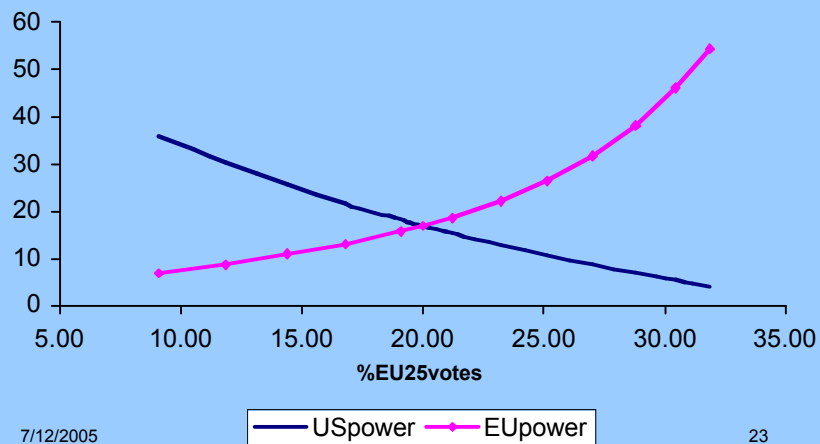
Graphs

Effects of Varying the Weight of the European Bloc between 500,000 and 140,000 votes (all other weights constant)

Power Indices for Selected IMF Members when there is a Single European Seat:
the EU25 Case

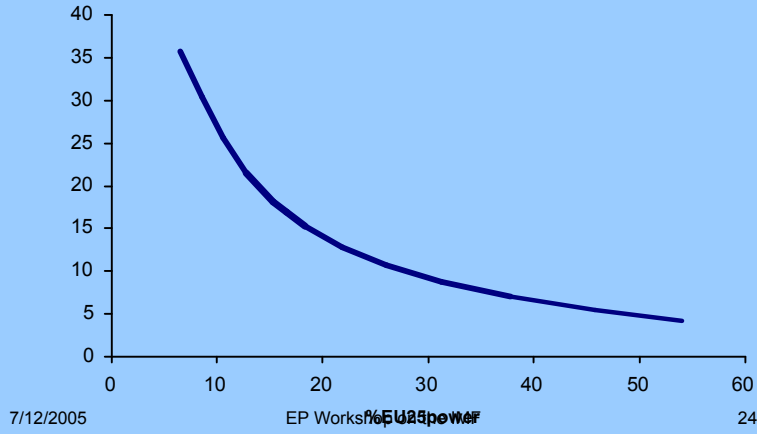
Figure 3(a) Voting Power of EU25 and USA

EU and US power



Power Indices for Selected IMF Members when there is a Single European Seat:
the EU25 Case
Figure 3(b) Voting Power Trade-off of EU25 vs US

EU - US Tradeoff



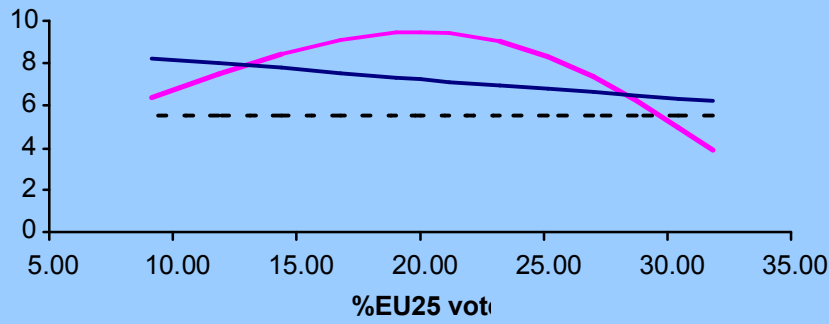
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Power Indices for Selected IMF Members when there is a Single European Seat:
the EU25 Case
Figure 3(c) Japan

Japan



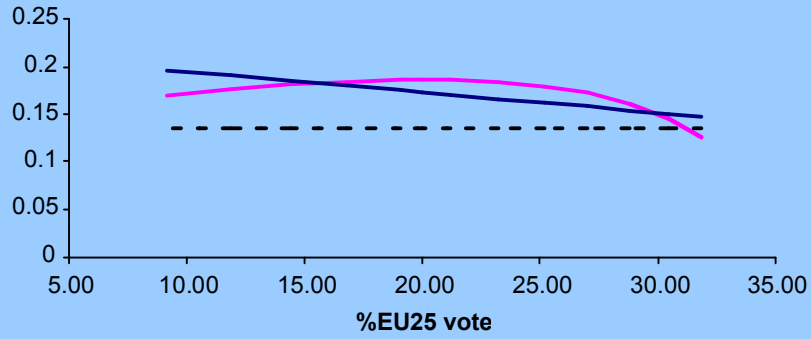
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— Norm power — vote - - - Baseline

25

Power Indices for Selected IMF Members when there is a Single European Seat:
the EU25 Case
Figure 3(f) Syria

Syria



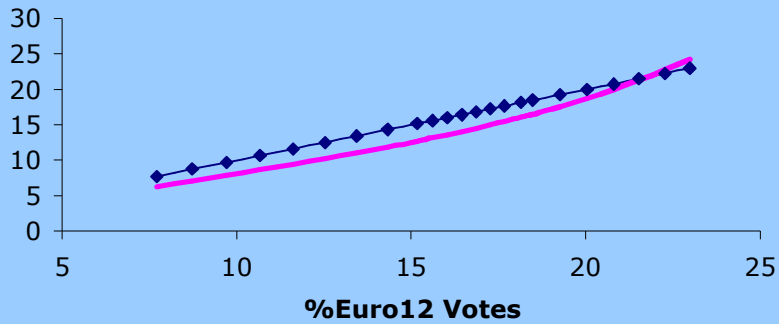
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Power Indices for Selected IMF Members when there is a Single European Seat:
the Euro12 Case
Figure 1(a) Euro12

