The Bretton Woods Institutions and the second crisis of multilateralism

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After 75 contentious years supporting expansion of the interests of the Global North with the support of elites from the Global South, the World Bank and IMF now face a crisis of multilateralism in no small part of their own making, as failed economic policies have resulted in wide-spread skepticism of the effectiveness and equity of the international order they helped to shape.

The first crisis of multilateralism

Exactly 75 years ago, on 1 July 1944, delegates of 44 nations gathered together at an old hotel in New Hampshire to negotiate the blueprint for a post-war economic order. For the next three weeks, with the war in Europe and Asia still raging, the delegates debated and negotiated whether to endorse plans drawn up by Harry Dexter White, relatively obscure US Treasury economist, to establish the International Monetary Fund (IMF) and the World Bank.

The previous world order, already rocked by World War I, had not been able to survive the two great disruptions of the 1930s: the Great Depression and rise of militant fascism. The depression, and the chaos that followed – the departure of key countries from the gold standard, a retreat of countries behind tariff walls and the so-called 'beggar-thy-neighbour' policies – saw a reduction in world trade, which further exacerbated the US economic crisis initiated by the 1929 stock market crash. The world was fragmenting into regional economic blocs: not only those led by the Axis powers, Germany and Japan, but even Britain, which established its own sterling currency area.[i] By the time of the 1941 Pearl Harbour attack, the US Treasury Department was already making plans for the new economic world order that it sought to impose on the world, and it would be a resounding endorsement of multilateralism in economic affairs. The chief architect was Harry Dexter White.

White's new economic order, based around his IMF, would have three outstanding features: first, it would allow countries to temporarily borrow currencies from each other, in the hope that doing so would prevent competitive currency devaluations. This feature arose from White's conviction that the major cause of the Great Depression was the competitive currency devaluations implemented by raw materials exporting economies in South America and elsewhere. Second, the IMF would discourage the continuation of trade and currency blocs of enemies and allies alike and promote economic multilateralism in trade. Third, it would make the US dollar, along with gold, the *de facto* international reserve currency. Although the IMF was very much the centrepiece of his proposal, White also recommended an International

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Reconstruction and Development Bank (IBRD, or World Bank) to give loans to aid post-war reconstruction and aid development in the so-called 'third areas'.

John Maynard Keynes, who also believed that the time had come to end trade and currency blocs and re-establish multilateralism, had developed an alternative proposal at the same time as White's. Keynes had developed an International Clearing Union, which, unlike White's creation, was a truly radical proposal because it put as much pressure on creditor nations (like the US) to reduce their balance of payments surpluses as it did on debtor countries to reduce their balance of payments deficits.

To be sure, Keynes was worried about White's IMF amassing too much power and policy control over debtor countries, one of which was likely to be Britain. But Keynes, and even some American experts, particularly at the Federal Reserve, also feared that neither the Fund nor the Bank would be able to generate enough liquidity to deal with needs of post-war economic construction. Nevertheless, at the Bretton Woods Conference itself, in July 1944, the US was able to convince enough of its allies (mainly European, Commonwealth and Latin American countries) to sign on to the plan; while many of them would have preferred Keynes' Clearing Union, they had long before determined that it was not in their interests to oppose an all-powerful America from its preferred solution. A huge public relations campaign in the US saw off challenges from isolationist forces in the US, and the Bretton Woods Agreement was passed by Congress in the spring of 1945.[ii]

The transformation of the Bank and Fund

White's Fund got started in 1946 and it set about determining the rules by which countries in balance of payments difficulties could borrow currencies from other Fund members. Given that so many countries were reliant on goods from the US and Latin America (the 'dollar area') to kick-start their reconstruction, everyone wanted dollars. But White's critics had been right. The way the Fund was set up was too limited to get enough dollars to all the countries that needed them. The World Bank could lend only to particular projects and was soon under the control of conservative Wall Street bankers. By 1947, most European countries were facing a balance of payments crisis even as the US economy was experiencing record balance of payments surpluses.

