

## International

The New York Times  
ON THE WEB

[Home](#)[Site Index](#)[Site Search](#)[Forums](#)[Archives](#)[Marketplace](#)

Click here for:

The New York Times  
ON THE WEB  
**Learning Network**  
www.nytimes.com/learning

October 2, 1998

# I.M.F. Role in World Economic Woes Is Hotly Debated

---

### Related Articles

- [Rubin Urges More Disclosure in Global Finance](#)
  - [I.M.F. Lets Its Rule on Full Repayment Slip](#) (Aug. 26)
  - [Second-Guessing the Economic Doctor](#) (Feb. 1)
- 

By DAVID E. SANGER

**W**ASHINGTON -- When the world's finance ministers and central bankers gathered last year in Hong Kong, they nervously congratulated each other for containing -- at least for the moment -- a nasty financial brush fire in Asia. In a year's time, many predicted in hallway chatter, the troubles in Thailand and Indonesia would look like a replay of Mexico in 1995 -- a rough bump in the road for a world enjoying remarkable prosperity.

Talk about bad market calls. Twelve months later, as the same financial mandarins clog Washington with their limousines and glide through endless receptions at the annual meeting of the International Monetary Fund and the World Bank, just about everything that could have gone wrong in the world economy has: the worst downturn in Japan since World War II, economic meltdown in Russia, a depression in Indonesia that is plunging 100 million people below the poverty line, and deep fears over what happens next in Latin America.

What makes this year's IMF meeting most remarkable, though, is that the harshest criticisms are directed at the monetary fund itself, and, by extension, at the U.S. Treasury, which is viewed as the power behind the IMF.

This year, in place of confident predictions, there are mutual recriminations. Arguments are breaking out over whether the true culprits were crony capitalists and weakened leaders like Russian President Boris Yeltsin, or huge investors who poured money into the world's emerging markets with reckless abandon in the mid-1990s and panicked in the past 12 months.

Whatever the reason, one reality prevails: Hundreds of billions of dollars have fled from economies on four continents -- seeking the safest havens possible, often in the United States -- and the money is not returning anytime soon.

And the subtext of every seminar on capital flows and every conclave of nervous ministers will be some painfully blunt questions: Can this be stopped? Or is the world headed for a global recession?

Fifty-three years ago the IMF was created after the Bretton Woods conference which sought to stabilize the world economy and secure the peace after World War II. Now it is under attack from all sides, charged not only with worsening a bad situation by misjudging the economics, but with being politically tone-deaf in some of the most volatile capitals in the world, from Jakarta, Indonesia, to Moscow. For the first time, there are disturbing questions about whether the institution itself is still capable, financially or politically, of containing the kind of economic contagion that caught the world unaware.

Once, the IMF's critics were largely found in Africa and South Asia, where the fund was often viewed as arrogant; today they include Wall Street's biggest players and top officials in the most powerful economies of Asia and Europe.

Only a few -- including former Secretary of State George Schultz and members of Congress who are increasingly suspicious of all international institutions -- are talking about scrapping the IMF altogether. But almost everyone is talking about creating a "new financial architecture" that can do what the old one clearly cannot: smother financial wildfires before they leap around the globe.

President Clinton, British Prime Minister Tony Blair and other leaders, after months of silence, have edged into the debate, in some cases wresting the issue for the first time from their finance ministers and central banks. Their fear, their advisers say, is that 15 months of financial turmoil are now threatening political stability.

The blunt-speaking Prime Minister of Singapore, Goh Chok Tong, recently described the cost of failure in stark terms that both Clinton and Treasury Secretary Robert Rubin have avoided. "A prolonged economic downturn in Asia will revive latent tensions against the West," he warned.

Such concerns have turned this year's meeting into a tumbled mass of worries and a groping for short and long-term solutions. The Japanese, the French, the Southeast Asians are all arriving in Washington with different diagnoses of what went wrong, and different solutions about how to set it right. The United States has its own set of plans, a mix of suggestions to force more disclosure of financial data in countries around the world and to impose more American-style financial standards and regulation.

Meanwhile, an ideological argument is breaking out over whether the world should slow down a long march toward more free and open markets -- a strategy pressed by the Clinton administration for the past six years. Others

argue that it is unwise to start rebuilding the hospital while the patients are still on the operating tables.

"Last year the standard answer that all of us were given came down to this: 'We have the IMF and the World Bank, and they know best,'" Indonesian Foreign Minister Ali Alatas said over breakfast in Washington the other day, reflecting on how the crisis turned 30 years of astounding growth in his country into an overnight depression.

