IMF: Predatory lender or Latin America's best chance?

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Abstract

Recently, there has been heated debate as to whether or not assistance from the International Monetary Fund has proven to be a great humanitarian effort or a scheme by Western governments to keep emerging Latin American countries in debt. The IMF partners with numerous governments in order to create a collective monetary community from which all may benefit in times of need. These partnered countries are also able to apply for assistance if they find themselves in monetary hardships.

Some studies have shown that the IMF has been too heavy handed, while other studies have shown that recipient governments may misallocate these funds. I gathered economic variables such as; GDP annual growth, inflation rates, and unemployment rates from the IMF and the World Bank. Preliminary results show that when corruption is present and assistance is loosely structured there are frequently difficulties with finances later. These findings show that there is really no one entity to blame, but there are collective responsibilities that need to be addressed by both sides for success.

Introduction

Countries partnered with the International Monetary Fund often find themselves at odds with their benefactor and economically unstable. The partnered countries receive loans and emergency funds to help stabilize their own economic status: however, even after receiving these funds which are intendedto help stabilize their economy, the partnered governments are still in economic distress. What causes this? Are the loan agreements with the IMF too stringent, are the economic policies of the partnered countries too spend-thrift, or are the economic difficulties just part of the regular economic ebb and flow?

Globalization and its effects on the developing world have had its growing pains. Many Latin American countries are faced with poor living conditions a, poor infrastructure, and governments unable to deal with internal matters. These factors and the external pressures of international leaders on internal policy have only compounded difficulties for the various governments. I identify some of these issues and how they affect the Latin American states in regards to relationships with the International Monetary Fund.

Literature Review

There are numerous studies concerning the IMF and its Latin American partners. These studies attempt to identify what factors have causal effect on the partnered countries and their attempts at achieving a higher standard of living, economic growth, and overall development of the state.

Origins and Operations of the IMF

The IMF was developed during World War II and finally came into being December 27th of 1945. After World War II many countries suffering from the effects of the war found themselves in disastrous straits economically. Furthermore, fears from the economic climate of the great depression facilitated the need for more economic cooperation between countries.

The IMF was conceived in order to stabilize countries and their economies in order to create a more cohesive global economy. This stabilization effort extended to assistance with exchange rates and trade between countries. These efforts were to also have the added effect of improving poverty rates, economic growth, and economic security within the partnered country.

The IMF may have aspects of a bank; however it operates on the lines of a global cooperative. Its efforts, as seen by its supporters, are also seen as for the global economic good. The IMF is able to assist its partnered countries in a number of ways. It's able to assist with internal governmental policy and spending in order to streamline government, monitor governmental administration in regards to economic policy, and establish a lending relationship with partnered countries.

In regards to the establishment of the lending relationship it has with countries and their respective governments, the IMF is able to offer a variety of loan packages. Each country is evaluated on their respective needs and offered one of the packages that the IMF best suits the partnered countries interests and needs.

The packages (loan instruments) are described as “facilities” of which there are several varieties. These “facilities” range from the stringent conditionality to those encompassing little to no loan conditions. These facilities are; extended credit facility (ECF), standby credit facility (SCF), rapid credit facility (RCF), stand-by arrangements (SBA), flexible credit line (FCL), precautionary credit line (PCL), extended fund facility (EFF), and emergency assistance (IMF, 2011).

Perceptions of IMF Assistance

The IMF as partnered with the governments are able to extend these funds in order to aid the loaner country. However, problems and controversy arise when the conditionalities and loans take shape. Some view the conditions enforced by the IMF and the loans given to the developed countries as a way of spreading IMF influence. The advanced economies along with the IMF are also commonly accused of exploiting developing countries in Latin America.

Recent literature points out the myriad of reasons for partnered governments to make and accept IMF loans and conditions. In a study by James Vreeland and Adam Przeworski (2000), it’s explained that countries are in need of foreign capital or investment in order to remain economically viable. However, this is usually short lived and the loans only proponents are that of the government actually making the agreement. The citizenry are usually against such agreements as the ones that are made. Furthermore the terms of the agreements sometimes invoke dissent amongst the general population (Przeworski, Vreeland 2000).

