THE PERPETUATION OF DEPENDENCE:

The International Monetary Fund and the Third World

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BY CHERYL PAYER

Radicals are correctly suspicious of the International Monetary Fund. They know that it is dominated by the developed capitalist nations, who comprise only one quarter of its membership but hold three quarters of its quotas and two thirds of the total votes. They know that, although it claims to be a universal and nonpolitical institution, most of the socialist countries have found membership incompatible with their own economic policies. They have noticed that IMF missions descend like vultures in the wake of right-wing coups in countries such as Ghana, Indonesia, and Brazil.

Yet despite this well-founded mistrust, there is little understanding of the real function of stabilization programs imposed by the IMF on economically weak countries. Monetary theory is a difficult and arcane subject, poorly understood even by many economists. During the 1930s financial experts quipped, "Only two people in the world understand monetary theory, and they disagree." This joke underlines not only the difficulty of the subject, but its essentially political nature as well. Monetary theory is not just an esoteric technology; it affects the real distribution of resources within and among national societies. An understanding of the IMF's role in the world capitalist system provides an invaluable tool for predicting the alternatives and the chances for success of attempted revolutions, and for under-

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standing the real reasons for the failure of democracy in the Third World.

The International Monetary Fund is the most powerful supranational government in the world today. The resources it controls and its power to interfere in the internal affairs of borrowing nations give it the authority of which United Nations advocates can only dream. Only the U.S. military establishment with its client armies can rival the IMF as the key institution of imperialism in the world today, and their functions are complementary. The discipline imposed by the IMF has often eliminated the need for direct military intervention in order to preserve a climate friendly towards foreign investment.

This tremendous power does not, of course, inhere in the corps of economists who comprise the IMF, nor even in the Board of Governors appointed by the member nations. The IMF must be seen as the keystone of a total system. Its power is made possible not only by the enormous resources (about $29 billion) which it administers directly in short-term lending to cover balance-of-payments fluctuations, but more significantly as a result of its function as international credit agency. All of the major sources of credit in the developed capitalist world, whether private capital, bilateral government aid (of which U.S. aid is by far the most important), or other multilateral institutions such as the World Bank group and the various regional development banks, will refuse to aid a country if that country persists in defying IMF "advice." The real importance of the IMF lies in the authority delegated to it by the governments and capital markets of the entire capitalist world.

Its power over the underdeveloped countries derives, on the other hand, from their economic weakness, specifically their chronic foreign exchange difficulties. As the Pearson report[1]* recognized, the lack of foreign exchange is the *major external constraint* on the development programs of poor countries. These countries' foreign exchange difficulties are the result of several factors: declining prices for their exports; the huge proportion (as much as 40 percent for some Latin American countries) of export earnings that must go to debt service and to the remittance of profits on foreign investment; and the poor

* Notes will be found at the end of the article.

countries' critical need for capital goods and raw materials for industry, food for their urban population, and consumer goods which they are not manufacturing themselves.

The IMF and its client institutions have the resources to ease these payments difficulties, but they will grant credit only if the borrowing country institutes a stabilization program to control inflation. The IMF, arguing that it is chiefly inflation which is responsible for the balance-of-payments difficulties, enforces programs which invariably contain three main elements:

(1) Domestic anti-inflationary policies, including the reduction of government spending and the contraction of bank credit. This implies the curtailment of public expenditures for welfare and of government investment in development projects; economic recession; the failure of many domestic businesses and their forced sale to foreign speculators; and a large unemployment problem resulting from both curtailed government expenditures and business recession.

(2) Devaluation of the currency in terms of the U.S. dollar, and the elimination of as many direct controls on foreign exchange expenditure as possible.

(3) Encouragement of foreign investment through policies which range from anti-strike legislation (and action), through tax benefits, to guarantees of profit remittance. This part of the program contains a self-fulfilling prophecy, since the IMF first prescribes the policies necessary to attract foreign capital and then gives the country the credit rating required by foreign capital suppliers.

The IMF claims that the aim of this stabilization package is long-term balance-of-payments stability, but its actual effect in practice has been reinforcement of the dependence on traditional exports, which was the real cause of instability in the first place. If the government implements these policies on IMF advice, it is rewarded, not with a healthy and diversified economy, but with temporary relief for immediate exchange difficulties. This relief typically takes the form of new loans to the government, rescheduling of old loans when repayments become burdensome, and credit for the import of consumer goods. Indonesia after the military coup of 1965 is a good example of this: the *new* debts contracted after the government adopted

IMF recommendations are so large that one business weekly warned:

> The Indonesian economy has won a reprieve from bankruptcy but can expect eventually to be strangled by its foreign liabilities just as the economy starts to get off the ground after the present five-year plan. . . . Do donors really intend to force Djakarta into bankruptcy in the long run? Or does the West believe the enormous debts are essential to control Suharto?[2]

When another payments crisis arises as a result of these new obligations, debts can again be rescheduled if the government is still behaving properly.