"Then they said everything that went wrong was our fault," he said. "But now, now I think people know that much of the problem came from the outside, and we need something better."

And the IMF itself is beginning to fight back, an awkward role for an institution dominated by Ph.D. economists who are unaccustomed to being openly challenged.

"Every place you turn you read the same story, that we came in, that we made things worse," said Stanley Fischer, the deputy managing director of the fund, who was born in Northern Rhodesia -- now Zambia -- and became chairman of the Massachusetts Institute of Technology's economics department before taking a job that has now put him in the center of the financial storm.

"We frequently get the blame, some of it well-deserved," he said. "But it is politically convenient for governments around the world to cry, 'The IMF made us do it,' and pin their mistakes on us. That's fine. We'd rather be loved, but more than that we'd like to be effective."

## **MISCALCULATIONS, POLITICS AND SAFETY NETS**

On a steaming January day, Michel Camdessus, the IMF's top official, slipped into Jakarta to the private residence of President Suharto and sat down for a four-hour meeting to tick off, line by line, the huge reforms Indonesia would have to implement in return for tens of billions of dollars in emergency aid. Two previous deals had collapsed when Suharto ignored the fund's conditions, so Camdessus insisted that he strike a deal directly with Suharto, then Asia's longest-serving leader.

It was a meeting of men who knew different worlds of power politics: Suharto rose as a general in central Java, and Camdessus had detonated mines in Algeria for the French army before entering the French Treasury on his way to becoming head of France's central bank.

"It was all there," a senior IMF official recalled. "He was told he had to dismantle the national airplane project, the clove monopoly, all the distribution monopolies."

At one point, Camdessus looked at the impassive Suharto and said, "You see what this means for your family," a reference to their vast investments in the

country's key industries.

"He said, 'I called in my children, and they all understand.'"

But within months, that exchange in Jakarta came to symbolize the IMF's twin troubles: Its inability to understand and reckon with the national politics of countries in need of radical reform, and its focus on economic stabilization rather than the social costs of its actions.

Suharto had no intention of fulfilling the agreement. It was, one of his former Cabinet members said, "a delaying move that was obvious to everyone except Camdessus."

Perhaps one reason why the IMF sometimes appears tone-deaf is that its senior staff is almost entirely composed of Ph.D. economists. There are few officials with deep experience in international politics, much less the complexities of Javanese culture that were at work in Indonesia. Historically, experts in politics and security have gravitated to the United Nations, development experts to the World Bank, and economists to the IMF -- creating dangerous gaps in a crisis like this one.

As a result, the fund had only a rudimentary understanding of what would happen if its demands were met and all Indonesia's state monopolies were quickly dissolved. While that system lined the pockets of the Suhartos and their friends, it also distributed food, gasoline and other staples to a country that stretches for 3,000 miles over thousands of islands. To help balance the budget, the fund demanded a quick end to expensive subsidies that keep the price of food and gasoline artificially low.

But that, combined with the huge currency devaluation that sparked the crisis, resulted in high prices and shortages that fueled riots that continue to this day, as millions of Indonesians lose their jobs.

The IMF -- unintentionally, its officials insist -- also sped Suharto's resignation, insisting on the elimination of "crony capitalism," code words for removing the Suharto family from the center of the economy. Ultimately, that may prove to be Indonesia's salvation, if the new government can contain the rioting against the ethnic Chinese minority -- whose money is desperately needed to save the country's fast-shrinking economy.

"It is worth noting," Fischer said this week, "that our programs in Asia -- in Indonesia, Korea and Thailand -- only took hold after there was a change in government."

Nonetheless, the Indonesia experience has revived the argument that the IMF is so focused on stabilizing banks and currencies, on preventing capital flight and freeing up markets, that it is blind to the social costs of its actions. Among the toughest critics has been its sister institution, the World Bank, whose main charge is alleviating poverty.

"You've seen the tension almost every day," one senior World Bank official said recently. The bank has gone to extraordinary lengths in recent months to differentiate its role from that of the fund, and to announce a tripling of aid to the poorest in the countries hit by the economic chaos.

Even U.N. Secretary General Kofi Annan has joined the argument, warning in a speech at Harvard recently that "if globalization is to succeed, it must succeed for poor and rich alike. It must deliver rights no less than riches. It must be harnessed to the cause not of capital alone, but of development and prosperity for the poorest of the world."