Vreeland and Przeworski also go on to examine the data of the various IMF programs. However, the literature misses about half of the facilities named above. This is due to the study being a little older, with the IMF making changes to become more flexible with the partnered countries. More importantly their empirical study also points out that while any assistance between the IMF and the partnered country is a joint agreement, between the two. There are also questions as to how voluntary these agreements are.

In addition to the Przeworski and Vreeland study; further studies have shown that some of the issues with the agreements are those that concern structural adjustment. Structural adjustment refers to the policy of internal economics and administration streamlining (Stephens, 1999). This is done so as to minimize government costs without losing effectiveness and maximizing these savings in order to pay back loans and or promote economic growth. Included in this model is that of privatization of formerly public goals (i.e. pensions).

Government streamlining is nothing new in economics, however, with it has become an unwanted (by the populace) hallmark of IMF conditionalities. As countries and their respective governments inch towards a more social democratic state, they are spending more and more on entitlements that become cumbersome or and beyond their means. In a recent study by IrfanNooruddin and Joel Simmons (2006), it was found that the domestic cuts do affect the lower classes, but the IMF isn't the only party to blame. The study points out that political agendas and governments are also equally complicit when it comes to making domestic cuts (Nooruddin, Simmons 2006).

Evidence of this can be found in the example of Uruguay. James Vreeland (2000) examined the question of why governments enter into agreements with the IMF. It was discovered that Uruguay was attempting to push through complicated and unpopular spending cuts. The cuts were unable to garner much support in the legislature, but governmental proponents of the cuts found an ally in the IMF. They found that by taking the loan, they would be able to offer up the spending cuts as an IMF condition. Previous and concurrent legislation regarding the spending cuts had previously failed by a large majority voting against. In this manner, the executive of Uruguay was able to leverage the traditional legislation and budgeting processes.

Other examples of domestic spending cuts are those of social security programs. In a recent article in the *International Journal of Health Services*, It was found that social security along with programs for the elderly were suffering from the cut backs. This was in the form of medical care, social security, and pensions. The article puts the blame on the IMF and other multinational organizations using "aid" and health agendas as tools to entrench themselves into the developing countries by gaining so much influence on how the administration and economic policies are ran(Armada, Muntaner, Navarro, 2001).

Further complicating matters are the number of countries emerging from post military style governments and defense spending. Previous military governments would accept IMF loans and bolster theirgovernment by spending resources on the military. This in turn would repeat every so often, which created enormous amount of debt. Once the interim military

government would step down, elected governments found themselves with a high amount of debt and very few in solutions to counter the economic difficulties (Hagopian, 1993).

Conversely, some studies show that there are pre-existing problems before the IMF is even introduced into the equation. These may be from pre-existing inflation difficulties, unrelated global economic issues, and governmental changes. In a study by Barro and Lee (2005), it was found that governments may spend excessively after receiving IMF funds and that the programs themselves may encourage inefficiency in government (Barro, Lee, 2005).

At the end of the day there are quite a number of reasons Latin American countries enter into agreements with the IMF. They may range from genuine need and economic emergency to more subtle reasons within the machinations of regional politics and government. For whatever reason countries may have, they still enter into agreements and there are still going to be complications. If they have the need and the IMF is willing, than what choice do the partnered Latin American countries have?

ALBA: An IMF Alternative

Recently, Venezuela and Brazil have been spearheading regional projects that provide an alternative for Latin American countries. This is through the ALBA projects and the Bank of the South. ALBA is the Bolivarian Alternative for the Americas and the Bank of the South is a conglomerate based around Brazilian bankers. These economic bodies provide alternative resources for partnered and other Latin American countries to draw from.

Through resources (oil revenues) backed by the Venezuelan government, President Hugo Chavez was able to help create and drive ALBA into helping needy countries that they viewed were at the hands of the IMF. At a recent conference in Ottawa, Canada, a paper was presented outlining the views on international loaning and loaning alternatives. Included in this topic was insight on economics in the Western Hemisphere.

