

Will the IMF swallow its own medicine?

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The news disseminated on Wednesday 22 November, 2006 by the *Bloomberg*² agency that the IMF would be selling an exorbitant amount of gold, must have caused agitation within the international financial community as well as in Peru among certain mining business circles and among those who are aware that gold exports substantially contribute to our trade balance surplus. Last year they amounted to \$3.16 billion (only slightly inferior to the \$3.36 billion of copper exports), which accounted for 18% of exports of goods (\$17.3 billion), and which – provided the price remained at current levels – would reach this year the sum of \$4 billion, thus also reaching such share in total exports (\$22 billion).

This proposal has been put forward by the IMF Finance Department, which has recommended selling 11 million ounces of gold, accounting for 10.7 per cent of the total 103 million ounces of gold currently stored in its vaults. Such sale would amount to a \$6.9 billion revenue, with the current price of gold at \$628 an ounce; but indeed, such a thing would be unrealistic since the sole announcement of the sale would drive down gold prices in a few hours or days. The main reason for this apparently desperate measure lies in the IMF's growing deficit, which threatens to reach unsustainable levels within a few years. Throughout this year, it is expected to rise to \$88 million, equivalent to nearly 9% of its \$1 billion budget, having said figure doubled in the last ten years. On the basis of a passive projection, this unbalance would even reach the amount of \$280 or \$300 million by the two-year period 2009-2010, thus apparently indicating that this institution is not precisely an example of what it has always preached to us. How come the 'lender of last resort' has financial difficulties? Basically, owing to three reasons.

On the one hand, because countries are behaving increasingly well, blindly following the recipes of the 'Washington Consensus' and even exaggerating its commandments. However, it may be better explained by the international economic prosperity in the most recent triennium, which has led to drastic increases in raw material prices, to the massive attraction of foreign investments and to a relatively widespread boom in exports that favors peripheral countries, basically China and India, large oil exporters and even satellites within the orbit of the former Soviet Union and Latin America itself. This has allowed them to accumulate exorbitant amounts of Net International Reserves (NIR). This Scrooge McDuck-like accumulation comes as a result of the traumas that have been haunting these countries since the outburst of the successive and unexpected financial crises and the regional contagion that took place in recent years: Mexico (1995), Southeast Asia (1997), Russia (1998), Brazil (1999) and Argentina (2001), without taking into account that of Turkey. Reasonably, these and the rest of the so-called 'emerging' countries have decided to replace the support provided by IMF funds and other sources of finance by those resources resulting from their own NIRs, no matter how miserable their output. This implies major progress on account of the relative autonomy they are thus granted, both politically and economically.

¹ This article was first published in Spanish language at *La Insignia* website (<http://www.lainsignia.org>), IFIs Latin American Monitor (<http://ifis.choike.org>) translated it into English.

² *IMF should sell gold to cover losses, Directors say*
<http://www.bloomberg.com/apps/news?pid=20601086&sid=aE3NiMEzvrhY&refer=news>

On the other hand, it has been affected by the fact that many governments have decided to make early payments of their total debt service to the IMF, thereby remaining outside its sphere of influence and saving interest accrued thereon. In Latin America, such repayments have represented substantial amounts. Last December 13, Brazil – until then the IMF’s largest debtor – repaid in advance and on good terms all debts owed to the institution amounting to \$15.5 billion, thus saving \$900 million in interests. That same path was followed by Argentina two days later, paying up \$9.8 billion, on bad terms, and being freed of \$850 million in interests. Uruguay has just announced that it will do the same thing within the next days, repaying the amount of \$1.1 billion. Therefore, interest payments to be collected by the IMF have drastically shrunk. It is worth noting the evolution of the amounts owed to the IMF until recently, having said figure reached its highest level at the end of 2003, amounting to \$72 billion, and falling then to \$64 billion in 2004 and 34.7 billion in 2005. As of October 31 of this year, the amount owed to the institution barely stands at \$15.3 billion; that is to say, only 21% of the amount it was owed three years ago! To make matters worse, 80% of that amount accounts for the debt owed by Turkey (\$12.2 billion).

Finally, the growing deficit can also be blamed on an apparent overspending by the IMF, although the institution blames it on the “new roles” it has been given in recent years, such as the monitoring and control of money laundering. However, let us just think of the IMF staff which has increased from 1800 people in 1990 to 2700 nowadays. And we better not talk about the salaries earned by IMF staff.

As a result, the IMF – the global financial doctor, policeman and fireman – has practically remained without clients and is heading not only towards financial bankruptcy but also towards moral and political crack, which has led – according to experts – to an ‘identity crisis’. So, the IMF should hopelessly take a series of steps in order to cover its growing deficit, being one of these precisely the sale of its gold stockpile, which amounts to 14% of the world’s annual production. In view of this imminent danger, there are indeed reasons to panic, when recalling that the Fund already sold many millions of ounces in 1976 and 1980, although for other motives. But there are also reasons to prevent the dreaded proposal from being materialized since the resulting fall in gold prices is not convenient for the US, given the fact that it is the world’s third largest gold producer (and the first in terms of actual reserves), with a share – as of 2005 – of 10.4% of the total, following South Africa (11.8%) and Australia (10.4%), and ahead of China (8.9%), Peru (8.2%), Russia (7.2%), and Indonesia (6.6%). And, since 85% of votes in the Executive Board (made up of 24 members) are needed to approve such a decision, the US could easily give it a veto given the fact that it has a 17% voting share in the Fund.

If such a way out is not feasible, the IMF must be wondering: And who can save us now? Unless the Red Grasshopper shows up, it will have to swallow its own medicine. Self-medication will call for a drastic reduction of excess staff and, following the Peruvian lead, could cut salaries and per diems by half. Another possibility to prevent gold prices from falling would be to convince Central Banks to get those precious metal bars the IMF needs to sell instead of Treasury bonds. An increase in contributions made by some of its 184 member countries to the Fund’s ‘capital stock’ has also been suggested; however, this would be a very troublesome process since it would imply a change in terms of member quotas (and votes). Finally, among other suggestions, some people suggest that the institution could devote itself to manage the NIRs of countries wanting so, thus ensuring them an increased output in exchange for substantial commissions. Let us see what

happens, since we will still have to wait three or four months before a high-level panel (including the participation of Alan Greenspan) appointed by the IMF to evaluate the convenience of a sale of gold submits its report.

Of course, the issue of whether to maintain or close down the great international financial institution remains open, but that is a horse of a different color (we are sure that Wal Mart would be willing to buy the eight-floor building to sell Chinese goods!). Undoubtedly, the fact that there are no longer any fires in the large majority of countries (with the exception of the US, but the IMF evidently gets cold feet about it) does not necessarily mean that firemen should cease to exist. But, undoubtedly, it is necessary to change the way in which 'financial programming' is carried out, so that not all IMF 'financial aid' programmes end up always leading to recession. For such purpose, the macroeconomic models on which it is based – either the Polack or Robichek model – will have to be changed so as to include variables related to the impact that adjustment and stabilization measures have on inflation and economic growth.