EU



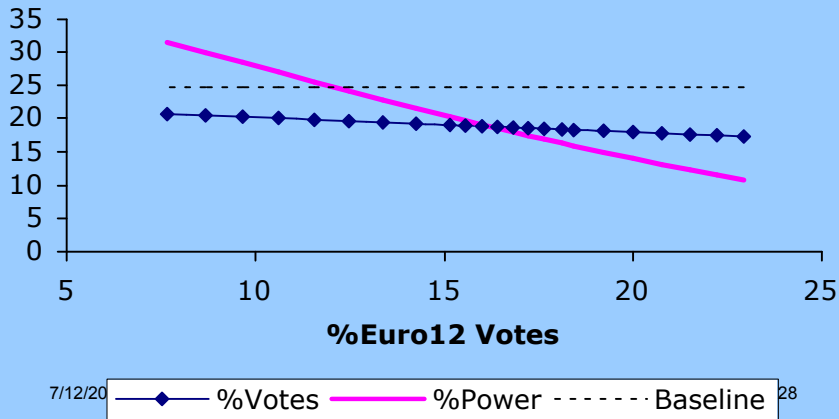
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◆ %Votes — %Power

27

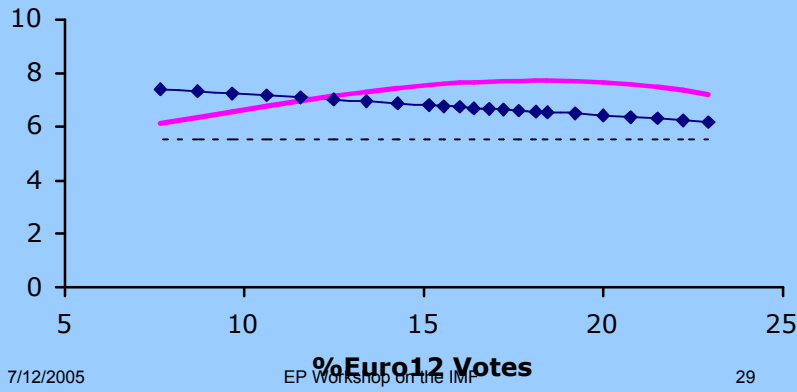
Power Indices for Selected IMF Members when there is a Single European Seat:
the Euro12 Case
Figure 1(b) USA

US



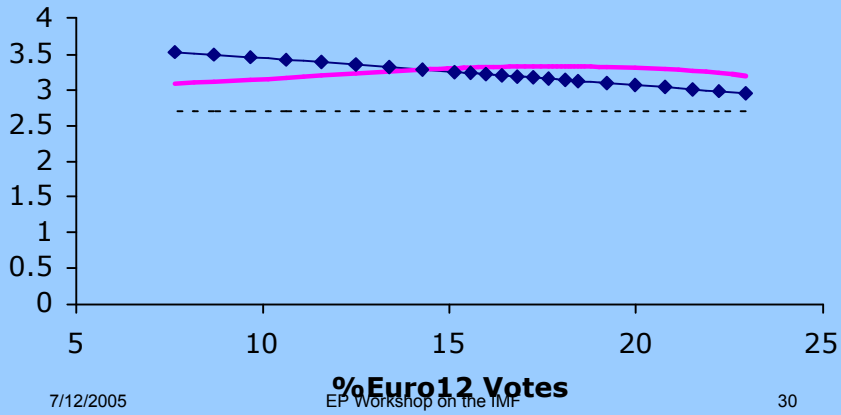
Power Indices for Selected IMF Members when there is a Single European Seat:
the Euro12 Case
Figure 1(c) Japan

Japan



Power Indices for Selected IMF Members when there is a Single European Seat:
the Euro12 Case
Figure 1(d) China

China



Power Indices for Selected IMF Members when there is a Single European Seat:
the Euro12 Case
Figure 1(f) Ethiopia