Under the guise of development and "aid" the North was perceived as exploiting the South monetarily. As they would receive loans for aid and development, Latin American and other developing countries would in turn have to give up far more in areas of trade, labor, resources, and interests on loans. In order to have actual long term growth, money would have to remain regional in order to circulate instead of traveling north to the advanced economies.

Also put forward was that the formation of the ALBA community and the Bank of the South was not the end, but merely the beginning. Latin America still needed to change its perceptions on their relationship with the North and see the inequities being exploited (i.e. "extraction of wealth from the South to the North"). Furthermore, the use of caution and with the new bodies from a critical position would also be emphasized. "We do not wish to substitute the rule of one group of northern capitalists by a group of southern ones." (Bendana, 2008, pp.6)

Remaining Questions

In conclusion, the literature reviewed for the issue was mixed. Some found that the IMF as an institution was performing poorly with its main goal of development and growth. Other

scholarly references found that countries were using the IMF to meet their own needs to push forward unpopular domestic agendas. Questions arise on whether or not there can be a middle ground or reasonable long term solution.

Do the answers lie in the passing of IMF policies and relaxing the conditionalities on domestic restructuring and interest payments or are there solutions in the area of public administration and government spending. In a perfect world these answers are obvious; unfortunately these issues are going to be complex.

With the perceived inequities involved on both sides, Latin American partnered countries have found themselves left with a bad taste of the IMF after dealings with the institution along with its lending and agreements. Conversely, the IMF have found themselves as an impromptu bill collector. In order to answer the questions posed it’s necessary to analyze the data in order to come to a valid conclusion instead of preconceived notions.

Methodology

After reviewing my sources and reading previous studies related to the IMF and Latin America, I found several resources. I found corruption levels used at Transparency International, statistical economic information at the World Bank, and the IMF respectively. From the literature and previous studies corruption and economic models had been utilized. Furthermore, corruption is a common source of government difficulties.I was also able to locate information from the CIA “World Factbook”. My units of analysis for the study are 32 countries from South America and the Caribbean also commonly referred to as Latin America.

In order to gain a solid foundation and for basic commonalities between the units of analysis (32 countries), I decided on using percentages on GDP growth, Inflation change in rate percentages, and change in unemployment rates. These three are the dependent variables in the study. The changes are measures in three separate intervals; as 1st year after receiving IMF assistance, 3rd year after receiving IMF assistance, and 5th year after receiving assistance.

This was done in order to see the immediate effect if any, and the proceeding years were taken if goals or growth were registered in subsequent years. This was done for each of the three variables from each of the units of analysis (32 countries). The information gathered is from the World Bank's (www.worldbank.org). The year chosen for each unit of analysis was chosen from the agreement date for IMF assistance and proceeded with the subsequent; 1st, 3rd, and 5th years.

This leads us to the source for the first of the independent variables. The IMF data site was used in order to ascertain the date and type of the agreement of assistance (www.imf.org). Also located at the IMF data site was the type of facility used by the partnered country. Each agreement, generically referred to as an IMF loan was modified into a dummy variable and assigned to each unit of analysis. The variable was labeled to the unit of analysis as 1 for participation in the IMF program and 0 for non-participation.

Further variables used in the study are government consumption as percentage of GDP, status of unit analysis having a prior military government, and corruption ratings as provided by Transparency International. The government consumption variable is an interval variable as percent and is taken from the World Bank data site (www.worldbank.org). Units of Analysis as

having a previous military government can be labeled as 1 for previously having a military government, and 0 for not. The corruption rating found at Transparency International is anindex of ratings put together by the group for statistics purposes. This ordinal variable rates the units of analysis from 0 to 10 with 0 having the most corruption and 10 being the least.

