The IMF, Global Inequality, & Development

What Are The Obstacles to Development?

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What are the Obstacles to Development?

The IMF's policies embody a liberal economic worldview in which pro-market policies and integration into the global economy are considered prerequisites for economic growth and development. From this perspective, the misguided policies of developing states have been the main obstacles to development.

Critics of the IMF disagree. In their view, the primary obstacle to development is a global economic order that works systematically to the advantage of the wealthy and powerful at the expense of the poor and weak. Heavily influenced by a Marxist analysis of global capitalism, this perspective portrays the IMF as an integral part of a global economic system that perpetuates poverty and inequality.
The IMF

Source: Dictionary of American History | 2003

- The IMF can make loans to member countries through standby arrangements. Depending on the size of the loan, the fund imposes certain conditions.
- Known as IMF **conditionality**, these measures often interfere with the sovereignty of member countries with regard to economic policy to the extent that Marxians call these interventions “Neo-Colonialism” or “Neo-Imperialism.”
- IMF conditions can require devaluation of currencies, removal of government subsidies and barriers to import, cuts in social services, control over wages, trade liberalization, and pressure to pursue free-market policies.
- This bundle of market-oriented reforms required for developing nations to receive IMF loans is called “structural adjustment policies.”
- IMF conditionality has been criticized as being too severe, imposing hardship on debtor countries. Because IMF policies are imposed by an international agency consisting of industrialized countries, they give the appearance of maintaining the dependency of the Third World.
- Watch this video (7 min). Susan George speaking about the IMF, WB, & WTO. For more details (50 min), check her video on Neoliberalism.
The World Bank

Source: Dictionary of American History | 2006

- In 2006 there were 180 members of the World Bank Group, each of which must also be a member of the IMF. Each member acts as a shareholder but, due to their size and resources, the United States, Japan, Germany, France, and the United Kingdom dominate policymaking.
- It invests money in projects designed to create stable, sustainable, equitable growth in developing countries. Project lending makes money available for tasks such as natural resource development.
- Loans can also be made to an entire sector of a country's economy—agriculture, for example—or can be designed to aid in reorganizing a country's institutions to orient their policies toward free trade.
- Finally, loans are made to temporarily relieve debt crisis.
The WTO


- The WTO took over General Agreement on Tariffs and Trade’s (GATT) rules with increased powers, and brought intellectual property rights, agriculture, clothing and textiles, and services under its control.
- On November 30, 1999, about 50,000 people demonstrated in Seattle against the WTO before the planned WTO Ministerial meetings.
- Over 1,400 organizations signed a letter stating their opposition to the WTO. According to the text of the letter, protesting organizations accused the WTO of principally trying to pry open markets for the benefit of transnational corporations at the expense of national and local economies; workers, farmers, indigenous peoples, women and other social groups; health and safety; the environment; and animal welfare. In addition, the WTO system, rules and procedures are undemocratic, non-transparent and non-accountable and have operated to marginalize the majority of the world’s people.
- Watch this video about protests against the WTO in Seattle in 1999.
International Division of Labor (IDL) & its Problems

After WWII, decolonization did nothing to alter the international division of labor that emerged over the previous century. **Manufacturing** was still concentrated in the industrialized economies of the **North**, whereas the newly independent countries of the **South** remained sources of **primary products** (e.g., unprocessed raw materials and agricultural goods).

Not only were Third World economies still reliant on primary product exports, but also most depended on just one or two products for the bulk of their export earnings. They were highly-specialized compared to diversified economies such as the United States. It was (and still is) not unusual for a developing country to receive more than half of its export income from the sale of a single commodity. More than two decades after independence, for example, **96% of Uganda’s** export earnings came from **coffee**, **89% of Zambia’s** from **copper**, and **59% of Ghana’s** from **cocoa**. A diversified economy can survive a slump in any single economic sector, but if the price of coffee falls by 50 percent in a given year, Uganda is in real trouble.
By the late 1950s, this division of labor and specialization came to be viewed as an obstacle to development for two reasons:

First, prices of many primary products often fluctuated wildly from year to year, and the resulting instability in income created difficulties for planning and development. Imagine, for example, individuals trying to borrow money or make investments if their incomes went up or down unpredictably by 50 percent from year to year.