Ethiopia

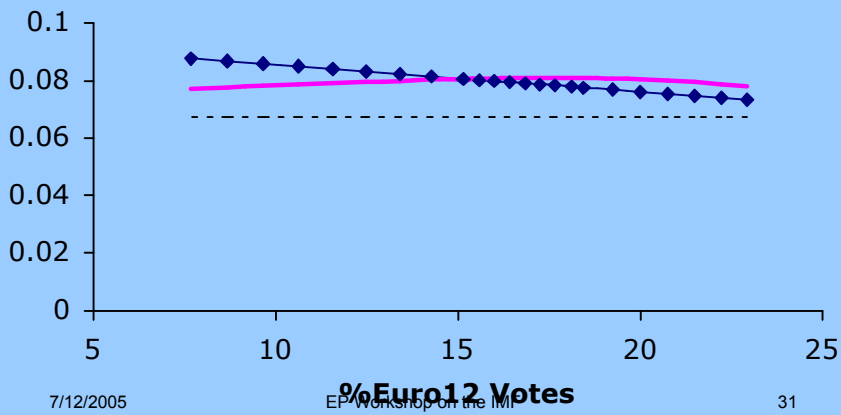


Figure 2(a) Voting Power of the Euro12 and USA

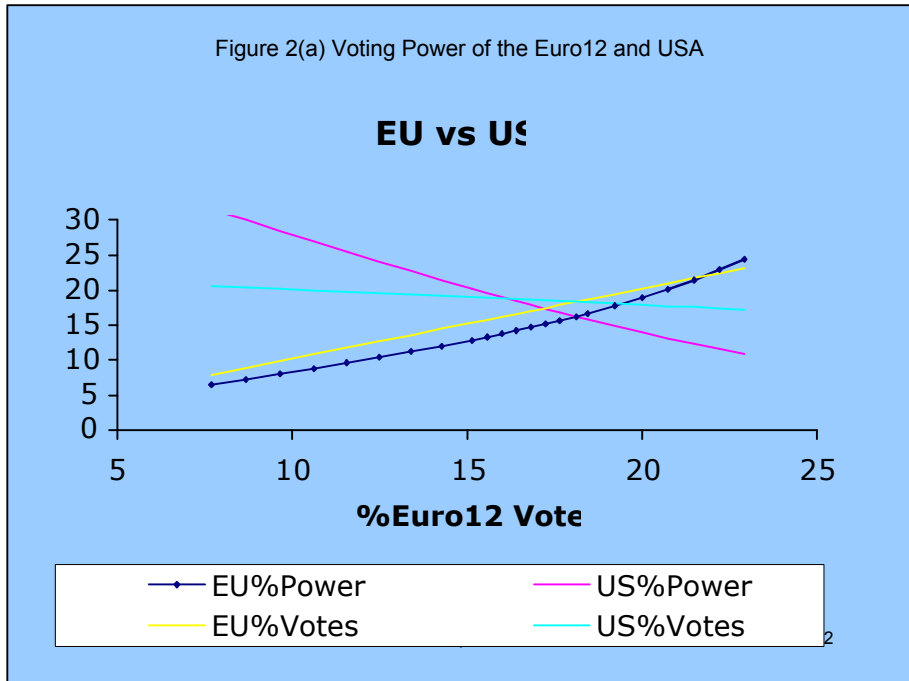
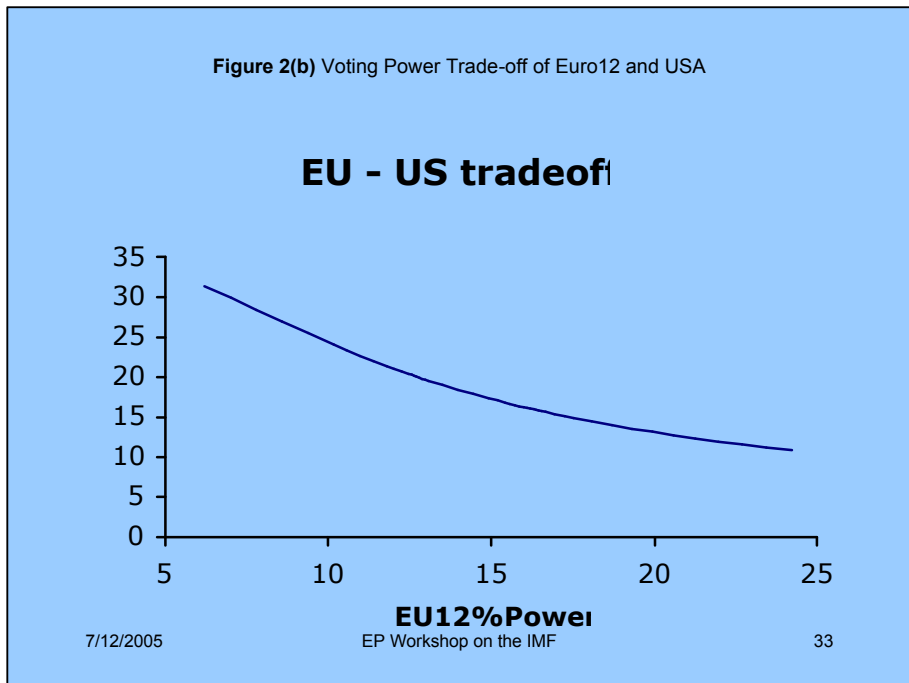


Figure 2(b) Voting Power Trade-off of Euro12 and USA



**Coordination and Representation
of the EU-Member States in the IMF**
Isabella Lindner
Oesterreichische Nationalbank
EP, December 7, 2005
Briefing Note

1

Isabella.Lindner@oenb.at

December 7, 2005

**1. Need for change in the „European“
IMF-Presentation**

- **Pressure from outside – present discussion on quotas and voice: Not only some EMEs but also EU is underrepresented**
- **Move to a Single European Chair/Constituency – is there enough political will?
At present long-term visionary project**

2

Isabella.Lindner@oenb.at

December 7, 2005

2. Possible Formats to improve European Representation

- **Status Quo (7 EDs out of 24 EDs are European):**
Elected multi-country constituencies
Appointed constituencies
Some EU-MS isolated
- **Improved co-ordination: most realistic in the short-term**
(EFC/SCIMF, Eurosystem, EURIMF)
- **Interim Solution, regrouping of EU countries in different constituencies – not advisable**
- **Single Chair: visionary long-term project**
 - Change in the Articles of Agreement
 - EU or Euro-area?
 - big bang or stage-by-stage approach
 - Governance of a single chair: to be determined role of MS, Commission, ECB

3. Influence on IMF Policy

- **Quotas (creditors vs. debtors)**
- **Constituencies**
- **US Blocking Minority**
- **Informal Groupings**
 - G 7
 - G 20
- **European Parliament/US House of Representatives**
- **Financial Sector Lobbying**
- **Washington Consensus**

Briefing papers

Voting Power Implications of a Single European Seat at the IMF

Briefing Paper for the Workshop on the IMF, 7 December 2005, held by the Committee on Economic and Monetary Affairs of the European Parliament

Dennis Leech

University of Warwick

Increased economic and monetary cooperation among EU countries has led to a view that the number of votes currently held by EU countries is disproportionately large and is distorting the voting system. However, as pointed out by Van Houtven (2004), the greater voting strength of the EU has not translated into commensurate influence over IMF decision making because the EU has not been effective enough in developing common positions. Therefore there have been calls to create a single European constituency in the Executive Board or a single European seat in the Board of Governors. In this paper I concentrate on latter. (See Bini Smaghi (2004) or Mahieu et al. (2005) for a fuller discussion.)

A unified representation, without changes in the quotas which determine voting power, would mean the EU bloc would be dominant in voting: the USA currently has 17.1% of the votes compared with 31.9% for the 25 EU members (and 22.9% for the 12 Eurozone countries). This voting disparity with the USA is out of line with comparative economic importance since the economies of the European Union and the USA are of roughly similar size: 31.1% versus 29.3% of world GDP (and the Eurozone is 22.9%).

Therefore the introduction of a single seat must go hand in hand with a reduction in European quotas, whether or not it is part of a general rebalancing as the emerging markets and developing countries want. However the implications of this are not obvious because the European representation will change from being divided among 25 (or 12) more or less uncoordinated seats, each with a relatively small voting weight, to a single governor with a substantial bloc vote, which we would expect to have enhanced power. IMF governance would change from one based on a unipolar voting structure, with one member with a large voting weight and many members with relatively small weights, to a bipolar structure with two members with large voting weights.

