The IMF's return to austerity?

By Kevin P. Gallagher | 10.13.2020

US intransigence at the IMF may leave middle and low-income countries unable to recover for years to come

People wait for food aid amid the economic crisis due to the coronavirus pandemic in Manchay, Peru

When the Covid-19 pandemic went global, the International Monetary Fund's (IMF) new Managing Director Kristalina Georgieva rose to articulate a bold, new and ambitious role for the IMF. Early on Georgieva declared: 'These are the times for which the IMF was created—we are here to deploy the strength of the global community, so we can help shield the most vulnerable people and revitalize the economy.'

Georgieva's was nothing less than a new vision for an IMF that in the past had become stigmatised for conditioning emergency finance on austerity measures including slashing health and social spending. Indeed, to cite one example, in a study of IMF programs in 137 developing countries between 1980 and 2014, scholars found IMF programmes lowered health system access, increased neonatal mortality and accentuated inequalities.

In a major step forward, at every occasion possible the Managing Director and other senior management have also emphasised that 'if this recovery is to be sustainable—if our world is to become more resilient—we must do everything in our power to promote a "green recovery."' Last week, the IMF even went as far as calling for a massive boost to public investment in rich countries. In contrast, its support for developing countries however falls tragically short.

The plight of developing countries in the pandemic

At the onset of the crisis, United Nations Conference on Trade and Development (UNCTAD) and the IMF each estimated that emerging market and developing countries would need at least USD 2.5 trillion in 2020 and more in 2021 to avoid economic collapse. In April, Georgieva even appealed to the IMF board to 'boost global liquidity through a sizeable SDR (Special Drawing Right) allocation, as we successfully did during the 2009 global crisis and by expanding the use of swap type facilities at the Fund.'

SDRs are the IMF's monetary assets – which allow the IMF to act in a limited sense as a kind of central bank to the world. SDRs are part of the foreign exchange reserves of countries and can be sold or used for payments to other central banks and multilateral institutions. As central banks in advanced economies used their balance sheets to secure finance in the advanced economies, the IMF could use SDRs for the rest of the world, as it did in 2009.

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But the United States under Donald Trump has abandoned multilateralism and instead built a wall between itself and most of the world. The US administration blocked the proposal for a new allocation of Special Drawing Rights and create swap-like facilities at the IMF. While the US Federal Reserve Bank loosened monetary policy at home and extended swap lines to other advanced economies while the US government spent more than USD 1 trillion on fiscal stimuli, they would not have the IMF take the same approach.

Thus, Georgieva has neither been very successful in harnessing the strength of the global community nor the potential of the IMF. Aside from USD 215 million in new grants for 25 of the poorest IMF countries to cover their IMF debt obligations, Georgieva had to resort to the confines of the existing IMF balance sheet of just under USD 1 trillion dollars, roughly USD 388 billion of which can be made available to emerging market and developing countries. However, in a new study we find that the IMF has made relatively trivial amounts of new financing available and have been slow to disburse the financing at their disposal — the IMF has financed just over 100 programmes at upwards of USD 88 billion.

The IMF makes some steps in the right direction

There are some positive news. Although the response has been relatively small, compared with the past the IMF's reaction to Covid-19 has proven to be far less conditional on fiscal austerity. The IMF has financed over 100 programmes thus far. Aside from 13 of the programmes, there are low to no strings attached forms of liquidity provision.

What is more, the IMF has encouraged its members to prioritise health expenditure and social spending to attack the coronavirus and protect the vulnerable. We show this in another new paper published in the journal COVID ECONOMICS, where we created an 'IMF COVID-19 Recovery Index' that measures and monitors the IMF's response to the Covid-19 crisis.

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According to our index, the IMF deserves credit for endorsing increases in health spending and measures to protect vulnerable people and firms in the midst of the crisis. The Fund encouraged health spending and increase the supply of medical devices in programs in Bolivia, Ghana, Gabon, Bosnia and Herzegovina, and the Dominican Republic.

Just as important, the IMF earns an even higher score in our index for encouraging the protection of the vulnerable, as indicated by programmes that recommend strengthening safety nets in Cameroon, increasing spending in Bolivia, wage support in Bangladesh and highlighting a food supply programme in the Bahamas.

A return to austerity looms on the horizon

Despite the rhetoric however, IMF emergency programmes are doing little to encourage a green recovery. The IMF did recommend mandatory hurricane insurance protection in its programme for the Bahamas and supported Bangladesh's request for climate change adaptation and mitigation measures, but the overwhelming majority of IMF programmes lack a green recovery component.

And things may be about to get worse. At a recent event, IMF First Managing Director and former Trump Administration official Geoffrey Okamoto said developing nations should 'keep those receipts,' hinting that a return to austerity is coming. Indeed, in a new report, Eurodad found that the IMF has encouraged 72 countries to begin a process of fiscal consolidation as early as 2021. These sentiments are echoed in the IMF's newest Fiscal Monitor released this week, encouraging advanced economies to increase spending and debt to mount a green recovery, but cautioning emerging market and developing countries to get frugal.

As the US retreats from multilateralism and the IMF is on the verge of backtracking, it is time for the rest of the world to lead. When finance ministers from across the world virtually gather the IMF's annual meetings this week, it is imperative to ensure that emerging market and developing countries have the fiscal space to attack the virus, protect the vulnerable and mount a green and inclusive recovery. If the Covid-19 crisis has proved anything, it is that no country can isolate itself from others. Until there is a universal vaccine, if the virus isn't tackled everywhere it can show up anywhere. Similarly, debt crises and big downturns anywhere effect supply chains and livelihoods everywhere.

Emerging market and developing countries need new liquidity in the form of SDRs alongside debt relief on a grand scale in order to attack the virus, protect the vulnerable and mount a green and inclusive recovery. That's what many countries are attempting among the more advanced economies, why should it be different for the poorer? We can't build a wall around progress, we need a multilateral effort to globalise a green and inclusive recovery.