If the government is not willing to take IMF advice, it will face severe sanctions in the form of inability to obtain credit anywhere in the capitalist world. Typically, in that case, the difficulties the defiant country suffers will be blamed on its "socialist" policies, rather than on crippling debts and dried-up aid.

The system can be compared point by point with peonage on an individual scale. In the peonage, or debt slavery, system the worker is unable to use his nominal freedom to leave the service of his employer, because the latter supplies him with credit (for overpriced goods in the company store) necessary to supplement his meager wages. The aim of the employer-creditor-merchant is neither to collect the debt once and for all, nor to starve the employee to death, but rather to keep the laborer permanently indentured through his debt to the employer. The worker cannot run away, for other employers and the state recognize the legality of his debt; nor has he any hope of earning his freedom with his low wages.

Precisely the same system operates on the international level. Nominally independent countries find that their debts, and their continuing inability to finance current needs out of imports, keep them tied by a tight leash to their creditors. The IMF orders them, in effect, to continue laboring on the plantation, while it refuses to finance their efforts to set up in business for themselves. For these reasons the term "international debt slavery" is a perfectly accurate one to describe the reality of their situation.

The stabilization program imposed by the IMF precludes any adoption of socialist policies, and is hostile even to mild social-welfare measures, whether direct subsidies such as government pensions and decent wages, or indirect consumer subsidies such as public utilities operated at a deficit. All such programs which involve income redistribution through government policy are considered distortions of free market forces, and thus undesirable, by the IMF advisers. The policies they require penalize the average citizen by reducing his income and raising the prices of essential goods and services. In Indonesia, for example, the prices for public utilities and petroleum products were decontrolled, causing a sharp rise in the cost of living.[3] The irony of this "anti-inflation" program is obvious.

Domestically controlled and financed enterprises are hard hit, and often bankrupted, by the measures demanded by the IMF. Tight credit restrictions make domestic financing extremely difficult to obtain; devaluation increases the local cost of both imports and existing loans; and domestic markets are usurped by the unrestricted imports financed by external credit.[4]

On the other hand, these measures give the foreign firm a strong relative advantage (in addition to the specific incentives for foreign investment which the IMF also encourages). Its capital resources are not affected by the local depression; it can buy up bankrupt local firms at bargain prices; and if it is chiefly interested in extractive enterprises rather than consumer goods, its potential markets are not affected by the depression. Because the general level of employment and wages is reduced in a depression, the foreign firm can assure itself of a stable, conservative labor force by paying slightly more than the general level of wages—still a huge bargain.

Underlying all the IMF arguments against inflation is its fundamental hostility to any type of development which is not carried out by, through, and for private foreign capital. To this end it systematically vetoes any possibility of domestically controlled growth, whether under public or private auspices. However, the type of speculative foreign investment which is encouraged by the IMF does not represent the transfer of resources from rich countries to poor, but rather the transfer of resources within the poor countries from domestic to foreign ownership. And, although foreign investment may provide some temporary relief to the balance of payments, in the long run it adds to the burden as profits are remitted to the investing country and loans must be repaid with interest.

The costs in human terms of these stabilization programs are enormous. In Indonesia, for example, a large number of native-owned industries were forced to close down, due to the contraction of the money supply and competition of foreign consumer goods imported (particularly from Japan) on credit; their employees were thrown out of work. Then, in 1968 an estimated 20,000 government employees—the class which had suffered most from the preceding inflation—were fired as an economy measure.[5] Critics charge that even the price stability that was achieved at this cost is an illusion, since it is only a massive influx of imported commodities that soaks up the excess currency, and the bill for these goods must be added to Indonesia's already heavy foreign debt.[6]

Another nation now in the throes of an IMF austerity program is the Philippines. Although President Marcos won election to a second term in 1969 after proclaiming his opposition to devaluation of the peso and the conditions attached to IMF loans, the government spending which was used to generate votes for his victory helped precipitate a foreign exchange crisis which Marcos and his Central Bank governor chose to meet by capitulating to IMF conditions. The underlying cause of the crisis was the basic weakness and foreign trade dependence of the Filipino economy—conditions which an earlier IMF program, instituted in 1962, did much to exacerbate.