In systems of weighted voting like the IMF voting power and voting weight are not the same: a member's power is its ability to influence votes that might take place, and depends on all the other votes as well as the decision rule; on the other hand, weight is just the arithmetical number of votes a member is allocated. For example, where there is one voter with very large weight and many with small weights, as in the current IMF, the power of the large voter is greater than its weight, and all the others less. If there are two or more independent members with large weights they will tend to restrict each other's power and the others could benefit. These are simple properties of the use of weighted voting.²The paper, "Power Versus Weight in IMF Governance: the Possible Beneficial Implications of a United European Bloc Vote" by Dennis Leech and Robert Leech, (Leech and Leech, 2005) demonstrates the fundamental difference between voting power and voting weight by means of examples.

The paper also reports a voting power analysis of the voting rule that applies to the Board of Governors for ordinary decisions (those requiring 50% of the votes). We do this by computing indices of power (Penrose and Banzhaf indices) for all member countries. (Voting power analyses for the Executive Board are given by Leech and Leech, 2004, and Bini-Smaghi, 2005; voting power analyses for decisions requiring special majorities are given in Leech, 2002, and Bini-Smaghi, 2005.)

Where there is a European voting bloc, its members have indirect voting power in a two-level voting system: at the first level they vote on the policy of the bloc and at the second level the bloc vote is cast by its Governor in the IMF. Power of each European member is calculated by multiplying the Penrose power indices at each level. In this way we can determine if a country gains or loses voting power by giving up its own seat and joining the European bloc. We examine several alternative possible voting systems.

Voting power analysis provides measures of a priori or constitutional power, or voting modalities, which are useful in the understanding and design of decision making rules, rather than behavioural or actual power, which depends on other factors.

We analyse the following scenarios:

- (1) The status quo of an IMF of 184 members assuming existing quotas.
- (2) A single European seat, which has voting parity with the USA, all other IMF member countries have their existing quotas, with separate analyses for two cases: (i) the Eurozone countries, and (ii) the European Union. (This follows a proposal of Van Houtven, 2004.)
- (3) A single European seat, and the same two cases, as above, but with a variable European voting weight.

Results:

- (1) In the status quo the USA has by far the largest voting weight, 17.1% of the total, followed by Japan, 6.13%, Germany, 5.99%, etc. This gives the USA a much greater share of the voting power than its weight, 24.5%, and all other countries have correspondingly less. Thus, the status quo can be said to artificially enhance US power above its intended level. Voting power is more unequal than intended.
- (2) The formation of a European bloc (in either case) would increase the voting power of all countries other than bloc members and USA compared to the status quo.
- (3) Where there is a European bloc (in either case), all countries other than bloc members and USA have a greater share of voting power than their weight. The European bloc and the USA have less power than their weight. Voting power is more equal than intended.
- (4) The sum of powers of the two big blocs is minimized when they have voting parity. The power of every other member is maximized when the European bloc and USA have parity.
- (5) The USA retains its unilateral veto over special majority (85%) decisions and the EU bloc gains the same veto power.

Many voting schemes for the European bloc are possible. We computed power indices assuming two-level voting and the following alternative voting systems:

For the Eurozone case: (1) Current IMF weights; (2) GDP weights; (3) Population weights; (4) One Country One Vote. Voting rule: simple majority.

For the EU case: (1) Current IMF weights; (2) Nice: the system of qualified majority voting currently in use in the Council of Ministers; (3) Draft Constitution replacement for Nice; (4) GDP weights; (5) Population weights; (6) Population Square Roots (approximation to Penrose square root rule); (7) One Country One Vote. Voting rule: simple majority except (2) and (3).

Results:

(1) Each EU member could gain voting power compared with the status quo - despite losing its seat and the reduction in EU voting weight - depending on the EU voting system that is adopted.

(2) A voting system based on current IMF weights would give every member country greater power as a member of the European bloc than before.

(3) All other systems would benefit some but not all members.

Conclusion

Voting power analysis suggests that reform of the voting structure to parity between a single EU bloc and the USA could be beneficial for the governance of the IMF, by enhancing the voting power of individual member countries, which have too little power at present.

Moreover, a unified EU representation *could*, depending on the voting rule used by the member countries of the EU bloc, result in EU countries gaining, or at least maintaining, voting power compared with the status quo, while reducing their absolute number of votes.

The analysis uses the existing IMF voting weights and the resulting voting powers are not those that would be chosen by design. It requires further work to compute appropriate voting weights that would lead to the required power distribution. (See Leech 2002.)

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Strategic review of the International Monetary Fund Tasks, Missions and effectiveness of the IMF

**Briefing Paper for the Workshop on the IMF, 7 December 2005, held by the Committee
on Economic and Monetary Affairs of the European Parliament**

Charles Wyplosz

Graduate Institute of International Studies, Geneva and CEPR

Executive Summary

The IMF's key task is to promote international financial stability. It pursues this task by:

- Conducting systematic surveillance of all member countries. The Fund's assessment are generally competent, its recommendations are more controversial. Critics often assert that the IMF errs on the side of toughness. It does, not because its analysis is flawed, but because it is unwilling to take any risk.
- Providing emergency lending. Lending is always conditional, for good reason. Yet the conditions are sometimes seen as unnecessarily harsh. The IMF contends that countries that need emergency finance have made grievous policy mistakes and cannot escape their situation

without adopting more disciplined monetary and fiscal policies. Here again, with some notable exceptions, the IMF's policy recommendations are basically correct but often err on the side of prudence. By and large, the IMF has delivered what it is required to do. It has made some mistakes, especially in some spectacular case involving large countries. In most of these cases, political interference is to be blamed, The IMF has been encouraged to deal with poverty reduction. This is not its mission and there is little that the IMF can do in this area.

The Asian crisis of 1997-8 has led to the end of the Washington consensus. This approach, emphasized rapid liberalization of capital movements, extended attention by the Fund to issues such as corruption, good governance and structural reforms. The result had been mission creep – increasingly intrusive recommendations and conditions – as it had been recognized that even the best macroeconomic policies cannot operate satisfactorily when economic and political conditions are deeply flawed. The IMF has stepped back, partly at least, from the Washington consensus and become considerably more transparent. The IMF's own governance has come under attack after the crisis, but its member countries, which hold the key to any change, have quietly shelved all attempts at serious reform.

1. Is the IMF fulfilling its tasks?

The IMF has initially been given the role of enforcer of the Bretton Woods system of fixed exchange rates and of promoter of international financial stability. The first role has been discontinued in 1972-3 with the end of the Bretton System. The second role remains; it makes the IMF the firefighter of financial stability. In recent years, the IMF has been urged to support poverty reduction and the Millennium Goals.

