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THE EVOLUTION OF THE INTERNATIONAL MONETARY FUND

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INTERNATIONAL FINANCE SECTION
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PRINCETON UNIVERSITY
Princeton, New Jersey

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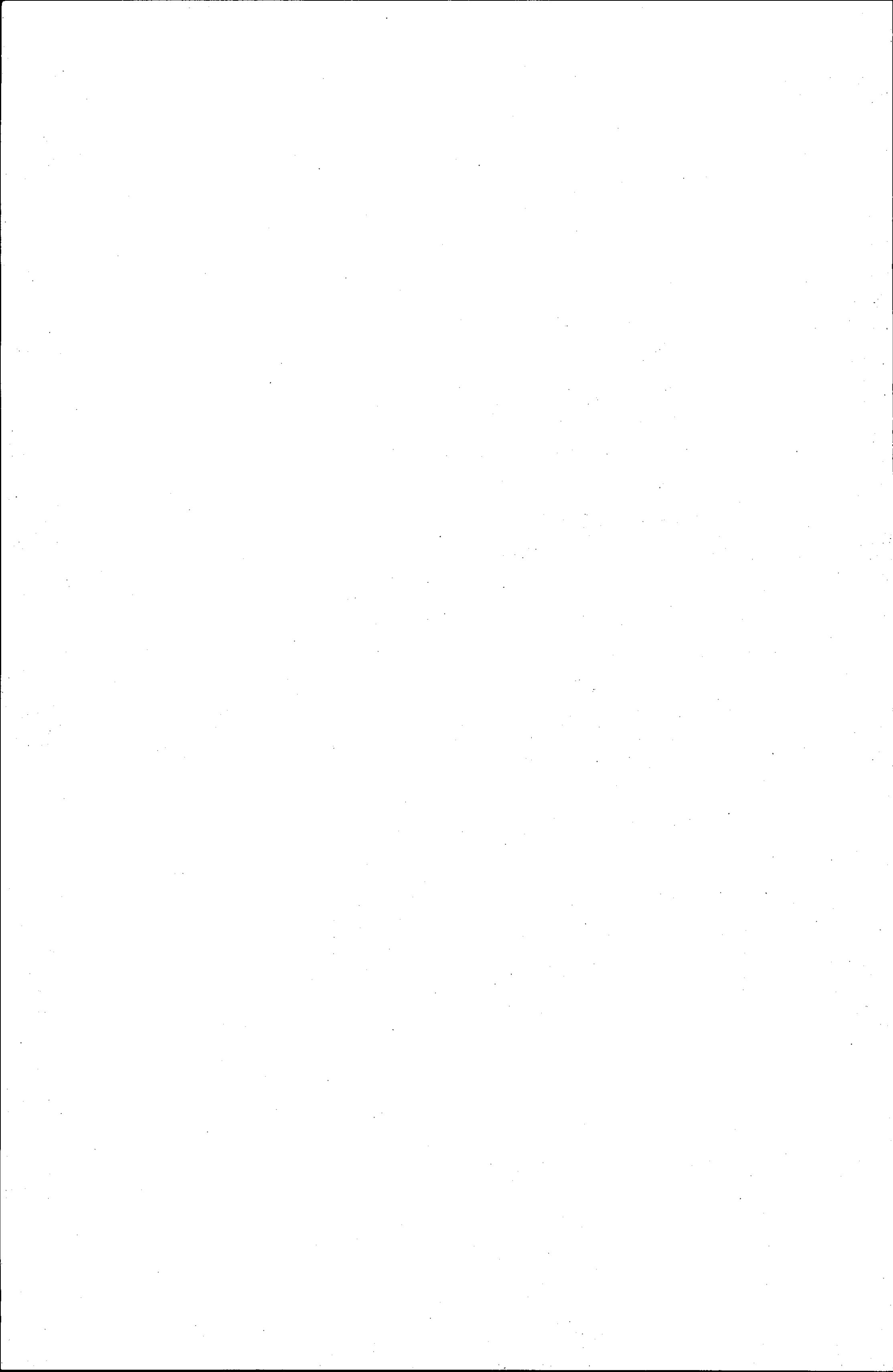

Introduction

There appears to be wide agreement that the International Monetary Fund is an effective international institution, standing alongside its sister, the World Bank Group, as a success of the post–World War II era. The Fund devised an organization, assembled a highly professional career staff, and by the end of its first decade had emerged from financial inactivity and seeming somnolence into the self-confidence and performance that have since characterized it. Shaken to its roots by the collapse of the Bretton Woods par-value system in 1971-73, the Fund displayed a capacity for survival and adaptation which gainsaid the funeral orations preached over its casket at that time.