Yet, instead of using the Fund or the Bank to deliver the much-needed dollars to European countries, the American Government chose to step in and buy the surpluses itself, then give them to the Europeans, *gratis*. This initiative, popularly known as the Marshall Plan, worked a treat: By 1951 the major European economies were back on their feet and were less dependent on US imports.

However, while this rather strange state of affairs had solved one major problem when it came to Europe, it created a serious public relations problem when it came to the emerging "Third World". Latin American nations and an increasing number of now-independent former colonies, especially in Asia, looked at the beneficent handouts that the US had given to its European allies for reconstruction and asked why they could not receive similar gifts for their economic development. The US was not disposed, however, to give grants to this admittedly larger group of nations, except in the case of military hand-outs to those few allies deemed important in the emerging Cold War against communist Soviet Union and China.

Through the 1950s, the US made a number of important reforms that would address this tension, at the same time placing the Bretton Woods Institutions (BWIs) at the front and centre of the relationship between the industrialised and wealthy Global North and what was seen as the poor, dependent, Global South. First, it relaxed the IMF's borrowing rules to encourage countries in balance of payments distress to come to it for temporary assistance, while at the same time pioneering a new type of arrangement called Stand-By Agreements (SBAs). These agreements set out the criteria that nations would have to fulfil in order to be eligible to borrow currency from the Fund.

Second, it created new bilateral and multilateral facilities with which to disperse loans to Third World countries. Some of these new facilities would become part of the growing World Bank system, such as the International Finance Corporation (IFC), the Bank's private sector investment arm, established in 1956, and the International Development Association (IDA), the Bank's

concessional lending arm, established in 1960. In 1957, the US also created the world's first loan-giving economic development agency, the Development Loan Fund, which the Kennedy Administration would re-christen as the US Agency for International Development (USAID) three years later. Throughout the 1960s, as a second wave of decolonisation swept the world bringing independence to dozens of African countries, most members of the rich country club, the Organisation for Economic Cooperation and Development (OECD), developed their own loan-giving aid agencies in imitation of the American example. This era also saw the initiation of the regional development banks, with the founding first of the Inter-American Development Bank (1959), followed by the African Development Bank (1964), and then the Asian Development Bank (1966).[iii]

Another big change came in the late 1960s with Robert McNamara's departure from prosecuting the war in Vietnam to the presidency of the World Bank. McNamara revolutionised the institution, increasing its loan portfolio seven-fold and inaugurating its transition into the self-styled knowledge leader in international development, a position which it continues to enjoy to this day.

By this time, the new aid regime had taken shape; and regardless of whether these new aid programmes were the province of individual countries or overseen by the multilateral development banks (MDBs), the IMF further secured its position in this regime as disciplinary headmaster. All the MDBs and, increasingly, the bilateral aid agencies, would insist on a country concluding an SBA with the IMF before loans could be disbursed. The process of conditionality – whereby countries would be required to make reforms to earn these loans in order to access official credits – had by now become well established.[iv]

In the meantime, the Bretton Woods Institutions continue to do pretty much what they have always done

The first debt crisis and the neoliberal era

The BWIs had thus established themselves as the gatekeepers of the relationship between the Global North (the US, Western Europe, Japan and the former settler nations of the British empire) and the Global South (everywhere else): first, on the basis of their undoubted technocratic and administrative skills and second, on their usefulness to the major powers. They could control access to the disbursement of loans desired by the developing nations, while at the same time imposing policy constraints and conditions on nations that would have often been awkward or uncomfortable for the wealthy nations to insist upon.