Second, there was a general tendency for the price of primary products except oil to fall without any similar reduction in the price of manufactured goods. Economists refer to this as declining terms of trade—that is, the prices for those commodities developing nations sell are going down, whereas prices for the manufactured goods they buy are not.

Since exporting agricultural produce and raw materials are always cheaper than sophisticated merchandise from the North, left unchecked, this trend in commercial exchange would inexorably lead to even greater poverty and inequality.
Import Substitution

In order for them to develop diversified industries Third World countries have tried developing their own industries. The problem was that in the initial stages manufactured goods from Third World countries would not be very competitive with those of established industries in North America, Europe, and Japan.

How could developing nations create a manufacturing base in the face of competition from the already industrialized economies? The solution adopted in Third World countries, particularly in Latin America and Africa, was import substitution. That is, domestically manufactured goods would be substituted for previously imported manufactured goods.

There were two components of this strategy.

First, governments channeled investment into selected industries.

Second, tariffs and quotas protected so-called infant industries from the international market until they could compete on their own.
1950’s & 60’s - Period of Success

- Import substitution met with some initial success during the 1950s and 1960s, with many Latin American and African countries experiencing high rates of economic growth.

- During this period the focus was largely on low-tech, labor-intensive industries such as nondurable consumer goods (shoes, clothes, etc.). These industries did not require huge investments and were labor intensive, allowing Third World nations to take advantage of their large pools of low-wage labor.

- Making the transition to high-tech, capital-intensive manufacturing such as electronics and appliances proved more problematic. Poor countries lacked the domestic capital for investment because their poor populations had low rates of saving. Third World nations were forced to look abroad for investment capital.

- There were two potential sources—multinational corporations and northern financial institutions. Both options had drawbacks.
1970s - Period of Stagnation

- Relying on corporations increased their power and influence, something viewed with great suspicion in recently decolonized nations. Borrowed money, on the other hand, would have to be paid back, with interest. But because this investment was supposed to produce economic growth, paying back the loans a few years down the road was not expected to pose much of a problem.
- By the 1970s, however, Third World economies began to stagnate. The situation was exacerbated when oil-producing nations, acting through the Organization of Petroleum Exporting Countries (OPEC) raised oil prices substantially, beginning in 1973 and again in 1979.
- Although higher oil prices inconvenienced wealthy industrial economies, they crippled many developing nations. Thus, by the mid-to late 1970s, many developing countries saw economic growth rates plummet and the costs of imported energy soar.
The Debt Crisis of 1970s

Since the developing countries did not have appropriate growth, they were not able to return their loans, which caused the Debt Crisis.

The **IMF** blamed the misguided economic policies of developing nations for poor growth. That is one side of the story.

The **opponents of the IMF** blame the lack of development on the global capitalist system as the primary obstacle to genuine development.

A great many **economists** blame the crisis on the increase in oil prices in **1970s** that hit everybody, but poorer nations got even more affected.

The oil prices went up in 1973 due to the political and military reason. That was the time of the **Yom Kippur war**, between Israel and its Arab neighbors. The Suez Canal was closed due to fighting. The tankers with oil could not pass through, which created the shortage of oil and its higher costs of transportation around Africa. The Arab countries also wanted to exert economic pressure on the U.S. and other Western powers that supported Israel in the war. They stopped exporting oil to them. The crisis hit the West hard and they stopped sending weapons to Israel. However, high oil prices hit the poor countries much more so.
The Mexican Debt Crisis of 1970s

- The most significant of the early crises involved Mexico. Throughout the 1970s, Mexico’s debt burden grew faster than its economy as a whole. By the early 1980s, it was clear that Mexico would be unable to pay back its loans on schedule. Fearing the consequences of a Mexican default, especially for major international banks, the IMF loaned Mexico money to makes it payments.
- The money did not come without strings, however. The IMF insisted that Mexico enact economic reforms. The IMF claimed the reforms were necessary to promote economic growth needed for Mexico to repay its loans.
- This set the precedent for subsequent IMF bailouts throughout Latin America, Africa, and Asia over the next two decades.
The late 1970s and early 1980s were not only a period of emerging crisis in much of the developing world but also changing intellectual currents in the industrialized world.