How did this successful evolution come about? This essay is addressed to that question. It is not a systematic chronological account (for which see Horsefield, 1969, and deVries, 1976) but rather a description of salient aspects of that evolution written from the vantage point of my years within the Fund from 1949 to 1974, first as Executive Director for the United States and thereafter as Deputy Managing Director. Of the many aspects that could have been included, some major and some minor, I have selected a few that I consider to have been strategic in structuring the Fund's organization, policies, and operations as they are today: (1) relations between Management and staff, Executive Directors, and Governors; (2) relations between the Fund and member countries; (3) the Fund's financial resources, their use and growth; (4) the Fund's exchange-rate policy; (5) the Fund and important but selected international financial crises.

These five aspects lie at the center of the Fund's development as a policy-making, policy-monitoring, and financing institution. To make that clear, I begin by considering briefly what the Fund was created to do.

The Role of the IMF

It is not necessary to recount the complex negotiations that resulted in the adoption of the Articles of Agreement of the IMF at the Bretton Woods Conference in 1944.[1] What is needed is to list the elements in those Articles that set forth the role assigned to the Fund:

To the extent necessary, the IMF has authorized the use of unpublished information known to me by reason of my service as a staff member in the capacity of Deputy Managing Director during the period November 1, 1962, through February 28, 1974. However, the views expressed are my own and not necessarily those of the Fund.

[1] The Articles have been twice amended, in 1969 to provide for Special Drawing Rights (SDRs) and in 1978 to make more basic changes.

1. Monitoring changes in par values or in exchange arrangements under which par values were not effective: The power to approve or disapprove par values was conceptually the most important provision in the Articles; this was the first time that states had agreed to such an invasion of sovereignty. The Second Amendment of the Articles terminated this power unless at some future time a system of par values is reinstated by nearly unanimous agreement. But the "surveillance" mandate in new Article IV does give the Fund substantial authority to evaluate the adequacy of exchange rates.
2. Administering what can be called a "code of fair practice" in the field of foreign-exchange rates and international financial transactions: This important power included approval or disapproval of payments restrictions or discriminatory practices.
3. Providing financial resources to member countries to assist them in dealing with payments imbalances: The framing of the terms on which resources would be made available became one of the most difficult, controversial, but also successful elements in the evolution of the Fund.
4. Developing relations with member countries and providing, or assisting them to provide, information needed by the Fund to carry out its responsibilities: The Fund was given the power to require that certain kinds of information be provided, even if the member regarded it as sensitive and was not publishing it.

In short, the Fund, while not a super–central bank in the full sense of that term, was and is an institution possessing broad powers to guide the international financial conduct of members and to give or withhold financial assistance. To put those powers and duties in the Articles of Agreement was one thing. To make the Fund into an effective operating institution was quite another.

The IMF Organization

The first task was to establish a *modus operandi* among the three organs of the Fund: the Governors, the Executive Directors, and the Management (i.e., the Managing Director and Deputy Managing Director) and staff.

The Articles, of course, provided some guidance. The ultimate power resides in the Board of Governors, which could and did delegate all powers to the Executive Board (except a few that could not be delegated, such as admitting new members or increasing quotas). The Executive Board, in turn, is "responsible for conducting the business of the Fund." The Board selects a Managing Director, who serves as its Chairman and conducts the ordinary

business of the Fund under the direction of the Board. "Subject to the general control" of the Board, he is responsible for the "organization, appointment, and dismissal" of the staff.

The problem was to make those interrelationships work in practice. What was the Board of Governors to do, and how would the Executive Board and the Management/staff divide the task of developing policy and operating the Fund?

The Board of Governors

There has never been any serious issue relating to the Board of Governors. It was evident from the beginning that a Board consisting largely of finance ministers and central-bank governors, who were destined to become very numerous as membership grew, could not meet often and could not be concerned with day-to-day Fund operations. Various devices were tried to give Governors opportunities for participation other than routine approval of the accounts and the passage (at Annual Meetings or by mail or cable) of resolutions on new members and quota increases. Some thought was given, but quickly dropped, to having frequent meetings. In the early years, committees were created at the Annual Meeting to discuss the Annual Report, and on one occasion there was a panel discussion. These efforts were unsuccessful; Governors attended with reluctance or not at all. In the case of the United States, as Executive Director I found myself, in the status of a "Temporary Alternate Governor," representing the United States to discuss an Annual Report with which I had already dealt on the Executive Board. By about 1952-53, it was accepted that Governors came to Annual Meetings to make speeches, perform their minimum legal duties of voting on resolutions prepared in advance by the Management and the Executive Board, talk with each other, and do business with the bankers and others who attended by the scores as invited guests. Indeed, achieving a decent attendance in the meeting hall—especially in the afternoon—has always been a problem; and in latter years the Meetings have been shortened.