Promoting financial stability involves two main actions:

- Surveillance. The IMF monitors all member countries as well as the financial markets. It prepares annual reports – in some cases, more frequently – on each and every of its 184 members, which include advice of desirable actions. The IMF has developed a unique knowledge of all countries, as well as a deep understanding of macroeconomic and financial stability. It draws on country experiences broad-ranging lessons that it seeks to generalize and apply. These lessons are often criticized as being too simplistic and stereotyped. In a way, they are, as is any generalization; but the recommendations are usually tailored to local circumstances. The often-decried dogmatic application of rigid principles is partly justified but easily misinterpreted. Any policy involves some degree of risk-taking. When making its recommendations, the IMF cannot be blamed for the analysis, which is usually correct, but with erring on the side of prudence. If fully applied, its recommendations would usually¹ achieve macroeconomic and financial stability. Yet, quite often, macroeconomic and financial stability could well be achieved with less drastic policies, if only the IMF were willing to take some risk of failure. The IMF takes zero risk; it seeks first and foremost to protect its reputation².

- Emergency lending. The occurrence of financial crises can be reduced through surveillance – if advice is heeded – but will never be eliminated – even if advice is heeded. The IMF responds to crises by providing emergency support. This support takes the form of loans, not grants. It adds to the recipient country's external debt. It is in the recipient country's best interest that the loan be put to a good use, i.e. that the risk of yet another crisis be sharply reduced. This is the logic of conditionality, the fact that the IMF attaches conditions to its loans. Like for its surveillance recommendations, the IMF's conditions are often criticized for being rigid, excessive and ignorant of specific local conditions. The criticism is frequently valid, but the interpretation is the same: to protect itself, the IMF calls for conditions that are sufficient but not always necessary. In some instances, this can be counter-productive.

Has the IMF delivered? There have been some spectacular failures, but it is fair to recognize that the vast majority of surveillance reports and loan conditions have been sound. In addition, most of the failures are spectacular because they concern large countries, where political interventions have undoubtedly skewed the Fund's actions.³ One important evolution of the Fund's practice has been the widening of the scope of its advice and conditions, as it moved beyond standard macroeconomic policies into structural and governance areas. Mission creep, as the evolution has been called, has been widely criticized.

¹ There are exceptions, for instance in Russia in 1998 and Argentina in 2001. These are instances of political interferences by the US. It should be noted that, in both instances, European countries have explicitly decided not to oppose the US in the Fund's Executive Board.

² There is no evidence that European Executive Directors have ever challenged the zero-risk approach

³ In nearly every major failure case, in private the IMF staff has been sharply critical.

The criticism is entirely justified, but the issue is complex. When the economy's structure is deeply flawed or when the country is seriously mismanaged by corrupt governments, loans backed by adequate macroeconomic measures are bound to fail. This is why, drop by drop, the IMF has enlarged its realm of intervention. There is no simple answer to this problem. In the end, it will always remain a matter of judgment.

Poverty reduction is a recent addition to the Fund's mission. Like the mission creep phenomenon, it is a serious mistake. The Fund intervenes in periods of crises, or period leading to crises, usually⁴ the outcome of mistaken macroeconomic policies, invariably a lack of monetary and/or fiscal discipline. The Fund has no choice but to request the restoration of discipline, which normally results in imposing hardship upon the citizens, while its loans raise the external debt. In the case of poor countries, most citizens suffer inordinately from both, especially the poorest of the poorest. The IMF cannot turn a blind eye on these consequences, but what can it do? Eliminating poverty is not its task; it has been entrusted to other institutions like the World Bank and UNDP.

The two most criticized international economic institutions are the IMF and the WTO. Unsurprisingly, they are also the most powerful institutions. The WTO's power lies in its tribunal. The IMF's draws its power from its fireman role: everyone knows that, he may need its help one day. It is also noted that the IMF exercises its power on the weak, not on the powerful countries. Countries that stand to need IMF loans, and are therefore most sensitive to its recommendations, are the developing countries with no market access. The rich countries, which are very unlikely to ever need IMF loans, evidently pay only polite attention to IMF recommendations. There is little that can be done about this asymmetry; after all countries are sovereign.

2. The IMF since the Asian crisis

The 1997-8 Asian crisis has exemplified many of the IMF's limits. The crisis has hit large countries, with significant contagion risks. Some of these crises were contagious and self-fulfilling: they occurred not as the result of serious policy mistakes, but because financial markets panicked. These countries' sensitivity to sudden financial flows was the consequence of hurried financial opening, largely at the insistence of international organizations like the IMF and the OECD. Given the size and location of these countries, political interference has been considerable. The loans were huge and the conditions deeply intrusive.

These crises exposed the flaws of the Washington consensus. The IMF has responded in many ways. It has retracted from the Washington consensus. It has stated its intention to scale back its loans and the intrusiveness of its conditions. It has moved to reverse the mission creep evolution. It has become considerably more transparent than before; in particular, its website now routinely posts country reports that used to be considered as highly confidential. In addition, it has established an Independent Evaluation Office. This office now publishes regular and detailed reports, which are well informed but obviously restrained in their sharpest criticisms.

In these respects, the IMF has adequately responded. What has not been done is a serious rethink of the Fund's governance. This is not an issue that the IMF can decide upon; it is in the hands of the member governments. Despite a flurry of debates at the time of the crisis, member governments have given up any attempt to deal with this issue.

3. The IMF and the other international institutions

⁴ There are exceptions, the case of self-fulfilling crises.