Hypothesis

In a comparison of individual countries in Latin America, those receiving stringent monetary loan agreements from the IMF will have a more troubled economy than those that do not. However, in order to have a larger and more comprehensive view on the matter we will introduce other variables on the matter. Independent variables such as; government consumption, and corruption will help clarify the matter.

Data and Findings

I use four Dependent Variables. They are; GDP growth, Inflation Growth, Unemployment, and Government Consumption listed as a percentage of GDP per unit of analysis.

I first used change in GDP growth percentage to observe any effects the countries may have experienced after receiving an IMF loan. To run data for my solution, I used an independent t test with the dependent variables against the IMF loan types. By running the t-

test I was able to observe each country and the change in GDP percentage after the IMF assistance had been given.

As we observe in Tables 1.1, the change in percentage GDP growth variable is seen as having varying effects for the different type of facilities. In some cases positive results are measured, but drop off at the end of the interval years. However, the Standby Facility, having the most countries reporting, has positive gains through the interval years. This is observed as the change in GDP rises from 2.9 to 5.5.

Tables 1.2 use the dependent variable of inflation. Some of the units of analysis vary greatly in their rates of inflation. However, if we take a look at the independent variables we can still see that inflation rates are taken under control. As we can see with the independent variable of IMFLNSCF in relation to units of analysis, there is a high rate of inflation at 49.2%. On a larger amount of countries, the same is true of the “Stand-by Facility” of IMFLNSTBY.

With two dependent variables down we next move onto the latter half of the study. In this portion we observe tables 1.3 in relation to the variable of unemployment. We are hoping that unemployment will fall with the input of funds from the IMF, thereby stimulating the economy. However, let’s see what happens to the unemployment rate after assistance from the IMF facilities are received.

The tables 1.3 shows us that the mean of percentages of the unemployment rate within the units of analysis. We can see that as a country uses assistance from the IMF, that country is not necessarily guaranteed lower unemployment from this perspective. We can see that in three cases (IMFLNEFF and IMFLNSAF) unemployment was lowered. However, the majority

showed rises in unemployment if they had received the IMF assistance or no change in unemployment.

As we move through our tables we can see that in our government consumption table of 1.4, we are able to observe the effects of government consumption in relation to our independent variables of the IMF facilities. As the IMF, wishes to assist countries and their respective governments with budgeting, and find out how the best way to minimize excess spending. They (IMF) usually have stipulations that governments must adhere to in order to receive assistance.

This streamlining and stabilization effort ideally wants the partnered country/government to minimize costs in government programs and unneeded expenditures or employments. However, when we examine the data in table 1.4, we can see that government spending varies very little from those governments that do not accept the assistance offered from the IMF. With respect to the facility/variable IMFLNSCF most of the independent variables show that are serious changes in government spending.

What does this mean? Before we answer that lets talk about some of the effects on our two other variables. The independent variables of the military government showed no significant results in this study in regards to our dependent variables. However, when we controlled for corruption using the CPI score from Transparency International there was significance at the .10 level through most of the levels of the dependent variables. As our scores for our dependent variable grew worse we also observed that our scores for the CPI measure were low to negative, indicating corruption.

Summary and Conclusions

Now that we have our variables and data in hand let's try to sort out what we have found. As we have observed through our independent variables and their relation to the dependent variable, we can see that there were some gains with particular facilities. This is seen in change in GDP percentage and the inflation variable.

However, on the other side of the coin we can also see that when the countries (units of analysis) did accept and use the IMF facility, they did very little with modest or no attempts at curbing government spending. In a lot of cases they spent more, after receiving the stimulus from the facility. Furthermore, the unemployment dependent variable had very little change through the data.

What does all this mean? How can anyone fix this quagmire? It means that the IMF is going to have to take a greater interest, not just monetarily, but to form a real partnership with realistic goals. The IMF and the partnered governments need to make longer terms and capitalize on current gains. The IMF is going to need to adjust its structural terms with regards to each individual partner. The partnered government should also see itself as a partner wanting to make the needed and right changes instead of propping itself up with borrowed money.