The lending itself was buttressed by the emergence of certain intellectual theories now in vogue, such as the modernisation theory (particularly W.W. Rostow's stages of growth theory) and the simultaneous emergence of development economics as an academic discipline. Unfortunately, these theories were not able to confront certain realities that undercut their policy logic: for example, industrialised countries who produced the majority of high-end products would always endeavour to make it more profitable to produce these products rather than to sell either the raw materials that went into making them or basic agricultural commodities. A population explosion in the Global South that was partly due to advances in medical science also undercut the capacity of the development project to produce the sort of quick results that the entire theory rested on.[v]

Some countries identified a loophole in the system and stepped up the ladder of development through exploiting it: if they could just establish themselves as an exporter back to the Global North of these high-end industrial products, loans could be repaid and the country could soon modernise and eventually end up in the rich club as an OECD nation. First Korea and Taiwan and then, in more recent years, China followed this path out of the development trap (by more often than not ignoring the advice of the BWIs than following it).[vi]

Indeed, the Bank's record of fighting poverty, especially rural poverty, including through the 'green revolution' which it backed, were unsuccessful: its programmess, more often than not,

helped mainly wealthy farmers and increased inequality.[vii] The World Bank and the IMF also developed a tendency to support authoritarian regimes in the Philippines, Indonesia, Zaire, Brazil, Chile and South Africa, as well as an unfortunate habit of endorsing the accessions of right-wing but US-friendly dictators by offering them big loans as soon as they stepped in to power.[viii] They facilitated, in collaboration with local elites, the extraction of natural resources and agricultural commodities from resource-rich nations.

As a result, by the early 1970s, most countries were in a virtually constant state of indebtedness, needing a regular injection of new loans in order to repay the principal and the interest of previous borrowings. This debt bubble expanded even further, when an excess of liquidity, due partly to Nixon's de-coupling of the US dollar from gold, signalled an end to the Bretton Woods monetary order, leading to a frenzy of reckless private lending, especially to Latin American countries.[ix]

Despite being complicit in the practices that led to inflation of the bubble, when the bubble burst in 1982, it was the Fund and the Bank that were asked to step in to manage the fallout. This was the era of structural adjustment, where the BWIs became the global proselytisers of the free market philosophy now in vogue in Washington and elsewhere: the liberalisation of trade and investment and the privatisation of government services became the mantra and a feature of all conditionality agreements. It ushered in the era of neoliberal globalisation that would reign supreme for the decades of the 1980s, the 1990s and the 2000s. The entire project received a boost in the years after 1989, when the term 'Washington Consensus' was first coined, and when the Soviet empire crumbled, further entrenching the conviction that capitalist globalisation was now inevitable.[x]

Nevertheless, the 1980s and early 1990s were the zenith of the two institutions' power and influence. The lost decade of development that followed when structural adjustment failed to lead to wealth and riches, the growing consciousness that the debt problem was a continuing sore for many nations of the Global South, as well as increasing concerns about the social and environmental impact of large development projects favoured by the Bank, saw the cachet of the institutions start to decline. The IMF's ideologically driven role in worsening the impact of the 1997 Asian Financial Crisis made it a further target of critique. Social movements in the Global North and the South protested in the streets, winning some institutional reforms to the Bank's lending practices and to their management of the debt crisis in the late 1990s and early 2000s.[xi]

The second crisis of multilateralism

The Bretton Woods Institutions' hegemonic power to set the terms of the debate about international development was definitely weakened by the early 2000s as a result of challenges to their judgement, the power of social movements and from authoritative policy and academic experts.[xii] But the Bretton Woods institutions' power has always, ultimately, come from the support given to them by the their most powerful nation-state members. And this institutional support did not really waver during this period.

Nevertheless, the rise of China and the continued fallout from the 2008 global financial crisis have ushered in a second crisis of multilateralism. President Trump's recent tariff war with China, whatever the real motivations behind it, has further weakened one of the fundamental tenets of multilateralism. However, the potential impact of China's rise on the BWIs is complicated. Although success of the Chinese model and

Photo: Disrupt the IMF/ World Bank Spring Meetings, 25 April 2009 by Elvert Barnes Protest Photography

the power of China as a global player in development, most clearly demonstrated by the establishment of the Asian Infrastructure and Investment Bank (AIIB), might be interpreted as a challenge to the hegemony of the BWIs, it could also be argued that there is more than unites the two models than separates them. China may decide that its interests lie in working through them rather than against them.

