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IMF/World Bank Tokyo Meeting: No major outcome expected

By Pradumna B Rana

Synopsis

Nearly 20,000 financial leaders, international bankers, and senior bureaucrats will converge in Tokyo next week (12-14 October) for the annual meetings of the IMF and World Bank. Can we expect any major outcome?

Commentary

AS IN the past, the annual meeting of the International Monetary Fund and World Bank to be held in Tokyo this week (12-14 October 2012) will be accompanied by a lot a fanfare. Nearly 20,000 financial leaders, international bankers, and senior bureaucrats from the world over will gather in elegant halls and luxurious hotels for important meetings. However no major outcome can be expected from this year's IMF and World Bank talkfest.

2010 Governance and Quota Reforms

All attention is on whether the 2010 Governance and Quota Reforms of the IMF will be ratified and become effective. Such a move will finally shift quota shares in the IMF in favour of emerging markets and developing countries so as to recognise their increasing role in the global economy and give them a greater say in running the institution. During the past few decades, world trade and GDP shares of emerging markets and developing countries have risen more rapidly than their share in IMF quotas leading to fundamental questions regarding the representativeness and legitimacy of the IMF. For example, Brazil, China, and India together have fewer votes in the IMF than Belgium, Italy, and the Netherlands collectively, although the former's share in world GDP (measured in purchasing power parity) is four times greater.

Can the proposed quota increases be approved at the Tokyo meeting? Most probably, not. According to the latest information available from the IMF, as of 4 October 2012, 131 members having 75.01 per cent of the total quota had ratified the increase. Although this meets the required threshold for effectiveness (which is the consent of membership accounting for over 70 per cent of the total quota), the quota increase cannot be effective until the Board Reform Amendment – which, among others, proposes that Europeans give up two chairs at the IMF Board - also enters into force.

As of 4 October 2012, 114 members having 67.27 per cent of total quota had accepted the latter amendment, well short of the required 85 per cent. The US has yet to ratify the amendment. Linking the two ratifications shows how decisions are made in the IMF and illustrates the difficulties in reforming the governance of the IMF.

It supports the view of many who argue that reform of IMF governance proceeds at a glacial pace.

IMF is doing its best, but....

In fairness, it is not that the IMF is not making the effort. At the IMF annual meeting in Singapore six years ago, the members had agreed to a package of reforms to be completed over a two-year period. This resulted in the April 2008 quota and voice reform which was labelled by the IMF Management as “far-reaching reforms” of the institution aimed at rebuilding its “creditability and legitimacy”. Again on November 2010, as part of the 14th General Review of Quotas, the IMF Management announced what it labelled as “the most fundamental governance overhaul in the Fund’s 65-year history”. This comprised a proposal to shift 6 per cent of the quota to dynamic emerging markets and developing countries.

The main reason why it is difficult to reform governance of the IMF is that it is a relatively inflexible organisation. It is a club in the sense that it produces a good/benefit (financial stability) that is both non-excludable and non-rivalrous in that individual countries cannot be excluded from use and where use by a country does not reduce availability to others. Like many other clubs it is designed to retain firm control in the hands of the founding members and is not open to allowing new members in its governance system.

The governance of the IMF was designed in the interest of the original core members (led by the United States) in 1944 and places strict limits on change as membership expands. In comparison with the 44 countries that participated at the Bretton Woods conference, the membership of the IMF now stands at 188. The world is also fast becoming multi-polar with the rise of emerging markets, particularly those in Asia (China and India).

However, even with the ratification of the April 2008 quota reform, the quota share of emerging markets and developing countries will increase by only 1.1 per cent. Another 2.8 per cent reallocation will occur when the 2010 agreement is ratified. Quota misalignments will, therefore, remain, but at a lower level. China would rank number three in the world in terms of IMF quota shares behind the US and Japan. But Italy with half the GDP share (in market exchange rates) of India would have a quota share which is 11 per cent higher. Indonesia which ranks 15th in world GDP share, would rank 21st in terms of IMF quota shares.

More decentralised monetary architecture

An important consequence of the slow progress in reforming the governance of the IMF is the move from a centralised to a more decentralised global monetary architecture where various regional initiatives work closely with a “senior” global institution. We are already witnessing the evolution of a multi-layered global financial safety net. The IMF is accepted as the “senior” institution, with various regional financial safety nets in existence such as the European Financial Stability Mechanism and European Stability Mechanism in Europe, the Arab Monetary Fund in the Gulf region, and the Chiang Mai Initiative Multilateralisation and the ASEAN+3 Macroeconomic Research Office in East Asia.

Such a move, however, complicates the governance of the global economy. As emphasised by the G20, global and regional institutions should complement rather than compete with each other.

Pradumna B. Rana is Associate Professor in International Political Economy at the S. Rajaratnam School of International Studies (RSIS), Nanyang Technological University. He is also coordinator of economic multilateralism and regionalism studies at the RSIS Centre for Multilateralism Studies (CMS).