Since the end of World War II, economic thought in the United States and Europe was dominated by the ideas of British economist John Maynard Keynes (1883–1946). While supporting the essential features of capitalism, Keynes advocated a greater role for government in moderating the ups and downs of the capitalist business cycle. During recessions, for example, when growth is low and unemployment high, governments should spend at a deficit to inject money into the economy to encourage growth and employment.
The IMF and Neoliberalism

By the mid-1970s, Keynesianism came under attack by economists such as Milton Friedman (1912–2006), who favored a diminished role for government.

The election of Ronald Reagan in the United States and Margaret Thatcher in Great Britain was an indication of these shifting intellectual currents. Domestically, both Thatcher and Reagan pursued similar agendas:
- tax cuts,
- lower government spending,
- fewer regulations,
- scaled-back social welfare programs,
- and privatization.
Structural Adjustment Reforms

1. Fiscal austerity (balancing government budgets.) This usually entailed either increases in government revenues (usually new fees for government services) or, more commonly, reductions in government spending.

2. Reductions in government subsidies to domestic industries. These subsidies had often been part of import substitution strategies.

3. Reduction of tariffs, quotas, and other barriers to imports. This would subject domestic industries to international competition.

4. Capital market liberalization. This is a technical term for reducing restrictions on foreign investment.

5. Privatization, or selling off government-owned industries to the private sector.
Washington Consensus

Taken together, these policies reflected the IMF’s worldview “that market forces, liberalized trade and payments, and general freedom in economic matters are usually more efficient and promote greater prosperity and a better allocation of resources than a system characterized by controls and restrictions.”

This bundle of policies and the underlying liberal/neoliberal economic philosophy became known as the Washington consensus, a description reflecting the United States’ significant role in shaping these policies.
The Bolster for Market Economy (Free Trade)

- The growing influence of free market policies was bolstered by the total failure of state socialism and communism in the Soviet Union and Eastern Europe, where decades of state planning and government control produced economic stagnation and social malaise.

- Even though the Soviet model of development appeared attractive to some in the developing world during the 1950s and 1960s because it held out the promise of rapid development, by the 1980s its luster was gone.

- The political and intellectual triumph of liberal democratic capitalism appeared universal.

- This vision of smaller government and increased reliance on the market came to be known as neoliberalism.
The Missing Part in the Story on the Soviet Economy

- While the Soviets did make their fair share of mistakes in their economy by not being very successful in enticing creativity among their workers and engineers and by completely blocking entrepreneurship, it would be only fair to state that the Soviet Union and Eastern Europe did not have the same start as the U.S. and Western Europe did after WWII. So, they needed more time to recuperate and rebuild after the war.

- In WWII, the Soviet Union lost more than 13% of its population (~24 millions) and the U.S. lost less than 0.5% (~500,000). Poland lost >18%, Lithuania ~14%, Latvia ~12%, Yugoslavia 7%, Germany ~11%, U.K. ~ 1%, France ~1.5%, etc.

- Undoubtedly, the destruction of infrastructure and industry in Western Europe was significant, especially in Germany. However, in Eastern Europe, especially in the Soviet Union, it was catastrophic.

- While all West European countries enjoyed the financial support of the U.S., which was virtually untouched by WWII, the Soviets and East European countries did not enjoy the benefits of the Marshal Plan.

- Why? They simply refused it, because it was conditioned by the introduction of free trade, i.e., capitalism.
The Argument for the IMF

The IMF and its supporters reject the argument that a liberal international economic order is an obstacle to development. If all the development efforts of the past fifty years had met with failure, there might be good reason to blame the global economic system. But this has not been the case. The past fifty years have produced some abject failures, some modest development, and even some truly remarkable success stories. This diversity of outcomes can be illustrated with some striking comparisons between Africa and East Asia.

