Thanks for Nothing

A former chief economist at the World Bank offers a case study in how heavy-handed interference can break what doesn't need fixing

by Joseph Stiglitz

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During the recent demonstrations in Seattle, Quebec City, and elsewhere denouncing the International Monetary Fund and the World Bank, the press tended to dismiss the protesters as fringe reactionaries ignorant of the benefits of globalization. But although no one condones the violence in Genoa, for example, it would be wrong simply to reject ma ny of the protesters' concerns. As the chief economist at the World Bank from 1997 to 2000, I have seen firsthand the dark side of globalization—how the liberalization of capital markets, by allowing speculative money to pour in and out of a country at a moment's whim, devastated East Asia; how so-called structural-adjustment loans to some of the poorest countries in the world "restructured" those countries' economies so as to eliminate jobs but did not provide the means of creating new ones, leading to widespread unemployment and cuts in basic services. The media and the public have since become concerned about this dark side as well—globalization without a human face, it is sometimes called.

However, the issue that is commonly debated—namely, whether we should be "for" or "against" globalization—is not the salient one. As a practical matter there is no retreating from globalization. The real issue is the conduct of the international economic organizations that steer it. If we continue with globalization as it has been managed in the past, its agenda driven by the North for the North, reflecting the North's ideologies and values, the future will not be bright. There will be a backlash in the developing world and increasing conflict with the developed world. There will be greater global instability and rising doubts about the value of a market economy. Those doubts are already reflected in a pervasive hostility toward the IMF in the Third World: in Thailand and Korea, for example, ordinary citizens refer to their countries' debilitating recessions as "the IMF." Yet well-managed globalization has enormous potential for improving the lives of people in poor countries.

Events in Ethiopia offer a case study of the ways in which globalization can go awry, and they highlight the need for reform. In March of 1997, barely a month into my job at the World Bank, I went to Ethiopia to meet with Prime Minister Meles Zenawi. Meles came to power in 1991, after a seventeen-year guerrilla war against a bloody Marxist regime. His victory left him facing seemingly intractable problems. Ethiopia, at the time a nation of 58 million people, had a per capita income of around $100 a year. Droughts had killed millions. Though he trained in medicine, Meles had studied economics at the Open University, in England, and knew that only major changes in economic policy could bring his country out of poverty. During our discussions he showed a deeper and more subtle understanding of economic principles (not to mention a greater knowledge of the circumstances in his country) than many if not most of the international economic bureaucrats I would deal with in the succeeding three years.

These intellectual attributes were matched by integrity: Meles was

quick to investigate any accusations of corruption in his government. He was committed to decentralization—to ensuring that the center did not lose touch with the various regions.

At the time of my arrival Meles was engaged in a bitter dispute with the International Monetary Fund, which had suspended its program in his country. At stake was not just some $125 million of IMF money but potentially hundreds of millions of dollars in World Bank loans as well. Traditionally the World Bank is reluctant to lend money unless the IMF certifies that the country in question has a solid macro-economic framework. The provision is well intentioned: history has shown that governments that cannot manage their overall economy do not do a good job managing foreign aid.

The IMF is supposed to judge performance by results. Ethiopia's results could not have been better. It had no inflation; in fact, prices were falling. Output was growing steadily. Meles was demonstrating that with the right policies even a poor country recovering from civil war and famine can experience sustained economic growth. After years of struggle and rebuilding, Ethiopia was beginning once again to receive assistance from Western governments.

Judging by results, then, the IMF should have given Ethiopia an A+. And there were other positive indicators, such as direct evidence of the competence and commitment of the government. For instance, it had cut back dramatically on military spending—a remarkable feat for a government that had come to power by military means—in favor of spending to fight poverty. This was precisely the kind of government to which the international community should have been directing assistance. Yet the IMF had suspended its aid. Why?

The Fund was worried, first, about the role of foreign aid in the government's budget. A poor country like Ethiopia has two sources of revenue—taxes and foreign assistance. The government's budget is balanced as long as those revenues equal expenditures. This may seem like elementary economics—but it is not IMF economics. Although Ethiopia's budget was balanced, the Fund argued that the country's budgetary position was untenable: what would happen if foreign assistance suddenly dried up? Ethiopia should act immediately, the Fund argued, to prevent the possibility of disaster. That meant cutting spending or raising taxes—a difficult action in any country, but especially in a desperately poor one.

