57. Multilateral Lending Agencies

Congress should

- reject proposals for more aid funds and new lending institutions and initiatives;
- terminate contributions to existing institutions, including the International Monetary Fund (IMF), the World Bank, and five regional multilateral lending agencies; and
- push to privatize or close all seven institutions.

As World War II came to a close, the United States took the lead in creating the IMF and the World Bank. In succeeding years Washington supported the creation of five regional development banks modeled after the World Bank and has consistently been the largest contributor to all of them. Although the lending agencies were touted as the answer to Third World poverty, they have proved to be expensive failures, doing more to retard than to advance economic progress throughout the developing world. At the same time, they have wasted billions in U.S. tax dollars and created a well-funded lobby devoted to the expansion of failed foreign-aid programs.

The International Monetary Fund

Perhaps the most controversial lending agency is the IMF. Originally created to help nations suffering balance-of-payments difficulties, the fund moved into the development business after President Richard M. Nixon closed the gold window in 1971. Nixon's move ended the international system of fixed exchange rates, thus eliminating the fund's function of managing that system.

The IMF lends money to governments in support of economic adjustment programs, which are theoretically intended to promote economic development. Unfortunately, little development is evident after more than

50 years of fund lending. Perhaps the best test of the effectiveness of the IMF is the number of troubled developing countries that have "graduated" because of its loan programs, which entail both money and advice. (Causation, not correlation, is the relevant standard of proof, since the fund has lent to most developing nations at one time or another.) Even friends of the organization have trouble pointing to many success stories. The fund itself acknowledges a declining compliance rate in recent years.

That is not surprising, since the organization has been subsidizing the world's economic basket cases for years, without apparent effect. Through 1993, 11 nations, including Egypt, India, Sudan, and Turkey, had relied on IMF aid for more than 30 years; 32 had been borrowers for between 20 and 29 years; and 41, almost one-fourth of the world's nations, had been using fund credit for between 10 and 19 years. While the organization now says it is tougher about cutting off nations that take its money and violate its loan conditions, it continues to let politics trump economics. Russia barely waited for the ink to dry on IMF agreements before announcing that it did not intend to keep them, but the fund has continued to send money to Moscow.

Of course, the IMF is not the only aid agency to act as a permanent dole for economic failures, but it has increasingly taken the lead in international lending. There are several problems with IMF activities, including the organization's reliance on inappropriate conditions and lack of effective enforcement. The main problem, however, is that foreign loans, whatever the formal conditions accompanying them, effectively subsidize the cause of borrowers' poverty when their economic policies are badly distorted. Among the fund's major clients have been Argentina, Brazil, Mexico, and (the now dismembered) Yugoslavia, all of which have promulgated anti-growth, dirigiste policies for decades despite IMF loan programs. That fund officials lack either a conscience or common sense is evident from the organization's support of the odious Ceaucescu regime in Romania and the Mobutu dictatorship in Zaire.

The World Bank

The record of the World Bank is similar. The bank, established in the aftermath of World War II along with the IMF to reorder the global economic system, was envisioned as a "lender of last resort" to assist developing countries only when the global capital markets proved inadequate. But over the years the institution has become even more profligate than the IMF, lending over $20 billion annually to countries, irrespective of their economic worthiness.

The bank was originally intended to help countries finance the infrastructure necessary to encourage private investment. However, bank policy changed dramatically during the 1960s and 1970s when the organization increased its lending 13-fold under its president Robert McNamara. Admitted one bank official at the time, "We're like a Soviet factory. The push is to maximize lending. The . . . pressures to lend are enormous and a lot of people spend sleepless nights wondering how they can unload projects. Our ability to influence projects in a way that makes sense is completely undermined."

The institution became the chief financier of government-led economic programs. During the 1970s the bank committed roughly 80 percent of its funds to public enterprises. There were, in fact, few money-losing state enterprises in such heavy borrowers as Argentina, Brazil, India, and Mexico that were not subsidized year in and year out by the bank. Today, poor nations are left with the job of cleaning up the consequences of their statist economic strategies. Indeed, many new, market-oriented governments are now attempting to privatize old, bank-funded mistakes.

Moreover, the bank has long promoted development at any cost, whether to human rights or to the environment. Like the IMF, bank officials never met a dictator they didn't like; the bank has provided assistance to Ceausescu's Romania, Mengistu's Ethiopia, and communist China. Bank funds underwrote the worst forms of social engineering, such as Julius Nyerere's coercive *ujamaa* program, which brutalized tanzanian peasants and devastated the nation's agricultural economy. The bank also supported Indonesia's forced transmigration project.

Unfortunately, the environment has not escaped unscathed. Bank-backed water programs have disrupted local ecosystems and forced millions of farmers off their land without compensation. Bank lending underwrote the destruction of the Brazilian rain forest; other bank-subsidized development projects promoted deforestation, desertification, and flooding around the globe.

Given that record, it should not be surprising that bank-funded projects failed in their essential purpose: promoting development. An internal Operations Evaluation Department report in 1987 conceded that "the Bank's drive to reach lending targets" had led to "poor project performance." In the same year, auditors judged more than one-third of the bank's rural lending projects, accounting for roughly half of total bank lending over the previous two decades, to be failures. Subsequent evaluations have documented a continuous record of projects that failed to meet expectations, were not sustainable, and left borrowing nations with little more than increased debt.