The 1962 program included such typical IMF staples as the elimination of restrictions on currency convertibility; the end of import and export controls; free exchange rates; fiscal and monetary restraints by the government and private enterprise; and devaluation of the peso. These policies, however, did not achieve their professed goal of balance-of-payments equilibrium. Rather, dismantling controls on foreign exchange allowed the dollar outflow for "services" (mostly profit remittances) to rise from $200 million in 1961 to $990 million in 1966. These deficits were eased by American loans; the external government debt rose from $275 million in 1961 to $737 million by 1968. Largely because of the pressures of this crushing debt, the Philippines is now being forced through the same wringer which in the past has proved so destructive to national industry, and is in addition powerless to achieve its professed aims.[7]

A detailed case study of the economic effects of an IMF stabilization program in Argentina in the years 1958-1963 has been published.[8] The authors' verdict is harsh: they found that the austerity program resulted in a decline in per capita consumption which they estimate as near 20 percent over the five-year period; the balance of trade and payments worsened considerably; and, despite a temporary influx of speculative capital during the middle years, the poor economic conditions and the political unrest that resulted ultimately led to a flight of capital. These austerity measures failed to curb inflation, however; in fact, the index of the cost of living rose by 400 percent over the five-year period—a larger increase than had been registered in any previous five-year period. The authors termed this paradoxical situation "deflationary inflation."

This paradox can largely be explained by examining the effects of the devaluation, which is another component of the "comprehensive stabilization program." In orthodox economic theory, a devaluation could be expected to improve the balance of trade by encouraging exports and discouraging imports. For example, a devaluation in the United States would predictably raise the price and thus discourage the purchase of Volkswagens and Japanese stereo components. This theory assumes, however, that the productive capacities of the various nations are basically comparable and consumer tastes nearly identical, so that a decline in imports will benefit domestic producers of similar goods.

In the case of underdeveloped countries dependent on raw materials exports, however, this assumption cannot hold, for the poor countries and the rich countries are not producing the same type of goods for the world market.[9] Imports of capital goods and manufactures are necessary to the economy but not available from domestic sources, while the export markets do not expand automatically when prices fall. The effect in these countries of devaluation is thus to worsen the already disadvantageous terms of trade, which forces the country to export more (if it can) to pay for essential imports, and raises the internal price level because imported goods comprise such a large part of it. Devaluation benefits three groups: exporters, who may be either local landowning oligarchs or foreign corporations owning mines or plantations; foreign consumers of these exports; and foreign companies buying up local businesses hit by the recession (a form of invisible export). In this way the program ostensibly introduced to check inflation and improve the balance of payments may have just the opposite effect.

It is important to understand that the various elements of the IMF stabilization programs are closely related. The IMF charter gives it no power to control the domestic policies of borrowing nations; in fact at the time of its founding in 1945 both Great Britain and the U.S. Congress required assurances that this would not happen.[10] The power to intervene was arrogated later, when Latin American countries began to borrow from the Fund, and it was justified with the argument that balance-of-payments problems could not be controlled in the presence of inflation. There is in fact another way to control payments deficits, which socialist countries have adopted and many bourgeois nationalist governments would prefer if given a choice: the imposition of exchange controls. Controls, despite the admitted dangers of corruption which they pose, offer the only way a weak economy can protect itself by setting its own priorities on the use of scarce foreign exchange. The IMF charter *does* commit it to promote currency convertibility—which is the necessary condition of capitalist penetration of other countries via investment and trade. It is by following this primary mandate that the IMF has been able to extend its supervision to domestic policies. In practice, a weak economy cannot hope to achieve full convertibility and the IMF knows this, but it can nevertheless exercise constant pressure in that direction and ensure that foreign investors and importers of foreign goods get priority treatment in the distribution of exchange permits.

I do not mean to assert that inflationary policies have any intrinsic superiority over stability. Rather, it is the rigid linkage of control of inflation with devaluation and currency convertibility plus incentives for foreign investment which effectively shut off all alternatives for autonomous national development, and therefore economic independence in the long run is precluded. If a government is willing to abandon the impossible quest for a fully convertible currency, a whole new range of possibilities appears. Dudley Seers has suggested that Cuba, which withdrew from the IMF in 1964, is probably the only country in Latin America which is willing and able to put IMF recommendations into effect—with the significant exceptions of convertibility of the peso and hospitality to foreign investment.[11] Japan provides a capitalist example of an economy that has achieved both growth and currency stability while keeping out foreign investment; the policies Japan followed to become the third largest economy in the world would never have been permitted by the IMF if it had been able to interfere.[12]

It should be clear by now that the IMF plays an intensely political role in its dealings with economically weak countries, not an impartial technical one. We must now go one step further, in order to understand the crucial part played by the IMF in the two most discouraging patterns of Third World politics: the subversion of social revolutions and the death of democracy.