Tables Index

Table Series 1.1

Table 1.1a Difference of Mean Change in GDP (as %) year 1

IMF Facility	Recipient	Non-Recipient	Difference
Emergency Fund	4.2 (1)	2.5 (26)	+1.7
Standby Credit	2.5 (4)	2.5 (23)	0
Flexible Credit Line	2.4 (1)	7.1 (26)	-4.7
Structural Adjustment	-2.3 (2)	2.9 (25)	-5.2
Standby Credit with Supplemental Reserve	4.4 (3)	2.3 (24)	+2.1
Extended Credit	4.4 (6)	2.0 (21)	+2.4
Standby Arrangement	2.9 (20)	1.4 (7)	+1.5

Table 1.1b Difference of Mean Change in GDP (as %) year 3

IMF Facility	Recipient	Non-Recipient	Difference
Emergency Fund	2.8 (1)	4.2 (24)	-1.4
Standby Credit	6.3 (4)	4.8 (21)	+1.5
Flexible Credit Line	8.6 (1)	4.2 (24)	+4.4
Structural Adjustment		4.0 (25)	
Standby Credit with Supplemental Reserve	5.0 (2)	4.5 (22)	+0.5
Extended Credit	4.8 (6)	5.3 (19)	+0.5
Standby Arrangement	5.0 (20)	4.0 (5)	+1.0

Table 1.1c Difference of Mean Change in GDP (as %) year 5

IMF Facility	Recipient	Non-Recipient	Difference
Emergency Fund		4.4 (23)	
Standby Credit	4.9 (4)	4.3 (19)	+0.6
Flexible Credit Line	5.2 (1)	4.4 (22)	+1.2
Structural Adjustment		4.4 (25)	
Standby Credit with Supplemental Reserve	5.8 (3)	4.2(20)	+1.6
Extended Credit	1.6 (6)	5.4 (17)	-3.8
Standby Arrangement	5.5 (18)	0.3 (5)	+5.2

Source: World Bank and International Monetary Fund

Table Series 1.2

Table 1.2a Difference of Mean Inflation (%) year 1

IMF Facility	Recipient	Non-Recipient	Difference
Emergency Fund	11.5 (1)	15.3 (27)	-3.8
Standby Credit	49.2 (4)	9.4 (24)	+39.8
Flexible Credit Line	3.0 (1)	15.6 (27)	-12.6
Structural Adjustment	4.8 (2)	15.9 (26)	-11.1
Standby Credit with Supplemental Reserve	7.1 (3)	16.1 (25)	-9.0
Extended Credit	10.2 (6)	16.5 (22)	-6.3
Standby Arrangement	17.2 (21)	9.0 (7)	+8.2

Table 1.2b Difference of Mean Inflation (%) year 3

IMF Facility	Recipient	Non-Recipient	Difference
Emergency Fund	4.7 (1)	9.9 (27)	-5.2
Standby Credit	23.0 (4)	7.5 (24)	+15.5
Flexible Credit Line	2.3 (1)	10.0 (27)	-7.7
Structural Adjustment	3.3 (2)	10.2 (26)	-6.9
Standby Credit with Supplemental Reserve	10.2 (3)	9.6 (25)	-0.6
Extended Credit	8.3 (6)	10.1 (22)	-1.8
Standby Arrangement	10.1 (21)	7.0 (7)	+3.1

Table 1.2c Difference of Mean Inflation (%) year 5

IMF Facility	Recipient	Non-Recipient	Difference
Emergency Fund	7.9 (1)	8.1 (27)	-0.2
Standby Credit	14.3 (4)	7.2 (24)	+7.1
Flexible Credit Line	8.4 (1)	3.2 (27)	+5.2
Structural Adjustment	3.0 (2)	8.6 (26)	-5.6
Standby Credit with Supplemental Reserve	8.8 (3)	8.1 (25)	+0.7
Extended Credit	5.7 (6)	8.9 (22)	-3.2
Standby Arrangement	9.1 (21)	5.4 (7)	+3.2