IMF officials say they are changing strategies when they see they are exacting too great a social cost.

"It's a very difficult formula to get exactly right," Fischer said in August, as Russia was teetering and the IMF was sending in \$4.8 billion in aid that was rapidly wasted. "You need enough discipline to send the right message to the markets and keep investors from fleeing. But you need enough leeway to keep people from suffering more than they otherwise would."

In recent months, he noted, the IMF has allowed more spending to sustain subsidies for basic goods for longer periods in Indonesia, Korea and elsewhere.

"There is a new flexibility at the IMF" a senior Indonesian official concluded recently. "It is a lot better."

### **A U.S. PAWN, OR A RUNAWAY AGENCY?**

The Clinton administration admits that the IMF has many failings, many of them on display this year. But it insists that the world has gone through global financial crises without an IMF once before in this century -- and the result was the 1930s.

"I have no doubt the situation over the past year would have been much worse -- with greater devaluations, more defaults, more contagion, and greater trade dislocations -- without the program agreed with the IMF and the finance it has provided," Deputy Treasury Secretary Lawrence Summers told Congress last week.

Many Republicans and some Democrats are unconvinced. Even though the Senate has overwhelmingly approved an \$18 billion contribution to the fund to help it fight new crises, the House defeated that measure two weeks ago. The fund's last hope of getting the money, which will free up nearly \$100 billion in contributions from other nations waiting for the United States to act, will come when the House and Senate try to resolve their budget differences in a conference committee in the next 10 days.

A rejection, Rubin insists, would send a message around the world that the

United States is turning its back on the one institution charged with restoring economic stability.

Everywhere else in the world, though, politicians and businessmen insist that one of the biggest problems with the IMF is that, contrary to the view of Congress, it acts as the U.S. Treasury's lap dog. Ask in Jakarta or Moscow, and the response is the same: The IMF never ventures far without looking back for the approving nod of its master.

That view may not be far wrong. In ordinary times, the United States largely leaves its hands off, as the IMF's executive board -- made up of 24 representatives of the 182 member nations -- delve into the intricacies of budget policy in Greece or banking regulation in Argentina. "Surveillance" of the world's economies is the fund's main activity.

When the United States weighs in, however, is when the IMF is called on to rescue a country in deep trouble. Only then does the IMF -- and the U.S. Treasury -- have the leverage to extract commitments in return for billions in aid. In theory, the U.S. influence is limited: It has an 18.5 percent vote in the fund. Germany, Japan, France and Britain have about 5 percent each. But in practice the United States usually gets its way, exercising its influence behind the scenes, often in interactions between Fischer and Summers.

The two met when Fischer was on the MIT faculty and Summers was a graduate student taking one of his classes, later becoming a colleague at MIT. Each served as chief economist of the World Bank. It was Summers who was instrumental in placing Fischer in the fund's no. 2 job, and these days they talk constantly.

"It's usually a warm relationship," Fischer said this summer. "Remember, this is a job where you cannot turn to outsiders for advice -- you can't call the chief economist at a Wall Street firm, or even many of your academic friends, because so many of the issues are confidential."

The Treasury's relations with Camdessus are often more strained as he plays the role of world diplomat, traveling the globe and trying to coax along political leaders. The tensions were obvious from the start of the Asia crisis. The fund made little secret of its displeasure that the United States was not offering direct aid to Thailand, a major U.S. ally, as a sign of support and confidence.

Mindful of the backlash in Congress when Mexico was bailed out with U.S. money, that was the last thing the Treasury planned to do. Summers, in turn, thought the fund was not forcing the Thais to implement its reform commitments rigorously enough or disclose their true financial picture. Within the U.S. government there was other dissension: The State and Defense Departments felt the United States should do more for Thailand, but backed off when the Treasury asked if they would like to pony up some aid out of their own budgets.

There were other conflicts. When Japan used the last IMF meeting to propose setting up a \$100 billion "Asia Fund" -- one that would exclude the United States and would probably offer aid under much more relaxed conditions than the IMF does. Rubin called up Camdessus at breakfast one morning and told him that the Japanese proposal would undercut the IMF's authority.

"We've just had a dispute with Michel," Rubin reported to his aides as he returned to his orange juice and croissant. One of them shot back: "And it's only 8 a.m."

Camdessus backed down at Rubin's insistence and walked away from money that Asia could have used. Japan says it will be back with a similar proposal this weekend, this time for a \$30 billion fund.