The IMF differs from most other international financial institutions in important ways:

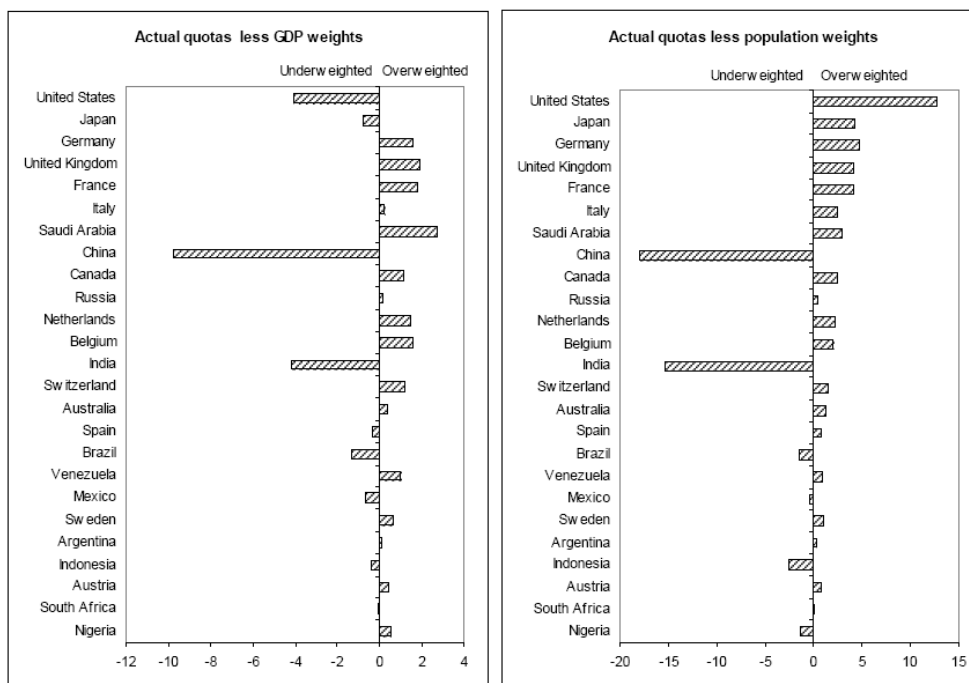
- The IMF has a clearly defined mission. This allows for more accountability than the World Bank, whose mission is wider, and especially than the UN agencies, which have been given vaguely defined terms of reference.
- Like the World Bank, its governance is based on the one-dollar one-vote principle. The rationale is based on its defining feature: it collects contributions from all members, to be used for mutual support. It is natural that voting rights be linked to contributions to the common pot.
- Decisions are taken by the 24-member Executive Board. This structure implies highly unequal representation of the membership: some countries constitute a single constituency, others have their own Executive Director at the head of a multi-country constituency, while others are only represented via their constituency. The advantage is that decision-making is efficient, in stark contrast with the UN system.
- The staff of the IMF is composed of highly competent professionals, recruited through an open and competitive procedure. There is an implicit quota system aiming at making sure that the staff comes from all countries in line with each country's weight. Most staff members hold PhDs from leading schools. The heavy representation of US schools reflects the relative quality of the schools. As a result, the IMF staff is arguably the most competent of all international financial institutions.

4. Remarks on governance

The distribution of power is based on a formula, with limited room for negotiation upon entry. The Appendix presents the formula. It is complicated, essentially reflecting a country's economic size and importance in world trade; in fact they are closely to GDP weights.

As the situation changes, the quotas are revised every five years. The latest revision, which should have taken place in 2003, concluded with no change and a promise to re-evaluate the system for the next revision due in 2008. Since the latest revision in 1998, a few countries have experienced fast growth and are currently underrepresented. This is approximated by the figure on the left below which displays the difference between the current quotas and the GDP weight of the 25 countries with the largest quotas. For instance, the US's quota is 17.49% of the total while its GDP amounts to 21.61% of world GDP; on this measure the US quota is underweighted by some 4.12%. With a quota of 3.00%, China is underweighted by 9.75%, and India is underweighted by 4.13% with a quota of 1.96%. Of course, one can think of other criteria. The right-hand side figure shows the situation if one would establish quotas on the basis of population size.

Comparison of actual quotas with GDP and population weights (%)



Appendix: IMF Quotas

Quota formulas have evolved over time. A formula that was used in 1944 as a basis for determining the broad configuration of the initial quota distribution became known as the Bretton Woods formula. This formula contained five variables: national income, official reserves, imports, export variability, and the ratio of exports to national income. A multi-formula approach was introduced in the early 1960s, when the Bretton Woods formula was supplemented with four other formulas containing the same basic variables but with larger weights for external trade and external variability. The quota formulas were last modified in the context of the Eighth General Review (1982/3) but their basic structure was retained.

The existing quota formula is a five-formula system, including the revised Bretton Woods formula (Q1) and four other equations.

$$\text{Revised Bretton Woods: } Q1 = (0.01Y + 0.025R + 0.05P + 0.2276VC) (1 + C/Y)$$

$$\text{Scheme III : } Q2 = (0.0065Y + 0.0205125R + 0.078P + 0.4052VC) * (1 + C/Y)$$

$$\text{Scheme IV : } Q3 = (0.0045Y + 0.03896768R + 0.07P + 0.076976VC) * (1 + C/Y)$$

$$\text{Scheme M4 : } Q4 = 0.005Y + 0.042280464R + 0.044(P+C) + 0.8352VC$$

$$\text{Scheme M7 : } Q5 = 0.0045Y + 0.05281008R + 0.039(P+C) + 1.0432VC$$

where

- Q1, Q2, Q3, Q4, Q5 = calculated quotas for each formula;
- Y is GDP at current market prices in a recent year;
- R is twelve-month average of gold, foreign exchange reserves, SDR holdings and reserve positions in the IMF for a recent year;
- P is the annual average of current payments (goods, services, income, and

private transfers) for a recent five-year period;

- C is the annual average of current receipts (goods, services, income, and private transfers) for a recent five-year period;

- VC is the variability of annual exports or current receipts, defined as one standard deviation from the centred five-year moving average, from a recent 13-year period.

The calculated quota is then defined as follows: $QC = \text{Max} (Q1, \text{mean of lowest two of } Q2, Q3, Q4, Q5)$.