In this context it is irrelevant whether a revolutionary government comes to power legally or illegally, via elections, military coup, or armed popular revolution. These circumstances may incline it towards one solution rather than another, but do not determine anything. The dilemma that any of these governments will face if it is genuinely nationalist (let alone socialist) lies in its foreign exchange weakness, the burden of debts and obligations inherited from previous governments, and the rising expectations of its supporters. It has the choice of going through one of two types of economic wringer: the first being submission to an IMF austerity program; the second a choice to go it alone with a different type of austerity program imposed by the lack of foreign exchange for imports. The latter choice will require that the government move rapidly leftward, in order to curb upperclass consumption and to mitigate austerity by equalizing whatever social benefits may be available. This is the road taken by Cuba, with a lot of help from the USSR.

Armchair revolutionaries should be hesitant to throw stones; the difficulties of the second choice must not be underestimated. To give just one example: when large food imports are necessary to feed the urban population, people may go hungry before even the best-intentioned government can revolutionize its nation's agricultural production. The penalties of defiance of the IMF are so heavy that most would-be revolutionary governments change course and bow to the will of international capital. One example which has been documented by Rebecca Scott is the Bolivian revolution of 1952. This began as a genuine popular rising: a real land reform was carried out, and the tin miners, an important element in the revolutionary coalition, gained wages and benefits and even a measure of workers' control in the nationalized mines. The United States, curiously enough, decided to support this socialist revolution with aid, and by 1958 had so thoroughly addicted the Bolivian government that the IMF, represented by an American banker, G. J. Eder, could force it to split with its working-class wing and pass legislation favorable to American investors as the condition of continued aid.[13]

The government of India was forced by a foreign exchange crisis in 1957 to change course dramatically and abandon its nationalist and social welfare policies as a condition of foreign exchange relief.[14] The same story has been repeated many times, for the pattern is inexorable: no country with a foreign-exchange problem can avoid the harsh choice between the two types of austerity program. Chile's crisis is approaching. If the government deigns even to negotiate with the IMF, the revolution may well be doomed. If it does not, the pace of revolution will have to be accelerated. In either case, formal democracy is likely to become a casualty.

The IMF is intimately connected with the failure of democracy in Third World countries. Contrary to official platitudes about the immaturity of democracy in those countries, military coups have overtaken precisely those nations where the electorate was relatively sophisticated and class-conscious, and elections were relatively free from corruption. An electorate that votes its pocketbook will vote against austerity programs, and the only "solution," if the upper classes hope to maintain their standard of living and their imported luxuries, may be to abolish elections. There is a fundamental contradiction between obedience to the IMF's demands and responsibility to the electorate in a democracy.

This pattern is clear in the case of Brazilian democracy and the military coup which ended it in 1964. One "populist" president after another struggled to reconcile the demands of the electorate for economic expansion on the one hand and the inexorable pressures of foreign debts and U.S. demands, via the IMF, for an effective stabilization program, on the other. As one observer put it:

> Abandoning the attempt at stabilization . . . could only mean the slide toward a radical political solution involving unilateral renunciation of foreign debts and possibly even confiscation of foreign investments in Brazil.[15]

When one president, Goulart, finally tried to opt for this radical solution to the dilemma, the military, with obvious approval from the United States, took the government away from him. The government installed by the military

> encountered the same problem which every postwar Brazilian government had faced: the overwhelming political unpopularity of any effort at anti-inflation policies. . . . The suspension of the political system existing between 1945 and 1964 therefore had a direct connection with the rhythm of economic development and economic crisis which has been evident since the Second World War. Faced with the problem of electoral reversals while pursuing an anti-inflation program, the Castello Branco government chose to change the rules of the electoral game so that it could not suffer defeat.[16]

A similar pattern can be seen in the events surrounding the 1966 military coup in Argentina. Strong military repression has been found necessary both to contain popular unrest and to prevent populist leaders from choosing a radical solution.

