"'No' to More Money for the IMF"

by Milton Friedman
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In the current debate about whether the United States should increase its contribution to the International Monetary Fund by $8.4 billion, there has been no mention of those "less developed countries" that are *not* in trouble, *not* in danger of defaulting on their debts, *not* asking for or receiving assistance from the IMF. They include such successful and rapidly growing LDC's as Taiwan, South Korea, Singapore, Hong Kong, not to mention Japan, which only two decades ago would also have been termed an LDC but no longer qualifies for that status.

Compare these countries with Poland, Romania, Yugoslavia, Argentina, Brazil, Mexico—all of whom, except for Poland, are currently receiving assistance from the IMF. The two groups differ sharply in one major respect. Every successful country has relied primarily on private enterprise and free markets to achieve economic development. Every country in trouble has relied primarily on government to guide and direct its economic development.

In the successful countries, government's major role has been to maintain and enforce a framework of law and institutions favorable to private enterprise and free markets—despite numerous deviations from that policy to favor specific industries by tariffs, quotas or subsidies.

In the countries in trouble, government has accepted major responsibility for organizing and directing the economy. At one extreme are Poland, Romania and Yugoslavia, where government controls essentially all economic activity. At the other extreme are countries like Brazil and Argentina, where military-backed governments profess support for private enterprise, but where government owns major sectors of the economy, imposes controls on prices, wages, imports and exports and follows unstable and inflationary fiscal and monetary policies. In between is Mexico, where government owns and operates about two-thirds of productive enterprises and imposes extensive controls on the rest of the economy.

Whatever the reason for the international debt crisis, it is real and serious. Defaults could impose heavy losses on banks in the United States and elsewhere and on governments that have guaranteed many of the loans. The IMF is playing a key role in arranging the rescheduling of debts and imposing conditions on debtor countries designed to improve their ability to repay the debts. Is it not desirable to strengthen the IMF's resources so that it can perform this vital function more effectively?

The answer is no. The IMF is a governmental institution. It operates by lending money to *governments,* not private enterprises. It imposes conditions on *governments,* not private enterprises. In the process it strengthens the government relative to the private sector. But the key problem with the debtor countries is that government has played too large a role, private enterprises and free markets too small a role. IMF assistance will, at best, postpone the day of reckoning, while making the long-run problem worse.

Central economic planning has proved a failure whenever it has been tried—whether behind the Iron Curtain, or in less extreme form in such developed countries as Britain, France and Italy, or such LDC's as Mexico, Brazil, Argentina and Peru. Perhaps IMF bureaucrats are more skillful central planners than the home-grown variety, but they too are bureaucrats spending someone else's money, not entrepreneurs risking their own, and they do not even have to face the political music when their best-laid plans go awry. We shall not help the LDC's by foisting a new layer of government planners on them.

The IMF was established in 1945 as part of the Bretton Woods monetary reform. It was assigned a clear role: to provide *temporary* financing to alleviate temporary balance-of-payment problems of member countries committed to maintaining fixed exchange rates for their currencies. That function disappeared when the Bretton Woods system collapsed in the early 1970s. However, the IMF did not disappear and ever since it has been seeking a new function. The debt crisis is a heaven-sent opportunity, creating the possibility that the IMF can become a world central bank. National central banks are bad enough; we do not need an international one. The IMF should be abolished, not expanded.

If the IMF is not strengthened, may not the Treasury and the Federal Reserve have to step in to prevent the failure of major commercial banks? Not at all.

Banks made loans to the debtor countries at terms they considered profitable, taking full account of the risks involved. Had all gone well, they would have reaped the profits. If any loans go sour, the banks (i.e., their stockholders) should bear the loss, not the taxpayers. If government socializes the losses, it will inevitably end up socializing the profits. Neither the banks nor the rest of us can have our cake and eat it.

If the IMF were out of the picture—or operating within its present resources—the banks would arrange their own rescheduling of debts, as they do with domestic borrowers in trouble. In the highly unlikely case that defaults caused some banks, perhaps including large ones, to fail, their depositors would be protected from loss by federal deposit insurance. The Federal Reserve would and should step in only to prevent bank failures from reducing the quantity of money. That would limit and isolate the losses. They would be borne by the banks that took the risk. The rest of the economy would not suffer.

In an understandable effort to minimize losses, major banks and their supporters have predicted dire consequences if the quota increase is not promptly approved—a world financial collapse or major deflation or perhaps runaway inflation. Their cries of "wolf" ring hollow. If the danger is so grave, it will take more than the Band-Aid of an IMF-quota increase to avert it. We should not let ourselves be stampeded by their apocalyptic visions.

President Reagan has long preached and practiced reduced intervention by government into the economy. His administration's support for an increase in the U.S. contribution to the IMF is in direct conflict with that philosophy.

Compiled by Robert Leeson and Charles Palm as part of their "Collected Works of Milton Friedman" project.