Tasks, mission and effectiveness of the IMF in today's global economy and division of tasks and cooperation with other international institutions

Briefing Paper for the Workshop on the IMF, 7 December 2005, held by the Committee on Economic and Monetary Affairs of the European Parliament

Kunibert Raffer
Vienna University

Are the tasks and the founding philosophy of the IMF still valid half a century after its foundation? Is the Washington consensus dead? – To be evaluated in connection with recent developments (debt relief, Millennium goals)

The demise of the Bretton Woods system left the IMF with very few remaining tasks, e.g. the Compensatory Financing Facility, which could have been transferred to another institution. No longer needed, the IMF should have been dissolved. Trying to justify its existence the IMF started “structural adjustment” after 1973 in Africa. As the Fund was glad to find clients, conditionality was lenient first. From 1979 on it became stricter. All countries asking for rescheduling in 1981 had a Fund supported “adjustment programme” in place when negotiating with their creditors – these programmes and Fund conditionality did not prevent the debt crisis. The IMF is part of the problem rather than the solution.

The demands of the Washington Consensus are now subsumed under “Anchor actions to achieve the MDGs” (<http://www.imf.org/external/np/exr/facts/mdg.htm> p.5). The IMF calls for “closure in 2005 on current proposals for additional debt relief”, obviously in order to avoid further multilateral debt reductions, while many poor countries “administered” by the IMF and the IBRD over decades need substantial multilateral debt relief. These demands are a time warp back to the 1980s, when the IMF steadfastly denied the necessity of any debt reduction (“growing out of debts”). As debt service overburdens many countries and substantial ODA increases are anything but likely, this would put the achievements of the MDGs beyond many countries’ reach. This, too, is not new: the famous UNICEF study of 1987 proved well before the concept of MDGs existed that “structural adjustment” cut precisely those expenditures one has to increase to reach them. M. Camdessus admitted at ECOSOC that the poorest “too often ... carried the heaviest burden of adjustment” (*IMF Survey*, 29 June 1987, p.195). Malawi had been forced to sell maize from her National Food Reserve to service debts, which left 7 million (population: 11 million) severely short of food in 2002 according to Action Aid. Mr H. Köhler asserted that “The IMF was part of the process of giving advice to the Malawi government”, but by no means the culprit. Definitely, the IMF did not defend the right to food either. In spite of rheto *K. Raffer – Submission EP, IMF Workshop, Brussels - 7 Dec 2005 p.2/4* ric, the real content of IMF policies has changed very little, although some anti-poverty measures under HIPC II, which was decided by the G7 after strong pressure by civil society, are examples to the contrary. Forcing debtors not to exercise their right to capital controls in open breach of the IMF’s statutes (Art. VI.3) makes increased stocks of international reserves necessary, money which could otherwise be used for anti-poverty measures. Adding insult to injury these reserves have become one of the widely-used “targets” of poverty reduction strategies.

What is the content of IMF policy and how are the policies implemented? Is the institutional division of task between the IMF and other international bodies efficient?

The IMF has tried to press as much money out of debtor countries as possible, without regard to safeguarding human rights, any form of debtor protection or the possibility of a fresh start of the economy. It has insisted on the same austerity policies everywhere, even in Asia 1997, where the public budget was not the problem at all. The SDRM does not know any debtor protection measure, falling back behind the standards HIPC II already established. Initially, the IMF insisted on devaluations of debtor currencies. After 1990, e.g. in Asia or Brazil, it insisted on defending fixed exchange rates. In the 1980s debts were in foreign currencies. Devaluing increased the debt burden in domestic currency, without touching creditor claims in dollars. The short term placements of the 1990s were often in the debtor's currency. Speculators would have had to take losses if currencies had been devalued immediately. Fortunately for them, the IMF made countries temporarily defend a fixed peg with extremely high real interest rates (around 40% in Brazil) driving domestic firms into bankruptcy.

According to the IMF's Independent Evaluation Office (IEO) restoring the viability of debtor economies has not necessarily been the IMF's aim. Regarding Indonesia the IEO states that "staff recognized that, if one questioned this basic assumption, an entirely different approach would be necessary, though it never explored comprehensively what that alternative would imply." But "Internal documents show that both staff and management perceived the crisis as an opportunity to assist the reformist economic team in carrying out financial sector reform and deregulation, both areas that were earlier emphasized in IMF surveillance." Ideology prevailed over proper crisis management. The IMF used distress as a leverage to enforce its ideological predilection, exactly as described by Dani Rodrik (*JEL*, 1996)

Joint "debt management" by IBRD and IMF is patently inefficient, as the turf wars between the two institutions show.

Were past interventions by the IMF efficient and effective? (Examples of perceived successes and failures)

Unfortunately not. The strong criticism by the European Parliament in 1992 remains fully relevant. So do its demands that the IMF reconsider the very foundations of its policy or for an alternative (European) approach, which GD VIII once tried to implement. During the first years of "Structural Adjustment" it was attempted to prove success by econometric evidence. As this did not produce statistically significant differences between programme and nonprogramme countries, econometrics was abandoned. One of the few significant results was, Khan's (1990): significantly reduced growth in programme countries (a predicted reduction in the growth rate of at least 0.7% of GDP each year a country had an IMF programme). After more than 3 decades of "structural adjustment" in Africa not one single country there has recovered sustainably. When Korea needed IMF money in the 1980s she did not implement IMF routine, putting this crisis successfully behind her

The grave errors during the Asian Crisis 1997 eventually sparked strong criticism from highly conservative circles. Asian countries were forced to finance large and sustained outflows of *K. Raffer – Submission EP, IMF Workshop, Brussels - 7 Dec 2005 p.3/4*, speculative capital although Article VI.1.a of the IMF's Articles of Agreement stipulates that a "member may not use the Fund's general resources to meet a large and sustained outflow of capital except as provided in Section 2 of this Article [this refers exclusively to reserve tranche purchases KR] and the Fund may request a member to exercise controls to prevent such use of ,the general resources of the Fund". If "a member fails to exercise appropriate controls" on request "the Fund may declare the member ineligible to use the general resources of the Fund". Forcing debtors to forgo their right to capital controls in open breach of the IMF's statutes, makes increased stocks of international reserves necessary. The Asian crash was nothing generically special. Liberalization and deregulation had triggered a host of crises before. In relation to

GDP, developing countries and countries in transition experienced on average more than one crisis per year between 1980 and 1998 that was several times larger than the losses in the Great Depression, as Stiglitz pointed out – one effect of the Washington Consensus and IMF policies enforcing it.