Not until the prolonged effort to "reform" the Fund and the monetary system, in the period from 1972 to 1977, was the role of the Governors considered once more, in an effort to find some way they could play a more active part. The result was the provision in the Second Amendment (Schedule D) for a Council of the Governors to "supervise the management and adaptation of the international monetary system." Pending the establishment of the Council, an Interim Committee is functioning. It has met more often than annually, settling down to twice a year, and has demonstrated an ability to reach agreement on policy matters. For example, in Mexico City in April 1978 it considered an increase in quotas and the second issue of SDRs, and it

agreed to them in Washington in September. The membership of the Committee (and of the Council when it is established) parallels the constituencies represented on the Executive Board.

The Executive Board

The Articles of Agreement provided for a Board of Executive Directors, whose number has increased as the membership has grown and is currently twenty-one. The five members with the largest quotas (at present the United States, the United Kingdom, Germany, France, and Japan) each have the right to appoint an Executive Director who serves at the pleasure of the member. If the first five do not include the one or two members whose currencies have been most used in the preceding year, then that country (or those countries) can appoint an Executive Director for a two-year term. Canada appointed an Executive Director in 1958 and Saudi Arabia did so in 1978. The remaining countries elect Executive Directors for two-year terms by arranging themselves in groups large enough to comprise the number of votes needed to elect. Each Executive Director is entitled to appoint an Alternate who, in the case of elected Directors, is often a national of one of the other members of the group that elected the Executive Director. From a strictly legal point of view, Executive Directors do not "represent" the countries appointing or electing them, are not paid by them, and are not legally subject to their control. For example, it has happened that an elected Executive Director has become *persona non grata* to the country of his nationality, but he may not be removed from office by that country. Nevertheless, in fact, Executive Directors *do* represent the countries that appoint or elect them.

The Executive Board is required to be in "continuous session" at the seat of the Fund. This represented a victory for the view, held especially by the United States, that Executive Directors should devote full time to the Fund and hence be available on short notice to make all necessary decisions. The opposing view was that they should be government officials at the policy level who would be available as needed or periodically.

When the Fund began operations, there were instances—notably Germany, Canada, Mexico, and Italy—of Executive Directors who came to Washington only occasionally, their Alternates being resident in Washington. Louis Rasminsky (an officer and later Governor of the Bank of Canada) was one such absentee Executive Director. He made a determined effort in the early 1950s to persuade leading members that a system of part-time Executive Directors operating at the policy-making level in their own countries would provide an Executive Board more closely in touch with governments. My opposition to this view caused me some difficulty, since the then

Secretary of the Treasury, George M. Humphrey, was more than half persuaded by Rasminsky's arguments.

Two considerations counseled the retention of full-time Executive Directors. One was that in the case of *elected* Directors the idea of an absentee Executive Director who was an official of one country was generally unacceptable to the other countries electing him. The other was the attitude of Per Jacobsson, who became Managing Director in 1956. Before he came to the Fund, Jacobsson had been given the idea that the Executive Board sat rather too heavily on the back of the Managing Director. But he soon concluded that he needed experienced and senior persons as Executive Directors who would be available at Fund headquarters at all times. Major issues could arise without warning, such as the sterling crisis resulting from the Suez venture, which landed in Jacobsson's lap almost as soon as he arrived (see Jacobsson, 1979, p. 299). The idea of part-time Executive Directors died thereafter and has never been resurrected, although Executive Directors do maintain close contact with the countries appointing or electing them. In some instances—notably the United Kingdom and France—the Executive Director is also attached to the country's Washington embassy as minister or counselor, and in a few instances the same person serves as an Executive Director in both the Fund and the World Bank. But for many years there have been no absentee Executive Directors.

Another problem was how the Executive Board would conduct its activities, whatever the division of responsibility between Board and Management/staff (dealt with in the next section). The question of voting was paramount, but there were other issues.

