New School Economic Review, Volume **4**(1), 2010, 87-91

THE IMF AND THE GLOBAL FINANCIAL CRISIS[1]

Ilene Grabel

I will analyze here the incoherence in the response of international institutions to the current crisis, and focus on the window of opportunity that this has opened for progressive thinking and policy-making. Things have been bleak for the Left in the past decades, and in this context it is quite understandable for all of us to not recognize change when it presents itself or at least when it becomes possible. This is true for all of us who have railed for so long at the extension of neoliberalism across the developing world at the hands of the IMF, the World Bank, the economics profession, the United States government, and neoliberal reformers in the developing world. All of these agents have collectively been a very powerful juggernaut. It is against that background that those wishing for change failed to recognize, let alone take hope in, any signs announcing it, and I think we could forgive ourselves if the stakes were not so high. But the matter of whether change is underway is so crucial that we can't afford to be complacent at the present juncture.

The pessimism resulting from these decades of neoliberal policies may lead progressives to discount far too readily evidence of aperture that I think could be exploited to bring out the kinds of changes in policies and ideas that the developing world so badly needs. I think at this juncture it is important to guard against premature conclusions suggesting that nothing has and nothing will change. In this spirit I will argue here that what we are seeing now is a chaotic response to the current global crisis by the IMF and even by national governments, and that this chaotic response to the global crisis represents a historical moment of what I call productive incoherence. That productive incoherence has displaced the constraining neoliberal coherence of the past several decades. By this idea of productive incoherence I am referring to the proliferation of responses to the crisis by national governments and by multilateral institutions that to this point has not congealed into any sort of consistent strategy or regime. And so by invoking this concept of incoherence what I hope to signal is the absence of a unified consistent and universally applicable response to the crisis.

The responses to the financial crisis that are emerging around the globe show both substantial continuity with neoliberalism, and at the same time reveal a much greater degree of discontinuity with neoliberalism than we have seen before. For so many of us at this conference who have worried about neoliberalism as a straightjacket constraining policy space in developing countries, this new emerging incoherence may signal the beginning of the end of neoliberalism. Again, I think it is very important that we do not prejudge the historical moment as one of continuity, but rather we should see it as one of aperture and of rupture. There are many different ways of thinking about how his incoherence has manifested itself and I want to mention some of these ways today.

Last week the IMF released two studies that throw some light on the ways that the crisis is causing mainstream economists to question some of their widely held beliefs. In one paper a group of Fund economists argued that central banks should adjust upward the acceptable target of inflation from the two percent that has been invoked during much of the neoliberal era to four percent. I would like to see the Fund's economists go much, much further and renounce inflation targeting entirely and recognize that even a four percent targeted rate of inflation is much too low for many developing countries due to its effects on economic growth. Yet, this particular finding is very significant. By doubling the acceptable rate of inflation the Fund's economists have begun to create space that validates earlier work by progressive academic economists – for example of Jerry Ebstein and Erin Gialdane – and a variety of civil society organizations who have been battling the Fund for a long time over its strident and damaging inflation targets.

Another IMF study on control of capital inflows should also be notable to progressives. It demonstrates that the Fund is continuing the admittedly slow and uneven process, which they began after the Asian financial crisis, of critically addressing the issue of capital controls. Up until the Asian crisis the Fund was poised to modify its articles of agreement to make the liberalization of international capital flows among the central purposes of the Fund and to extend its jurisdiction to international capital movements. But in the wake of that crisis the IMF started to change its views on capital controls – modestly and cautiously to be sure. The center of gravity at the Fund moved away from an unequivocal fundamentalist opposition to all capital controls to a tentative, tepid, and conditional support for some types of capital controls under some circumstances.

Given the inertia at the Fund, actions during the current crisis represent a minor revolution. Iceland, one of the first economies to implode during the first stages of the crisis has a stand-by arrangement with the Fund that includes provisions regarding the need for stringent capital controls. Of course, those capital controls were implemented by the Icelandic central bank prior to signing an agreement with the Fund, but the Fund's agreement with Iceland made a very strong case for the necessity of the maintenance of those capital controls in order to restore financial stability.

It is worth mentioning that changes in thinking on capital controls have been very uneven at the Fund. There was in some ways a dance around the issue since the Asian crisis – one step forward was followed by two steps back. A raft of reports in the context of the current crisis mention capital controls on many occasions, and most of those reports have contained rather tepid statements about the protective role of capital controls in some countries and about how they should be used temporarily, as a last resort.