The IEO's evaluation of the IMF's role in Argentina (*The IMF and Argentina, 1991–2001*, July 2004) uncovered many clear cases of, at best, grave negligence. The September 2001 “program was also based on policies that were either known to be counterproductive . . . or that had proved to be ‘ineffective and unsustainable everywhere they had been tried.’” (p.91) The IEO's critique is further damning because it is based not on perfect hindsight but rather on views “expressed by FAD [the IMF's Fiscal Affairs Department] at the time.” (p.91) The Board supported “a program that Directors viewed as deeply flawed” mainly because “no one has proposed a different strategy that, risk adjusted, promises a less costly alternative.” (p.81) The “September 2001 augmentation suffered from a number of weaknesses in program design, which were evident at the time. If the debt were indeed unsustainable, as by then well recognized by IMF staff, the program offered no solution to that problem.” (p. 89) The IMF “failed to use the best analytical tools,” (p.109), “[a]vailable analytical tools were not used to explore potential vulnerabilities in sufficient depth.” (p. 110)

IMF managed debt reductions have failed due to the Fund's “overoptimism”. IMF and IDA (“Debt Sustainability in Low-Income Countries - Proposal for an Operational Framework and Policy Implications”, 2004, p.13) themselves admitted:

“past experience suggesting a systematic tendency toward excessive optimism . . . a common theme behind the historical rise in low-income countries' debt ratios was that borrowing decisions were predicated on growth projections that never materialized . . . analysis of projections made by Fund staff over the period 1990-2001 suggests a bias toward over-optimism of about 1 percentage point a year in forecasts of low-income country real GDP growth. The bias in projecting GDP growth in U.S. dollar terms, however, was considerably larger, at almost 5 percent- age points a year.”

The document calls for “well-disciplined projections, including by laying bare the assumptions on which they are predicated and by subjecting them to rigorous stress tests that explicitly incorporate the impact of exogenous shocks.” (*ibid.*) The same “overoptimism” happened in, the Commonwealth of Independent States: “overoptimism by multilaterals contributed to the high debt levels” (Helbling *et al.*, *IMF Working Paper* WP/04/93, 2004, p.1), and in HIPC countries.

How to learn from past negative experiences such as the "One size fits all recipes" of the IMF?

The IMF's deplorable record is caused by an economically perverted incentive system that emerged when conditionality was introduced (in its statutes as late as 1969). As the IMF has to be repaid in full even when (rather than if) its staff negligently or willingly inflicts damages on its clients, its failures and debacles increase its income and importance. IMF-flops create IMF-jobs. Economically, ethically, and legally incorrect behaviour is rewarded. Victims are forced to pay. Change is mandatory. Acting as a consultant by giving advice (critics would formulate differently) the IMF must become financially accountable, liable to pay compensation for tortious actions [cf. K. Raffer, “International Financial Institutions and Financial Accountability”, *Ethics & International Affairs* 18(2), 2004, pp.61ff; in: S.M. Murshed & K. Raffer, eds, *Trade, Transfers, and Development, Problems and Prospects for the Twenty First Century*, Elgar, Aldershot K. Raffer – *Submission EP, IMF Workshop, Brussels - 7 Dec 2005* p.4/4 ate IMF-jobs. Economically, ethically, and legally incorrect behaviour is rewarded.

Victims are forced to pay. Change is mandatory. Acting as a consultant by giving advice (critics would formulate differently) the IMF must become financially accountable, liable to pay compensation for tortious actions [cf. K. Raffer, “International Financial Institutions and Financial Accountability” „*Ethics & International Affairs* 18(2), 2004, pp.61ff; K. Raffer, “International Financial Institutions and Financial Accountability”, in: S.M. Murshed & K. Raffer, eds, *Trade, Transfers, and Development, Problems and Prospects for the Twenty First Century*, Elgar, Aldershot (UK) 1993, also available at my homepage]. In cases such as those documented by the IEO this could be implemented easily. Stiglitz’s famous story of an IMF-“mission” copying large parts of the text for one country’s report and transferring them wholesale to another (leaving the original country’s name in a few places, though) is a glaring example of the difference between the IMF’s and decent and legally proper arrangements. Legal implications - including consequences under penal law in most if not all countries - are absolutely clear in the case of normal consultants. Undue IMF privileges must be discontinued. Whenever damages are caused by the IMF violating membership rights, such as in Asia, it must pay compensation.

In the case of programmes, where faults are difficult to isolate, I proposed an easy solution: treating the IMF like any other creditor within the framework of sovereign insolvency procedures based on the main principles of US Chapter 9 (municipal insolvency; cf. Raffer, *World Development* 1990, pp.301ff, or texts on my homepage) whenever a country “advised” by the Fund becomes insolvent. As the Fund is much more involved, there is no reason to treat it better than “normal” creditors. Legally, the IMF is **not** a preferred creditor, as one can read on its own homepage (v. James M. Boughton, *Silent Revolution*, Washington DC: IMF 2001, Chapter 16 www.imf.org/external/pubs/ft/history/2001/ch16.pdf, p.820). Rutsel Silvestre even argues that its statutes contain “a presumption against a preferred creditor status”. There is no reason why the IMF could not reduce claims like any other creditor. It has formed loan loss reserves: client countries have already paid for debt relief but are denied it by the IMF charging insurance fees without any intention to deliver what has been paid for. Obviously, one of the SDRM’s principal but unmentioned goals was surreptitiously to get this coveted legally preferred status.

If one accepts sound economic principles as well as the Rule of Law and the principles of Good Governance, the IMF must first respect its own statutes. Furthermore, there are two options:

- returning to its origins, i.e. unconditional emergency financing. This could justify a preferred creditor status, although none was enshrined at Bretton Woods. When conditionality became part of the IMF’s statutes in 1969, it was unfortunately forgotten to combine the power to demand compliance with appropriate financial accountability.

- continuing its present practice of combining policy advice and conditional money. Then the IMF would continue to make decisions on economic policy and must be made financially accountable for tortious behaviour. Introducing the market economy to one of the last hold-outs of central planning would improve the quality of its services dramatically. The present, perverted incentive system must go. It causes damages to debtors, the poor, and avoidable and unjust losses to other, especially private creditors. The IMF must no longer be denied the benefits of the market mechanism. Financial accountability, economic sense, good governance and the Rule of Law, once brought to the IMF, would change its policies fundamentally and to the better.