As is generally known, the Fund operates with weighted voting (that is, voting based mainly on size of quota), and in the early years, with fewer members, the United States had a decisive vote (30 per cent in 1949 and still 25 per cent as late as 1959, though just below 20 per cent in 1978). Was the Board to vote on most of its decisions, even though the Articles *required* a vote on only a very few matters? In the early years, voting was fairly often resorted to and the United States pushed some matters to a vote even though disagreement around the Board table was strong. One instance, in 1952, was the retention by Belgium of discriminatory restrictions aimed chiefly at the dollar area. The United States, with the support of the Chinese, Canadian, Egyptian, and Latin American Directors, proposed a reduction of such restrictions. Over the objections of the U.K., European, and Indian Directors, I called for a vote, and the proposal was adopted by 53,025 votes to 34,610.

Since voting was one way in which the preponderant influence of the United States was made apparent, a practical problem faced by the U.S.

Executive Director was how to exercise his power without convincing the rest of the Directors that discussion was futile because the U.S. view would prevail. Sometime around 1953-54, the United Kingdom told Secretary Humphrey that it was especially unhappy at matters being pushed to a vote. By that time I was able to explain that voting was becoming rare (except where legally required) and that taking decisions by the "sense of the meeting" was increasingly the rule. As the years passed, decision by consensus became peaceful, although sometimes at the cost of very long debates. Indeed, there have been many instances where, notwithstanding a decisive majority in favor of a given proposal, decision was delayed to permit a search for common ground. An adjunct to the procedure was that Executive Directors often requested that they be shown as opposing or abstaining, even though there was no formal vote on a decision.

Relations between Executive Board and Management/Staff

Once it was decided that the Executive Directors were to serve in Washington on a full-time basis, what were they to do? What was to be the division of function between them and the Management/staff? The Managing Director was clearly responsible for the day-to-day operations of the Fund and the direction of the staff, but in the first decade there were areas of activity for which the operating responsibility was not clear.

One issue was leadership in Fund missions to member countries or to represent the Fund in meetings of other international organizations. In early years, Executive Directors headed certain missions—for example, to represent the Fund during the negotiations on an International Trade Organization and on subsequent missions to the GATT. But it became apparent that no single Executive Director could represent the Fund acceptably—something akin to conflicts of interest could arise. Fund missions came ultimately to be composed exclusively of members of the staff (and the Managing Director at some ministerial-level meetings). This was, in fact, the practice almost from the beginning with regard to all missions to member countries. However, the Executive Director elected or appointed by the country concerned had a direct interest in such missions, since they deal with important economic and financial matters, so the practice developed that he or his Alternate would be present at most sessions, although not as a member of the mission.

The relationship between mission and Executive Director has not been free of awkwardness and, at times, friction. Responsibility for the negotiation rested with the mission chief, and the report to the Executive Board would be prepared by the mission and would not be seen in advance by the Executive Director or the country. Hence the Executive Director had to be con-

sidered to be participating by invitation of the member country and, in effect, as a member of its negotiating team. Yet this was not always clear, and conflicting views expressed by the mission chief and the Executive Director have sometimes caused confusion. For example, when the negotiation concerned a stabilization program and possible use of Fund resources, the mission might press hard for certain lines of action, while the Executive Director might be less demanding. Countries in such circumstances on occasion have been uncertain as to which voice to heed. Moreover, there have been meetings between a mission and officials of the member country to which the Executive Director was not invited. In short, at times participation by the Executive Director has given rise to difficulties, while at others his close relations with local officials have facilitated the mission's work.

A major—indeed the most important—range of issues in the early years of the Fund concerned internal procedures. What sort of oversight, if any, would the Executive Board exercise over the appointment or discharge of staff? How would the papers and reports submitted by the Management be handled by the Board? Would Executive Directors make proposals or would Board consideration generally be based on Management proposals? Would Executive Directors be privy to all information reaching the Fund? Each of these has more recently surfaced for renewed consideration.

It was not easy to answer those questions and thus determine how the Fund would operate. Executive Directors served full time, they were conscious that the Articles of Agreement gave them major powers, and many of them wanted to be activists. Nonetheless, in the end, the result was a strong Management/staff and an Executive Board that acted largely on Management recommendations—which is not to say that the recommendations were invariably approved, especially when matters of policy were involved. But the evolution which led to that outcome was not painless.