The destruction of democracy seems to be well under way in Ceylon at present. In the elections held in May 1970, Ceylon's remarkably literate and aware electorate chose Mrs. Bandaranaike's Sri Lanka Freedom Party, which had campaigned on a platform explicitly opposed to the IMF austerity program enforced by the previous government. As one journalist explained popular disenchantment with this "austerity";

When there was no foreign exchange for infant milk foods while Air Ceylon bought a new aircraft, or while sparkling Jaguar cars cruised Colombo streets, the word got around. And what could even the least enlightened peasant think when he saw 3,000 acres given on a "special lease" to a British engineering company or to a local industrialist? . . . The people knew that the burden had been cast on their frail shoulders while somebody else was having a ball.[17]

But the victorious party inherited an empty foreign exchange treasury. The government complained bitterly about the failure of socialist countries to come to Ceylon's aid with significant foreign aid, and apparently decided within months that it had no recourse but to negotiate with the IMF. Eventually the government decided to reverse its election promise of a doubled rice ration,[18] and the finance minister complained that he could not impose necessary foreign exchange controls because of IMF pressure.[19] While the world press pontificated on the inefficiency of socialism, the young, educated "Che Guevarist" rebels knew that the problem was too little socialism —and the betrayal of the campaign promises. Now Ceylon's democracy, robust and operating only last year, appears to be doomed. Perhaps once the ineffective army can be beefed up with outside assistance, it will take over the task of enforcing the unpopular stabilization, as other armies have done throughout the Third World.

Only a few examples of IMF subversion of revolutions and democracy in the underdeveloped world can be given here; there are many more. We must write the history of the Third World with a clear understanding of this powerful system; we must comprehend the system if we are ever to be able to destroy it.

NOTES

1. *Partners in Development,* report of the Commission on International Development (Lester B. Pearson, chairman) New York, 1969.
2. *Far Eastern Economic Review,* June 4, 1970, p. 16.
3. Gunnar Tómasson, "Indonesia: Economic Stabilization 1966-69," *Finance and Development.* vol. 7, no. 4, 1970, p. 49. (*Finance and Development* is published by the IMF and IBRD.)

4. Bruce Nussbaum, "So Little Hope," *Far Eastern Economic Review,* September 19, 1970, p. 54.
5. E. Utrecht, "Mass Firings Combat Inflation," *Information on Indonesia,* vol. 1, no. 1, 1970, p. 12.
6. *Information on Indonesia,* vol. 1, no. 1, 1970, p. 10. Compare this critical account with the IMF's own evaluation of the Indonesian stabilization program, which it considers a great success and a model for other countries, in Tómasson, *op. cit.* On this point Tómasson writes: "In addition to relieving the balance-of-payments pressure by providing foreign exchange resources for financing essential imports, the foreign aid program generated counterpart funds that were a major factor in the non-inflationary financing of the budget deficit throughout the stabilization period." (p. 48).
7. Nussbaum, *op. cit.,* pp. 51-57.
8. Eprime Eshag and Rosemary Thorp, "Economic and Social Consequences of Orthodox Economic Policies in Argentina in the Post-War Years," *Bulletin of the Oxford University Institute of Economics and Statistics,* vol. 27, no. 1, February 1965, pp. 3-44.
9. This distinction may explain another curious paradox. The IMF forces devaluation on the underdeveloped countries against their will, but it was IMF pressure that forced Great Britain to *postpone* devaluation of the pound much longer than other economists considered wise. Could the nations controlling the IMF have intended to prevent an improvement in the competitive position of British exports vis-à-vis their own products?
10. Accounts of the founding of the IMF can be found in Richard N. Gardner, *Sterling-Dollar Diplomacy,* Oxford, 1956; Robert M. Blum, *From the Morgenthau Diaries, III: Years of War 1941-1945,* Boston, 1967; and Roy A. Harrod, *Life of John Maynard Keynes,* New York, 1951.
11. Dudley Seers, "A Theory of Inflation and Growth in Underdeveloped Countries Based on the Experience of Latin America," *Oxford Economic Papers,* June 1962, p. 194, note 2.
12. See "Consider Japan," *The Economist,* September 1, 1962, for details of Japan's program for dealing with exchange crises. I am indebted to Yoshi Tsurumi for this reference and other valuable comments on an earlier draft of this article.
13. Rebecca Scott, "U.S. Foreign Aid to Bolivia: 1952-1964," Radcliffe Senior Honors Essay, 1971, unpublished. See also George Jackson Eder's own account of his mission to Bolivia, *Inflation and Development in Latin America: A Case History of Inflation and Stabilization in Bolivia,* Ann Arbor, 1968.
14. Michael Kidron, *Foreign Investment in India,* London 1965, pp. 120, 157, and *passim.*
15. Thomas E. Skidmore, *Politics in Brazil 1930-1964: An Experiment in Democracy,* New York 1967, p. 258.
16. *Ibid.,* p. 318 and *passim.*
17. Mervyn de Silva, "Revenge Through the Ballot Box," *Far Eastern Economic Review,* July 23, 1970.
18. *The Economist,* March 27, 1971.
19. David Baird, " 'No' to the Leftists," *Far Eastern Economic Review,* April 3, 1971.