The Fund has also taken great care to enumerate the costs of imposing capital controls. What we saw in the fall of 2009 were continued signs that the IMF was still wrestling with the issue of capital controls. When Brazil implemented capital controls this past October, the Fund issued a mild rebuke of Brazil and noted that these kinds of controls have proven porous over time in a number of countries. However, in contrast to the Fund's past behavior, witnessed for instance when Malaysia put in place their controls, the IMF's response was muted and seemed more about trying to deter other countries from pursuing capital controls without the Fund's blessing.

This new IMF paper reaches far beyond the public statements on capital controls to this point. The authors of this study commend capital controls for having prevented economic contraction in a number of countries during the current crisis, for having reduced levels of financial fragility, for having lengthened the maturity structure of countries' external liabilities, and improving the composition of capital inflows. The report also said that capital controls can retain their potency, even if investors devise strategies to evade these controls, and that unrestrained capital flows can contribute to collateral damage in developing countries. This suggests that today's IMF is not your grandfather's IMF. There are other parts of the report that have the typical and expected qualifications, which are portrayed as insuperable obstacles to the use of capital controls. But the existence of other views represents a minor advance on the part of the Fund that we as progressives should try and exploit.

I will look next at three other facets of the way in which the crisis is contributing to and highlighting the incoherence that may ultimately prove to be increasing policy space for development. First, the IMF's stances on fiscal policy in numerous stand-by arrangements it signed during the current financial crisis have been somewhat different and far less coherent than the ones it took in the context of the East Asian crisis. Certainly the IMF continues to apply pressure to developing countries to ensure compliance to stringent fiscal and monetary policy targets, but it has demonstrated a much greater degree of flexibility when some countries have been unable to meet their fiscal targets. This fiscal policy flexibility has been offset by the IMF's insistence on stringent monetary policy – notwithstanding the very recent report of on inflation targeting by the Fund that I looked at above. I think this is suggestive of a substantial incoherence in the cognitive framework: the IMF has an apparent lack of certainty about how exactly to respond to the current crisis, and in that context is sending very mixed signals about appropriate fiscal and monetary responses.

A second dimension of this incoherence relates to changes in the global economy. Time will have to tell how the expansion of the G-7 to the G-20 is ultimately going to influence the balance of global economic power and the salience of neoliberal ideology. At this point one simply does not know. It is notable that the developing countries that are now lending to the IMF and those that are now part of the G-20 are countries where the development strategies have run distinctly counter to neoliberalism. And more importantly the countries that appear to be coming out of the crisis successfully are countries where neoliberalism has not had much influence on policy-making. It is worth noting that China has a new position at the Fund, which is also a very recent development. Taken together, it is hard to imagine that these changes in participation in the global political economy are not going to have some practical effects on policy space in the future.

The last instance of this incoherence that I want to highlight is the way the problems in the European periphery may be helping to discredit the array of initiatives that were so much in vogue during the last decades. These involve national policy makers tying their own hands through measures such as hard pegs to hard currencies, the adoption of recessionary inflation targets, and trade and investment agreements that preclude the use of capital controls and other developmentalist policies. Depending upon how things play out in Europe, we may find that there is yet another locus of discussion about problems with important dimensions of neoliberal policy, regarding the constrained policy space in peripheral and semi-peripheral countries. It is a strange, new world when the European Union seems to be out IMF-ing the IMF to such an extent that some commentators, like Joseph Stiglitz, suggested that Greece would do well to go to the IMF rather than the European Union's Central Bank because the IMF is offering countries better terms on their bailouts than the EU.

In conclusion, I think what progressives have been wishing for from the IMF is for it to recant its misguided neoliberal biases of the last several decades. It is understandable that those of us who have been waiting so long for that kind of recantation are not apt to be satisfied with anything less than a full denouncement of the neoliberal regime. I also think that this helps to account for the pessimism of many progressives at the present time. But I want to note that intellectual change and ideological change does not happen overnight. It is not a neat or consistent process. It never has been, and we would do well to accept that it may not be at the present time either. Change can be messy; it can entail moments of ideological, theoretical, and political incoherence. It is best if we recognize that the current moment may be a time when incoherence could produce new thinking, new strategies, and new achievements – particularly if progressive economists capitalize on the apertures that are being created at the current time.

POSTSCRIPT TO READERS: Since this talk at the NSSR the process of normalizing capital controls has accelerated quite dramatically. Those interested in this matter might wish to read various essays on the recent normalization of capital controls that appear on http://triplecrisis.com.

END NOTES

[1] Transcription: William Kenton.
Talk given at the conference on The Effect of Financial Crises on Distribution at The New School for Social Research, March 5 2010. We thank Ilene Grabel for the permission to transcribe and publish her remarks.