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Sayonara to world finance sisters?

By Richard W. Rahn
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Do you think the International Monetary Fund (IMF) and the World Bank (WB) should be abolished? These sister organizations had their annual spring meetings in Washington this past weekend. It is obvious to everyone that both organizations are in deep trouble.

The two organizations were conceived at a Bretton Woods, N.H., conference in July 1944. The IMF was given primary responsibility for ensuring the stability of the international monetary and financial system and, specifically, to manage gold-denominated fixed-exchange rate system set up then (but abolished in 1973).

The World Bank is actually a group of five international organizations whose principal mission is to provide development finance and advice in order to eliminate global poverty. For several decades, responsible critics of the World Bank (including a number of its former senior professionals, such as former chief economist and Nobel Laureate Joseph Stiglitz and distinguished economist William Easterly) have presented considerable evidence that the institution has created many more problems than it has solved.

The primary mission of the WB was misperceived at the beginning, and hence it was doomed to failure. Back in 1944, there was the widespread belief that if governments in poor countries were provided funds for infrastructure and other development they could quickly become more prosperous. As we now know, government officials spending other peoples' money on politically determined projects usually results in overspending and poor performance, even in wealthy democracies. In poor countries, the results are almost always worse. So all too much of the money the WB acquired from middle-class taxpayers in wealthy countries went merely to enrich government officials and corrupt leaders in poor countries.

The WB, because of lack of accounting controls and proper oversight and transparency, fueled corruption and oppression in Africa and elsewhere. In addition, the poor people who did not benefit from WB spending ended up saddled with the debt they were obligated to repay to the WB.

In 1990, I was the co-chairman of the Bulgarian economic transition team, sponsored by the National Chamber Foundation and the Bulgarian government. As part of our effort, we were trying to privatize most state-owned companies, including the state telephone company. Behind our backs, the WB provided a loan to the state telephone monopoly with a provision the government could not allow private competition. When I confronted the responsible WB official, he said it was more important that the WB be paid back than that the people of Bulgaria have private competing telecoms (i.e., lower prices and better service). Even today, this is still too much of the mentality at the WB. There has been some improvement in oversight and transparency in recent years, but far too many WB projects are still poorly thought out, incompetent in administration, and, of course, corrupt.

When Paul Wolfowitz took over as World Bank president in June 2005, he made anti-corruption among the WB borrowers, contractors, and even bank employees a central priority. Of course, the corrupt governments and their supporters, the corrupt contractors, and even some bank employees complained. Mr. Wolfowitz then made the foolish mistake of giving several of the folks he brought with him and his girl friend (a WB official) big salary increases, thus undermining his anti-corruption campaign and setting himself up for slaughter by his enemies.

The WB is so inherently flawed it can neither be fixed nor justified on a reasonable cost-benefit basis. As the late development economist Peter Bauer explained, if the institutions and policies are right in a country, it can obtain all of the investment funds it needs from domestic and foreign private sources without foreign aid, and if the institutions and policies are not right, no amount of foreign aid can succeed. Knowing what we do now, the World Bank would never have been established in first place, and thus it should be abolished before it does any more damage.

The case of the IMF is more complex in that it has made major mistakes, e.g., forcing poor countries to increase taxes, and by being the lender of last resort to irresponsible countries adding to global systemic risk. But it has also had some successes, e.g., helping to establish the banking, financial and monetary systems in some of the former communist countries.

Its current problems stem from the fact the IMF obtains its operating funds from the loans it makes to governments in distress, and now that most of its big debtors have repaid their loans, the IMF income is hundreds of millions of dollars below its costs. During its fat days, the IMF engaged in almost endless and unnecessary mission creep and general bureaucratic bloat with far too many highly paid people.

If the IMF radically downsized and restricted itself to data collection, promoting orderly international payments and the expansion of trade, and some limited technical assistance (all which it could do with a tenth of its current staff and budget), it might be able to justify its continued existence.

Saying goodbye to the WB and much of the IMF is likely to have the same beneficial results that welfare reform had in the U.S. When governments, like individuals, have no choice but to take more responsibility for their own actions, most will.

Richard W. Rahn is chairman of the Institute for Global Economic Growth.

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