Source: World Bank and International Monetary Fund

Table Series 1.3

Table 1.3a Difference of Mean Unemployment (%) year 1

IMF Facility	Recipient	Non-Recipient	Difference
Emergency Fund	3.9 (1)	12.2 (18)	-8.3
Standby Credit	15.6 (4)	10.8 (15)	+4.8
Flexible Credit Line	(0)	(19)	
Structural Adjustment	8.7 (2)	12.1 (17)	-3.4
Standby Credit with Supplemental Reserve	12.7 (3)	11.6 (16)	+1.1
Extended Credit	13.2 (1)	11.7 (18)	-1.5
Standby Arrangement	12.3 (15)	9.6 (4)	+2.7

Table 1.3b Difference of Mean Unemployment (%) year 3

IMF Facility	Recipient	Non-Recipient	Difference
Emergency Fund	4.6 (1)	11.6 (18)	-7.0
Standby Credit	13.9 (4)	10.4 (15)	+3.5
Flexible Credit Line	(0)	(19)	
Structural Adjustment	8.0 (2)	11.6 (17)	-3.6
Standby Credit with Supplemental Reserve	11.8 (3)	11.1 (16)	+0.7
Extended Credit	9.8 (1)	11.3 (18)	-1.5
Standby Arrangement	12.0 (15)	8.2 (4)	+3.8

Table 1.3c Difference of Mean Unemployment (%) year 5

IMF Facility	Recipient	Non-Recipient	Difference
Emergency Fund	4.4 (1)	11.2 (18)	-6.8
Standby Credit	13.2 (4)	10.2 (15)	+3.0
Flexible Credit Line	(0)	(19)	
Structural Adjustment	7.0 (2)	11.3 (17)	-4.3
Standby Credit with Supplemental Reserve	11.2 (3)	10.8 (16)	+0.4
Extended Credit	10.7 (1)	10.8 (18)	-0.1
Standby Arrangement	11.3 (15)	9.1 (4)	+2.2

Source: *World Bank and International Monetary Fund*

Table Series 1.4

Table 1.4a Difference of Mean Government Consumption (as % of GDP) year 1

IMF Facility	Recipient	Non-Recipient	Difference
Emergency Fund	17.6 (1)	12.9 (25)	+4.7
Standby Credit	11.5 (4)	13.3 (22)	-1.8
Flexible Credit Line	20.5 (1)	12.7 (25)	+7.8
Structural Adjustment	13.2 (2)	13.0 (24)	+0.2
Standby Credit with Supplemental Reserve	14.8 (3)	12.8 (23)	+2.0
Extended Credit	13.5 (6)	12.9 (20)	+0.6
Standby Arrangement	12.8 (19)	13.7 (7)	-0.9

Table 1.4b Difference of Mean Government Consumption (as % of GDP) year 3

IMF Facility	Recipient	Non-Recipient	Difference
Emergency Fund	18.0 (1)	13.0 (23)	+5.0
Standby Credit	12.7 (4)	13.3 (20)	-0.6
Flexible Credit Line	19.3 (1)	13.0 (25)	+6.3
Structural Adjustment	(0)	13.2 (24)	
Standby Credit with Supplemental Reserve	14.5 (3)	13.1 (21)	+1.4
Extended Credit	13.9 (6)	13.0 (18)	+0.9
Standby Arrangement	13.0 (19)	14.0 (5)	-1.0

Table 1.4c Difference of Mean Government Consumption (as % of GDP) year 5

IMF Facility	Recipient	Non-Recipient	Difference
Emergency Fund	(0)	13.0 (22)	
Standby Credit	11.9 (4)	13.0 (18)	-1.1
Flexible Credit Line	20.5 (1)	12.5 (25)	+8.0
Structural Adjustment	(0)	8.6 (24)	
Standby Credit with Supplemental Reserve	14.8 (3)	12.5 (19)	+2.3
Extended Credit	14.3 (5)	12.4 (17)	+1.9
Standby Arrangement	12.5 (18)	14.4 (4)	-1.9

Source: *World Bank and International Monetary Fund*

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