The consequences of the global financial crisis have probably been more profound: years of stagnation and imposed austerity have finally made populations in the US and Europe question whether the elite-led project of neoliberal globalisation was really contributing to a more just and peaceful world. More and more people are increasingly conscious that inequality is not only a problem between the Global North and the Global South, but within countries of the North and South as well. The rise of the environment movement in reaction to the climate crisis has also brought the contradiction between Bank and Fund policies and the requirements of ecologically sustainable development to the fore. As the Bretton Woods Institutions were two of the major champions of the neoliberal project, their brand has been tainted. Even the IMF, the most rigid apologist for free market policies, has started to talk about inequality and capital controls. Nevertheless, the IMF's backing of austerity across Europe through its surveillance function was influential and arguably responsibly for unnecessarily deepening the crisis—and its role in the Greek crisis as a member of the infamous 'Troika' has further undermined its legitimacy.

In the meantime, the BWIs continue to do pretty much what they have always done. The Bank is still primarily a lending institution, favouring large, capital-intensive, often extractivist development projects with loans that must be repaid. It continues to push a model of development whose success in bringing nations out of poverty has long been in question. The Fund continues to be primarily a crisis manager and gatekeeper of access to finance for countries in balance of payments trouble. Its policy 'advice' to wealthy countries is a choice, but the story is very different for poorer countries experiencing a balance of payments crisis. A recent analysis of the impact of the Bank's policies in South Africa suggests that it has not learned a great deal: it is still pushing an agenda favourable to corporations and the wealthier members of the population and has hampered South Africa's attempt to address systemic inequality.[xiii] Similar 'lessons not learned' also apply to the Middle East and North Africa region, and Argentina, among others.

With the Fund's mixed record on economic management, and the Bank's patchy results addressing poverty and development, one might have hoped by now to see more fundamental change coming out of the organisations. This has not occurred. Constrained by their mandates and their institutional forms, they appear incapable of questioning the basic assumptions of their approach or their purpose. They have, nevertheless proved themselves rhetorically and practically adaptable enough to ride out several storms, usually of their own making. Although their influence, along with US hegemony, appears to be in gradual decline, the institutions have shown themselves up till now an uncanny ability to survive. It would be a bold observer indeed to predict that their 75th anniversary will be the last major landmark that they reach.

Comparisons between the 1930s and the 2010s are common, because both decades saw a financial crisis at the end of the preceding decade followed by years of sluggish growth and the rise of nationalist and fascist movements. But the current crisis of multilateralism differs from that of the 1930s in a number of ways, not least in that it is much more of a global crisis, where the model(s) of development being adopted have more often than not led to disappointment and frustration. The tragedy is that there are different policies and models out there that could lead to a new multilateralism, such as those outlined in the Geneva Principles.[xiv] The question is, do we have the wisdom and the courage to pursue them—and do the World Bank and the Fund have the capacity to admit their failures and to adapt themselves and their philosophy to a new century?

As the World Bank and IMF celebrates their 75th Anniversary this year, the Bretton Woods Project is publishing in October 2019 a series of essays analysing the heritage and forecast of both institutions under the lenses of democratic governance, human rights, and the environment.

ENDNOTES

[i] For how US policymakers understood the breakdown of the post-war order, see Jeffrey Frieden, *Global Capitalism: Its Fall and Rise in the Twentieth Century* (New York: W. W. Norton & Company, 2006), Chapter 8 & Chapter 9; Lloyd C. Gardner, Economic Aspects of New Deal Diplomacy (Boston: Beacon Press, 1964).

[ii] There are too many works of the Bretton Woods negotiations and outcomes to list here. Many of the classic studies, such as Richard Gardener's *Sterling-Dollar Diplomacy: The Origins and Prospects of Our International Economic Order* (New York: Columbia University Press, 1980) and Alfred E. Eckes, Jr, *A Search for Solvency: Bretton Woods and the International Monetary System, 1941-1971* (Austin and London: University of Texas Press, 1975) are valuable but falsely imply the agreement as a compromise between Keynes and White. Ben Steil's recent *The Battle of Bretton Woods: John Maynard Keynes, Harry Dexter White and the Making of a New World Order* (Princeton and Oxford: Princeton University Press, 2013) is much more accurate.