The Articles made it explicit that the Executive Board would engage a Managing Director, and the same procedure was followed when the position of Deputy Managing Director was established, except that the Managing Director proposed the candidate. The appointment of an American as President of the World Bank made it inevitable that the Managing Director of the Fund would be a non-American. It was less inevitable that he should be a European, but—given the power structure—that became the unwritten rule, although each time a new appointment has been made there have been challenges behind the scenes. There have been suggestions that a slate of possible appointees should be presented for discussion by the Board, but it has been accepted that no suitable candidate would wish to be the subject of open debate. Accordingly, on each occasion names have been privately considered and a single person has finally been approached. A committee of the

Board has then been appointed to negotiate terms of service, and its report has always been accepted. With such an informal hit-and-miss procedure, it is perhaps remarkable that Managing Directors, taken as a whole, have been able and effective men, like Per Jacobsson, Pierre-Paul Schweitzer, and H. Johannes Witteveen. The latest, Jacques de Larosière, comes to the Fund from a notable career in France.

The Articles explicitly provided that the Managing Director was responsible for the organization, appointment, and dismissal of the staff, subject to the "general control" of the Executive Board. As for nationality, he is enjoined only to pay "due regard" to the importance of recruiting staff on as wide a geographical basis as possible, subject to the paramount criterion of technical competence. The Executive Board recognized early (after a few unhappy episodes) that it should not seek to debate staff appointments. Only two rules were set: First, the Board should be given written notice of the intention to appoint persons to positions above a stated rank or salary. Second, there has been an unwritten tradition that the director of an area department should be a national of one of the countries in the area. This latter understanding has in my view done much to win Fund acceptance in the less-developed countries.

Just as the Board recognized that it should not seek to challenge the Managing Director's appointments to the staff, he in turn has recognized that important ones should be privately reviewed with Executive Directors. For example, a director would not be formally proposed for the African Department without careful consultation with Executive Directors elected by the African countries, and because of linguistic and other aspects of Africa, there have been some intense discussions behind the scenes. But I do not recall any case in which a Managing Director felt obliged to propose the appointment of a particular person solely because of representations by Executive Directors, although that does not mean that such representations are without effect. In one important instance, the Managing Director privately sought suggestions from several countries for persons suitable to be director of an area department. The results were disappointing, so he pressed one country to come up with a first-rate name. He was not satisfied with the response, and, having rejected that name, insisted on a more senior and promising proposal, which he then accepted and submitted to the Executive Board.

Of course, Executive Directors have not been uniformly and invariably enthusiastic about the Managing Director's proposals. But they recognize that their suggestions should be made privately and that there is no practical alternative to accepting his formal appointments. I do not know of a single instance during my twenty-five years in the Fund in which the Managing

Director withdrew a proposed staff appointment because of objections by the Board, although this had occurred earlier in at least one important case.

The nationality distribution of the staff has caused remarkably little difficulty. In the first decade, there were objections, usually when the budget was reviewed, to "too many Americans" (not surprisingly, considering that in those years a very high percentage of the professional staff was American). But time and energetic worldwide recruitment corrected the situation, although an Executive Director might from time to time complain privately to the Management that his country or area was underrepresented. Here, too, the fact that directors of area departments were nationals of the area has been helpful. I recall an instance in 1966 when, as Deputy Managing Director, I was on an official trip in Africa, accompanied by the black African director of the African Department. In one country, the Finance Minister sharply complained about the sparsity of Africans on the staff. I was being placatory and reassuring, promising more diligent recruiting. My colleague, however, did not hesitate to challenge the Minister, arguing that suitably trained Africans were few in number and were in high demand in Africa.

The Executive Board soon came to realize that it would have to depend on Management/staff to prepare papers and reports, either at the request of Executive Directors or, more usually, on the initiative of the Managing Director with the advice of the staff. The important questions were how the Board would treat those papers and whether the Board would act on its own motion without a Management-sponsored paper or recommendation.

One issue was whether the Board would seek to revise staff papers or reports. The answer that gradually emerged was that it depended on the type of paper. Policy papers or the Annual Report could be and usually were discussed in detail—even line by line—by the Board, after which the staff prepared revised drafts. Reports on country consultations, including those recommending use of Fund resources, were not to be revised unless actual errors were found. The Executive Director, speaking on behalf of the country concerned, could and usually did submit his own and the country's comments, which might challenge the staff report. The draft decision for a member subject to Article XIV, which included a summary of the main conclusions stemming from the consultation, was subject to review and change by the Board, even though the staff might not be altogether happy with the alterations. With the advent of the Second Amendment, country consultations fall under new Article IV (which includes the mandate for "firm surveillance"), rather than under Articles VIII and XIV as before. The staff reports no longer include an evaluative draft decision. In its place, the Managing Director sums up the Board discussion, and this constitutes the Board's conclusion of the consultation.