Camdessus has also rankled U.S. officials with statements that amounted to cheerleading to reassure the markets -- sometimes in the face of the facts. In June, with Russia on its way to collapse, Camdessus declared that "contrary to what markets and commentators are imagining" about the slow collapse of Russia's economy, "this is not a crisis. This is not a major development."

The bailouts of Russia and South Korea were prime examples of how Washington muscled into the IMF's turf as soon as major U.S. strategic interests are involved.

Last Christmas, as South Korea slipped within days of running out of hard currency to pay its debts in December, it sent a secret envoy, Kim Kihwan, to work out a rescue package. "I didn't bother going to the IMF," Kim recalled recently. "I called Summers' office at the Treasury from my home in Seoul, flew to Washington and went directly there. I knew that was how this would get done."

Within days the Treasury dispatched David Lipton, its most experienced veteran of emergency bailouts, who is leaving his post as undersecretary for international affairs this month, to shadow the IMF staff's negotiations with the government in Seoul.

Fischer was displeased. "To make a negotiation effective, it has to be clear who has the authority to do the negotiating," he said.

### **WHO LOST RUSSIA?**

The pattern was repeated this summer, when the United States raced to put together a \$17 billion package for Russia. The IMF's staff in Moscow declared that Russia needed no money at all -- it just needed to enact policies that would restore confidence in investors. The Americans and Germans came to a different conclusion.

Soon after, U.S. officials gathered in the White House situation room to consider what might happen to Russia if the ruble was devalued and market

reforms collapsed and to push the IMF to come up with emergency money. So the fund began assembling a last-ditch program to prop up a country that had resisted its reform plans for seven years.

Camdessus, though, was still hesitant, questioning whether the IMF should risk its scarce resources in Russia. "We had to pull Michel along," a senior Treasury official recalled.

As it turned out, Camdessus' instincts were right while the approach championed by Rubin and Summers proved disastrously wrong. The first installment of that payment -- \$4.8 billion -- was wasted, propping up the currency long enough, in the words of one IMF official, "to let the oligarchs get their money out of the country." Then Yeltsin reversed his commitments, let the ruble devalue anyway, began printing money with abandon and fired virtually every reformer in his government -- resulting in a collapse of the IMF agreements and the indefinite suspension of its aid program.

Now, inside the IMF and on Capitol Hill, there are recriminations over "who lost Russia."

Publicly, Fischer argues that "there are no apologies owed for what we attempted in Russia." But some IMF officials complain privately that they let Rubin and Summers run roughshod over them, striking a deal that fell apart within weeks as the Russian parliament rebelled and Yeltsin backed away from his commitments.

Summers responds that the United States "took a calculated risk" because "it was vastly better that Russia succeed than not succeed."

The Russian collapse touched off new rounds of economic contagion, with investors fleeing Latin America, and triggering huge losses in hedge funds like Long Term Capital, the Greenwich, Conn., investment firm that needed to be rescued by Wall Street powerhouses whose money it had invested.

"Russia was a turning point," said Robert Hormats, the vice chairman of Goldman, Sachs & Co. "It made the world realize that some countries can fail, even if the IMF and the Treasury intercede. And that changed the perception of risk."

Now, as the countries meet to face a future that the IMF has warned could be very bleak, they need to reverse those perceptions, or watch countries slowly starve for lack of capital. The emerging markets are calling for controls on short term investments. The French want a stronger IMF. The Americans say the answer is more disclosure, so that investors are better warned, and tougher regulation.

"These are usually nice, quiet meetings; everyone very polite," a top U.S. official said earlier this week. "Not this year."

### Other Places of Interest on The Web

- [International Monetary Fund -- World Bank Group 1998 Annual Meetings.](#)

<a href="#">Click Here</a>
The New York Times on the Web <b>LearningNetwork</b> <a href="http://www.nytimes.com/learning">www.nytimes.com/learning</a>

[Home](#) | [Site Index](#) | [Site Search](#) | [Forums](#) | [Archives](#) | [Marketplace](#)

[Quick News](#) | [Page One Plus](#) | [International](#) | [National/N.Y.](#) | [Business](#) | [Technology](#) |  
[Science](#) | [Sports](#) | [Weather](#) | [Editorial](#) | [Op-Ed](#) | [Arts](#) | [Automobiles](#) | [Books](#) | [Diversions](#) |  
[Job Market](#) | [Real Estate](#) | [Travel](#)

[Help/Feedback](#) | [Classifieds](#) | [Services](#) | [New York Today](#)

[Copyright 1998 The New York Times Company](#)