- In the early 1950s, for example, Egypt had roughly the same average income as most East Asian nations, but today incomes in East Asia are between five and thirty times larger than Egypt’s.
- “In 1965, Nigeria (oil exporter) had higher GDP per capita than Indonesia (another oil exporter); twenty-five years later, Indonesia had three times the Nigerian level.”
- Even more dramatic is a comparison of Ghana and South Korea: In 1957, Ghana had a larger gross national product (GNP) than South Korea, but by 1996 Ghana’s GNP stood at $7 billion whereas South Korea’s GNP had soared to $485 billion, almost seventy times larger than Ghana’s.
The Argument for the IMF

The variance in development among developing countries is not easily explained by histories of colonialism because some of the most successful East Asian nations had also been colonies. To many observers, the fact that some nations have achieved genuine development and others have not indicates that “the basic obstacles to economic development [can be found] within the less developed countries themselves.”

But what might these obstacles be? The list of possibilities is long indeed:

- war and frequent civil unrest,
- political instability,
- rampant government corruption,
- cultural and religious beliefs that inhibit initiative, and
- cumbersome bureaucracies.

One of the most commonly cited problems, however, is bad or misguided policies.
The IMF remedy to underdevelopment

From the IMF’s perspective, one thing was clear: Excessive government control of the economy and attempts to cut off developing economies from foreign trade and investment are definitely not routes to development; instead, “market openness, fiscal discipline and noninterventionism constituted the route to economic development.”

The poster children for economic development are the so-called East Asian “tigers” or newly industrializing countries (NICs). According to Robert Gilpin, “The most successful economies among the less developed countries are precisely those that have put their houses in order and that participate most aggressively in the world economy. They are the so-called Gang of Four: Hong Kong, Singapore, South Korea, and Taiwan.”

Do these cases support the neoliberal view that free market policies and does the integration into the global economy lead to development?
Are the four Asian Tigers really Neoliberal Tigers?

- As a matter of fact, East Asian governments were often heavily involved in directing investment into targeted industries. This development with a heavy dose of government guidance does not seem to have followed the neoliberal formula of development, but was rather guided by Friedrich List’s conservative idea of state control.

- On the other side, it could not be denied that their policies were more market and trade oriented than the import substitution policies of Latin America and many African nations.

- Truly enough, the East Asian nations did clearly embrace international trade as the engine of the economic growth even if governments played a more active role domestically.
The case of India

- India provides a somewhat more clear-cut example of successful market-oriented policies.
- In the two decades following independence, India’s economic performance was disappointing. “The main elements of India’s policy framework stifled growth until the 1970s.” These elements included
  - “extensive bureaucratic controls over production, investment and trade,”
  - “inward looking trade and investment policies,” and
  - “a substantial public sector, going well beyond the conventional confines of public utilities and infrastructure.”
- Beginning in the 1980s (and especially after 1991), India undertook reforms to reduce government control and increase foreign trade and investment.
- The result has been consistently higher rates of economic growth and a substantial reduction in poverty. Though India’s reforms were not the result of IMF pressure, its experience is seen as confirmation of the IMF’s underlying market-oriented philosophy.
The case of Chile

Chile provides a more controversial case. In the late 1970s, under the influence of economists trained by University of Chicago economists such as Milton Friedman, the Chilean government adopted a radical free market agenda, opening Chile’s economy to imports and foreign investment while reducing government spending, going so far as to privatize Chile’s version of social security. After some initial hardship, Chile enjoyed more than a decade of sustained economic growth unrivaled in Latin America. Chile’s example remains controversial for two reasons.

- First, its market reforms were indeed radical, going well beyond anything the IMF demands.
- Second, the reforms were enacted by a military dictatorship that did not have to worry about its unpopularity.
- The connection between military dictatorship and market reforms was not exactly a public relations success for advocates of similar reforms elsewhere in Latin America.
Moral Hazard

**moral hazard** - Situation created when policies promote the very problems they were intended to solve. Many argue that IMF loans to debt-ridden developing nations serve to relieve them from the consequences of their mistakes and rescue banks that made bad loans. In doing so, these loans only encourage further irresponsibility.

Other, in turn, argue that the IMF is actually not trying to “relieve” indebted countries by giving them new loans, but rather to further make them dependent and controlled by itself. As someone said, “There are two ways to conquer and enslave a nation. One is by the sword. The other is by debt.”

See this video featuring John Perkins to hear the counterarguments to the IMF’s praises of its own work.
Three Main Points of Criticism of Neoliberalism

Critics of the IMF, neoliberalism, and structural adjustment make three basic arguments.

