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## Timothy Lane: “Tensions in the Role of the IMF”

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Dr. Lane noted that changes in the world economy since its post-war establishment had brought into question the IMF’s purpose and role. There had been important attempts to reform the institution over the last six to eight years but significant tensions remained. Dr. Lane set out three principal areas of tension over policy.

The use of conditionality in IMF Programmes had been the subject of sustained scrutiny. Revised guidelines issued in 2002 called for streamlining so as to include only conditions critical to the macroeconomic objectives of the programme. However, Dr. Lane observed that tension was inherent in the setting of conditions since – even absent the more heavily criticised and intrusive ‘grandmotherliness’ of some conditions – there was often room for debate as to whether certain structural conditions were instrumentally important to macroeconomic outcomes. The recent review of prolonged lending suggested that the IMF should be more ready to refuse its financing to countries whose policies are not, in the IMF’s judgement, conducive to economic growth and the repayment of the lending. However, since there was political pressure to lend, conditions were often seen as the second best alternative to saying ‘no’.

The emerging market financial crises since the mid-nineties pointed to the need for a number of changes in the IMF’s work. The crises had pointed to weaknesses in its surveillance: in some cases (such as Korea and Indonesia), crises were not anticipated while in others (such as Thailand) the Fund did point

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<sup>1</sup> Dr. Lane spoke in a personal capacity and noted that the views he presented did not represent the position of the IMF.

to vulnerabilities but was not effective in persuading the authorities to take action to head off the crisis. There were also concerns that the IMF did not pay adequate attention to the risks of capital account liberalisation. The financing provided to countries in crisis had been criticised from both sides—i.e. both for being too generous and for being too mean; in any event, this financing, together with the accompanying policies, had not averted the need for massive adjustments in crisis countries' external current accounts. These concerns generated changes in a number of aspects of the IMF's work, including surveillance, crisis management, and financing facilities. However, tensions still remained. In particular, there was an inherent tension between the need for a consistent institutional approach to crisis financing and the concerns that too much predictability could be counter-productive because of the market response it could generate: moral hazard in the case of official financing or greater volatility and contagion in the case of attempts to bail in private creditors.

The level of prolonged use indicated that the IMF had departed from its initial role of providing short-term, revolving finance to member countries, becoming a sustained lender to countries with more long-term, structural economic problems. The IMF's Independent Evaluation Office had drawn attention to this issue in its report on prolonged use. The IMF had responded primarily by introducing ex post assessments of prolonged users to ensure that a longer-term program engagement does not occur for the wrong reasons. But prolonged use also highlighted two problems that are less soluble. One is that it is extremely hard—sometimes for political reasons, sometimes due to the 'Samaritan's Dilemma'—for the IMF to say 'no' to borrowers. Furthermore, since many other potential donors or financiers relied upon the agreement of an IMF Programme as a signal of sound macroeconomic policies to trigger their grants or loans, the IMF often finds itself under pressure to approve a financing arrangement even when there is not a clear basis for an IMF-supported program.

Dr. Lane summarised the tensions arising as being five-fold:

- between clear principles and the need for discretion;
- between selectivity and pressure to lend;
- between selectivity and the IMF's signalling role;
- between parsimony and comprehensiveness in the design of conditionality; and
- between conditionality and ownership by sovereign governments.

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