An argument against long-term reliance on foreign aid may be superficially appealing, but in reality it dictated that Ethiopia's expenditures could be paid for only by tax revenues. That is a fundamentally unsound policy: it means that foreign aid does not lead to more schools or health clinics. Instead the money is, in effect, simply added to reserves. Surely this was not the intention of the international donor community. Surely donors wanted to see those new schools and health clinics built in Ethiopia. Meles put the matter to me passionately: he said that he had not fought so hard for seventeen years to be told by some bureaucrat that he could not actually provide improved services for his people once he had persuaded donors to pay for them.

I cannot adequately describe the emotional force of his words or the impact they had on me. I had taken the World Bank job with one mission in mind—to work to reduce poverty in the poorest countries of the world. I had known that the economics would be difficult, but I

had not fathomed the depth of the bureaucratic and political problems imposed by the IMF.

Meles provided an economically sound response to the IMF's concerns about the stability of foreign aid: flexible spending. Building schools and clinics does not require long-term commitments. If donors provided money to build schools, Ethiopia would build schools; if they stopped providing funds (as they had for a while), Ethiopia would stop building schools. But the IMF would not be swayed.

he IMF had other bones to pick with Meles. In 1996 Ethiopia repaid a U.S. bank loan early, using some of its reserves. The transaction made perfect sense. In spite of the solid nature of its collateral (an airplane), Ethiopia was paying a far higher interest rate on its loan than it was receiving on reserves. But the United States and the IMF objected. They were bothered not by the logic of the strategy but by the fact that Ethiopia had undertaken this course without consulting the IMF. The IMF used this failure to consult as one of the grounds for suspending its program. But why should a sovereign country—one whose policies had convincingly demonstrated its capability—have to ask permission of the IMF for every action it undertakes?

Another point of contention related to financial markets. Even after the United States experienced the ruinous consequences of financial deregulation, in the form of the savings-and-loan debacle, the IMF preached the gospel of rapid deregulation around the world, to countries far less able to withstand its negative consequences. Earlier deregulation in Kenya had led to soaring interest rates there. Meles sensibly resisted such a move in Ethiopia. But the IMF continued to insist on deregulation, and not even a panel of scholars I assembled, most of whom supported Meles's position, could budge the organization.

These episodes highlight two troubling aspects of the IMF's characteristic behavior. The first concerns secrecy. Because so many of its decisions are reached behind closed doors, the IMF leaves itself open to suspicions that power politics, special interests, or other agendas unrelated to its stated purposes are at play. For example, some critics questioned whether it was just a coincidence that Ethiopia's early repayment deprived a U.S. bank of a high-interest, secure-collateral loan on which it was making large profits and that the United States was the country most vociferously protesting. A second, closely linked aspect concerns the subordination of matters of substance to matters of process. The processes themselves, with the numerous conditions that are often attached, not only infringe on national sovereignty but also tend to undermine democracy.

I returned to Washington from Ethiopia gravely upset by what I had seen. During the following weeks I convinced the World Bank that the IMF's position made no sense, and the Bank tripled its lending to Ethiopia. In the ensuing years the country has been beset by political problems and war. It is impossible to know whether some of its travails could have been avoided or mitigated if aid had been more forthcoming.

The debate over globalization has already had an impact: the IMF’s rhetoric, and in some instances its actions, have changed. The IMF talks more about poverty and participation than it used to. Last year it finally offered a number of poor countries meaningful debt relief. Still, these are only beginnings.

The biggest problems afflicting the IMF and other instruments of globalization concern governance. At the United Nations five countries can exercise veto power. In the IMF only one—the United States—can do so. At both the IMF and the World Bank voting rights are allocated not according to population but according to economic power, and the various countries' representatives are typically finance ministers or members of central banks, not officials with broader outlooks and concerns. Most of the debate about reforming the international economic architecture has occurred within these same small, elite circles. The voices of those most affected by globalization are barely audible in discussions about how the table should be reshaped and who should have a seat at it.

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