[iii] See B.I. Kaffman, *Trade and Aid: Eisenhower's Foreign Economic Policy, 1953-1961* (Baltimore and London: Johns Hopkins University Press, 1982).

[iv] The idea of the 'aid regime' is taken from Robert E. Woods, *From Marshall Plan to Debt Crisis: Foreign Aid and Debt Choices in the World Economy* (Berkeley: University of California Press, 1987).

[v] On development economics see Albert O. Hirschman, 'The rise and decline of development economics', in *The Essential Hirschman* (Princeton: Princeton University Press, 2013) and Stuart Corbridge, 'The (im)possibility of development studies', *Economy and Society*, 36(2) 2007, 179-211, On modernisation theory see Nils Gilman, *Mandarins of the Future: Modernization Theory in Cold War America*, (Baltimore and London: Baltimore University Press, 2003).

[vi] On the bias of the system and exploiting its loopholes towards see Ha-Joon Chang, *Bad Samaritans: The Myth of Free Trade and the Secret History of Capitalism* (London: Bloomsbury, 2007). On China's success in spite of Bank and Fund advice, see 'Chinese growth's contribution to poverty reduction challenges IMF and World Bank neoliberal policies,' *Bretton Woods Observer*, 6 December 2017, https://www.brettonwoodsproject.org/2017/12/chinese-growths-contribution-poverty-reduction-challenges-world-bank-imf-neoliberal-policies/

[vii] See Robert L Ayres, *Banking on the Poor: The World Bank and World Poverty*, The MIT Press, Cambridge, MA, 1983, 102-109, 226-227; Susan George, How the Other Half Dies: The Real Reasons for World Hunger, Allanheld, Osman and Co., Montclair, NJ, 1977, 104-105;

[viii] See for example, Eric Toussaint, 'The World Bank and IMF Support to Dictatorships,' Committee for the Abolition of Illegitimate Debt (CADTM), 6 May 2019. http://www.cadtm.org/World-Bank-and-IMF-support-to-dictatorships Bello, Walden 'Development and Dictatorship: Marcos and the World Bank' in Walden Bello and Severina Rivera (eds) *The Logistics of Repression and Other Essays*, Friends of the Philippino People, Washington DC, 1977, 91-133.

[ix] See Cheryl Payer, *The Debt Trap: The International Monetary Fund and the Third World* (New York and London: Monthly Review Press, 1974).

[x] For an insider analysis of the Bank's role in this era see Devesh Kapur, John P. Lewis, and Richard Webb, *The World Bank: Its First Half Century*, The Brookings Institution Press, Washington DC, 1997. For a critical analysis see Susan George and Fabrizio Sabelli, *Faith & Credit: The World Bank's Secular Empire* (Boulder, Co.: Westview Pres, 1994).

[xi] See Stuart Corbridge, *Debt and Development* (Blackwell, 1993) and Michael Goldman, *The Wold Bank and Struggles for Social Justice in the Age of Globalisation* (New Haven: Yale University Press, 2005); see especially Joseph Stiglitz, *Globalization and its Discontents* (New York: W.W. Norton, 2002).

[xii] On the 9/11 attacks impact on the global justice movement see David McNally, 'From the Mountains of Chiapas to the Streets of Seattle: This is What Democracy Looks like,' in Jai San (ed), *The Movement of Movements, Part 1: What Makes Us Move?* (Oakland and New Delhi: Open World, 2017, 47-68).

[xiii] Patrick Bond, 'World Bank Punches South Africa's Poor and Coddles the Rich, ' Committee for the Abolition of Illegitimate Debt (CADTM), 12 February 2016, http://www.cadtm.org/World-Bank-punches-South-Africa-s.

[xiv] Kevin P. Gallagher & Richard Kozul Wright, *A New Multilateralism for Shared Prosperity: Geneva Principles for a Global Green New Deal*, Boston University Global Development Policy Centre & United Nations Trade and Development Conference on Trade and Development, April 2019.

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