- First, the neoliberal vision fails to recognize the fundamentally unequal terms on which developing nations participate in the global economy.

- Second, after twenty years there is little evidence that structural adjustment policies promote economic growth or reduce poverty.

- Third, developed nations are hypocritical in imposing a model of development that virtually none of them adopted during their growth.
Though criticisms of the IMF and neoliberalism come from many perspectives, the dominant critique is rooted in dependency theory, which emerged in Latin America during the 1950s and 1960s to explain the region’s lack of development. Unlike neoliberals, “all dependency theorists maintain that underdevelopment is due primarily to external forces of the world capitalist system and is not due to the policies of LDCs [less developed countries] themselves.”

Dependency theorists see a world divided between an industrial core and an underdeveloped periphery (a category of semiperiphery has also been included to account for the very few nations that have managed to move out of the periphery, such as the East Asian economies).

Though the troops and governors of formal colonialism left long ago, a new form of economic imperialism, referred to as neoinperialism or neocolonialism, has taken its place.

The primary agent of this new imperialism is the multinational corporation, “the embodiment of international capital.” Multinational corporations benefit from an impoverished periphery because it provides cheap commodities and inexpensive labor that allow them to reap windfall profits.
Comprador Class

This profiteering is done in conjunction with a domestic political-economic elite within Third World nations that has been bought off by, and serves the interests of, international capital. This comprador class collaborates with foreign capital in its domination of peripheral nations and forms an “anti-nation” within the nation.

Even when developing nations experience high rates of economic growth, the benefits are not distributed evenly. The new wealth goes disproportionately to economic elites. The benefits of growth do not “filter” or “trickle” down to the masses.

So-called economic growth in many developing nations has not always resulted in the reduction of poverty or improved living standards.

Growth and development are not one and the same.

Impressive statistics about economic growth are misleading and all too often obscure the growing inequality within developing nations.
Distribution of Wealth
(check how the wealth is distributed in the U.S.)

- Increasing inequality within developing nations is accompanied by a growing gap between developed and developing nations in the global economy. The periphery is systematically impoverished or underdeveloped as multinationals earn substantial profits they send home to line the pockets of shareholders and corporate executives.

- Profits are not reinvested in the Third World nations where they were made. The result is a massive transfer of wealth from the periphery to the core.

- The contrast with the economic development of nations such as the United States is critical here. Although Andrew Carnegie and John D. Rockefeller raked in hundreds of millions in profits during the late 1800s and early 1900s, at least they reinvested most of their profits back into the American economy, producing genuine development.

- This is why even Marx agreed that capitalism was a “progressive” force: It is very good at developing a society’s resources. But when corporations earn huge profits in the periphery today, these profits are not reinvested but rather siphoned away. This constitutes an exploitative process of unequal exchange that produces underdevelopment and exacerbates global inequality.
The IMF and the U.S.

As an almost physical manifestation of its role in the global economy, the IMF is headquartered just a few blocks from the White House and the World Bank in Washington, DC. This alone is telling. Voting within the IMF is weighted according to a nation’s contributions to the fund.

Because it contributes 18% of IMF funds, the United States has an equivalent share of voting power; as a result, it is almost impossible for the IMF to do anything over the objections of the United States.

Belgium and the Netherlands combined have more voting power than China, the world’s most populous nation, and Canada has more voting power than India, the second most populous nation.

In what some found to be a moment of rare candor, U.S. Trade Representative Mickey Kantor once characterized the IMF as a “battering ram” for U.S. interests.
Poverty & the Lack of Development as “Overdetermined”

- Poor, undeveloped, ailing, hungry, war-ridden societies due to all of their internal problems end up caught on the horns of a dilemma:
  - Without economic growth there will be no stability, but without stability there can be no economic growth.
- One can also look at the relationships among economic growth, education, and healthcare.
  - Economic growth requires a decently educated and healthy work force, but without economic growth how do developing nations provide the education and healthcare their people need? etc. etc.
- Poverty and the lack of development seem overdetermined—that is, there are so many obstacles that the elimination of just one or two would barely make a dent in the larger scheme of things.
- A good place to start seems to be the economy, and the foreign friends should help. It is our human duty.