However, the bank's primary problem is not that it backs bad projects, though many are bad, but that it, like the IMF, has regularly underwritten governments that have had overall economic policies that preclude self-sustaining development. One bank evaluation found that 54 percent of agricultural projects studied were adversely affected by price controls and similar misguided regulations. Concluded the auditors, "It has become clear that it is not possible to implement viable projects in an unfavorable policy environment." Yet bank lending only increased in succeeding years.

To meet growing criticism of its record, in the 1980s the bank embarked on a program of so-called adjustment lending—policy-reform loans much like those offered by the IMF. But the bank is more interested in lending money than some nations are in borrowing it. A devastating internal study, the 1992 Wapenhans report, concluded that staffers were reluctant "to take a firm stand with Borrowers," preferring to ignore or waive noncompliance. As a result, "the high incidence of non-compliance undermines the Bank's credibility." Even bank senior vice president Ernest Stern was forced to admit that "time and again the best of policy intentions, the best of policy letters solemnly agreed to and signed by the finance minister and the Bank, broke down."

Of course, some countries have accepted bank adjustment loans and reformed their economies. But they received equally lavish funding before they reformed. In the end, countries will adopt politically painful reforms only if they possess the political will to do so. And they will generate that commitment only if forced to confront the high price of economic failure. For decades the bank has essentially handed alcoholic borrowers a fistful of $100 notes and told them to drink no more; after the money was squandered the bank demanded repayment. That policy has never worked, and it will not work in the future, even though bank officials now voice free-market rhetoric as readily as they issue checks.

A better reform model is provided by countries, such as the Soviet Union, that changed only when faced with the abyss of economic collapse. Countries determined to reform their economies don't need outside aid; those receiving outside aid will face less economic pressure to continue reforming. Sadly, the bank is not only wasting American taxpayers' money. It is hindering development in the very nations it says it wants to help.

The Regional Development Banks

Although the IMF and the World Bank are the leading lending agencies, five regional institutions have been created in the image of the latter: the African Development Bank, the Asian Development Bank, the European Bank for Reconstruction and Development, the Inter-American Development Bank, and the Middle East Development Bank. (The latter became operational only in November 1996.) Naturally, the United States is the largest contributor to every one.

The smaller development banks have all followed the same flawed lending policies as the World Bank. The African Development Bank wasted billions in some of the worst economic rat holes on earth while falling into administrative and fiscal chaos. The Inter-American Development Bank subsidized many of the same Latin American fiscal black holes underwritten by the IMF and the World Bank. The European Bank for Reconstruction and Development places greater emphasis on the private sector, but it spent most of its initial years of operation lavishing dollars on itself and has little to show for its efforts.

New *Schemes*

The fact that past lending has failed to promote economic growth has not slowed the profusion of plans for increased lending in the future. For instance, the G-7 has proposed creation of a new $50 billion fund, paid for by Western industrialized nations and run by the IMF, to subsidize nations, such as Mexico, that face financial crises. The multilateral lending agencies have developed a nearly $8 billion debt-relief initiative—which would require countries like the United States to forgive bilateral debt while the World Bank and the IMF offered new loans. Moreover, IMF head Michel Camdessus has proposed expanding borrowing rights from his organization by $36 billion and as much as doubling its capital, now $200 billion, and has pressed Washington to contribute $300 million for the fund's subsidized lending facility. The World Bank is preparing to push for another round of contributions to the International Development Association, a bank affiliate. The United States is committed to paying $234 million in arrears on a past capital increase for the Asian Development Bank and putting up 21 percent of the $1.25 billion in new capital for the Middle East Development Bank.

But none of those initiatives is likely to do any more good than did aid in the past. After all, there has been no shortage of foreign aid or commercial credit over the years, else poorer nations would not have been able to accumulate a $2.1 trillion debt. But that flood of cash has done nothing to promote development; to the contrary, much of the Third World has imploded while the number of development agencies has been increasing. Fully 70 developing states are poorer today than they were in 1980; 44 are worse off than they were in 1960.

Conclusion

Aid levels do not correlate with economic growth, and many recipients of the most foreign assistance, such as Bangladesh, Egypt, India, Sudan, and Tanzania, have been among the globe's worst economic performers. But the problem is not just that foreign assistance doesn't help. It almost certainly hurts. For years foreign aid from a multitude of sources has helped cover poorer countries' financial losses and sustain their economies, pushing off their days of reckoning. Today, Third World states are left with both huge debts and low growth. The answer is economic reform, not more foreign loans. Once reforms are in place, private credit and investment will follow naturally. The transition will, of course, be painful, but no amount of international lending, whether directly from the United States or from the IMF, the World Bank, or other development banks, can prevent that. Bad economic policies have to be made right.

Congress should end U.S. funding for all of those institutions. But that is not enough, since even without further American contributions the repayment of past loans would allow the lending agencies to continue lending tens of billions of dollars annually. Thus, the U.S. government also needs to push to privatize the organizations, like the IMF and World Bank, that might be viable and close down those, like the African Development Bank, that almost certainly are not.

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