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The Stabilization and Structural Adjustment Procedures of the International Monetary Fund and the World Bank

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The Stabilization and Structural Adjustment Procedures

of the International Monetary Fund and the World Bank

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BY

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The Stabilization and Structural Adjustment Procedures of the International Monetary Fund and the World Bank

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Abstract

The IMF and the World Bank began to attach structural adjustment restrictions to many of their loans to developing countries in the early 1980s. Some of these restrictions are not based on solid economic ground and are, in many cases not effective in improving the economic standing of the countries that receive loans. In addition, there was also a misdiagnosis of the problems that occurred in the underdeveloped countries of the world. Under the IMF/World Bank paradigm, the difficulties that most underdeveloped countries experienced were due to internal distortions and non-effective development strategies. Evidence to the contrary shows that many of the problems that these underdeveloped nations experienced in the 1970s and early 1980s were mainly exogenous and out of the control of the individual countries, such as: Two severe oil shocks, a world wide recession, and increased real interest rates.

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Table of Contents

Chapter 1:

Components of Stabilization and Structural Adjustment Programs Imposed by the World Bank and the International Monetary Fund

Introduction

The International Monetary Fund (IMF) and the International Bank for Reconstruction and Development otherwise known as the World Bank (WB or the Bank) emerged out of the Bretton Woods Conference in 1944. The stated intent was to help foster more economic "openness" around the world. The IMF's policy was to loan nations (mostly war ravaged European nations after World War II) money to assist with balance-of-payments difficulties and interest owed to other banks for previous loans (George and Sebelli, 1994, p. 10). The World Bank was mainly concerned with providing loans for specific development projects, and with the reconstruction of Europe and Japan

Soon after its inception, the World Bank quickly became the largest supplier of infrastructure to the underdeveloped world (George and Sebelli, 1994, p. 2). However, in later years, critics have seen flaws in their policies. The Bank's policies have dislocated entire communities, destroyed large sections of forests, turned grasslands to desert, and transferred land and wealth to the hands of a few rich farmers and entrepreneurs -- all in the name of development (George and Sebelli, p. 2).

When the World Bank first arrived on the international scene, the focus for loans was to help borrowing countries with specific difficulties in their infrastructure. Between the years of 1961 and 1965, 76.8% of all WB loans were for electric power or for transportation, and only 6% of these loans were for agricultural development projects (Ayers, 1983, p. 2). This focus later changed to projects that placed emphasis on the natural resources of the economy. In many countries the emphasis was on agriculture production and export. In countries like Mexico, the emphasis was on fossil fuels such as oil.

When Robert McNamara became President of the World Bank, he began a move toward agricultural investment. He saw that agricultural investment for exports was the way for these countries to get their people out of poverty (Ayers, 1983, p. 2). However, in many cases the end effect was that the agricultural workers/owners he "intended" to help were devastated. This was in part due to IMF/WB recommended policy changes and because of exogenous economic factors that caused agricultural prices to bottom out.

Over the years, restrictions attached to the loans have also changed. In the early stages, loans were given with few restrictions. They were mainly concerned with the country’s debt service ratio. This was the ratio of a country's interest and amortization payments on its' public and publicly guaranteed debt to the country’s earnings from exports of goods and services (Ayers, 1983, p. 3). Beginning in the late 1970s and early 1980s, most loans were given with conditions. In exchange for the money (which they still had to repay with interest) the borrowing countries would agree to certain stipulations, which would move their economies to be more open and "market friendly."

It was (and still is) the belief that if these economies were forced to adhere to these new IMF/WB economic standards that they would foster growth and push these countries further up the development hill. In my opinion, the IMF and the World Bank have not succeeded in their tasks in many areas of the world. Also, in many cases, the negative externalities associated with IMF/WB policies have exceeded the supposed gain.

The *1991 World Development Report* defines economic development as, "A sustainable increase in living standards that encompasses material consumption, education, health, and environmental protection" (World Bank, 1991, p. 31). The publishers of the *WDR*, namely the World Bank, believe that countries who achieve rapid and successful development exhibit two characteristics: They invest in the education of men and women, i.e. human capital; and from these human capital investments the country achieves a high level of productivity by giving leading roles to markets, competition, and foreign trade (Fanelli, Frenkel, and Taylor, 1992, p. 1). Theoretically, these general beliefs are then molded into policy provisions. However it is ironic, given the *1991 WDR's* definition of development, that in many cases the

IMF/WB policies actually force the project countries to cut back on human capital investments rather than to embrace it as a necessity for development.

At the outset of their creation, the roles of the IMF and the World Bank were quite different. The function of the International Monetary Fund was to extend short-term balance-of-payments support to countries experiencing temporary payment difficulties (Payer, 1982, p. 103). The World Bank, on the other hand, was supposed to lend funds for economic development (Payer, p. 109). The WB would lend funds for specific development projects such as transportation improvements or new electrical power facilities (Payer, p. 109). Although their missions were different, the two institutions sometimes worked hand in hand.

Over the years the provisions associated with receiving IMF loans changed. They (IMF/WB) began to insist on increasing levels of economic restructuring. Around 1980, the IMF began to issue loans with a specific package of economic "improvements." Table 1.1 gives a good representation of the economic policies the IMF/WB insisted on.

In recent years the relationship between these institutions has been solidifying and their loan processes have become more aligned. The World Bank began making loans which held to the standards of the new IMF restructuring policies. These new (late 1970s and early 1980s) World Bank loans were called "non-project" loans (Payer, 1982, p. 109).

This newly introduced cooperation intensified in 1988 when the Structural Adjustment Facility (SAF) was created (Bello, 1994, p. 30). This organization was set up to oversee the economic policies set in place by the IMF/WB's technocrats (Bello, p. 30).

> The unification of the IMF and the World Bank treatments came to be known to its patients as "shock therapy" or the simultaneous application of short term stabilization measures and more long-term structural reforms. It was not without reason that adjusting countries came to label the two institutions with derision as the "Bretton Woods Twins" (Bello, p. 30).

In addition to the loan conditions listed in Table 1.1, the country had to agree to stringent monitoring by the Bank and/or the IMF in order to ensure the country met the agreed upon targets (Bello, 1994, p. 27). These targets were specific figures that the IMF/WB wanted the country to reach by "improvements" in specific areas of the economy. Namely, the current account balances, fiscal balances, trade balances, and monetary balances.

After agreements were reached, the payments could begin. However, the disbursements of the loans were made in increments. If the country would fail to meet the "targets" or fail to cooperate in the reform procedures, then the IMF/WB could hold back payments or refrain from issuing any further loans. Because these reforms covered such a broad economic area and were so radically different (relative to the previous economic policies), these loans essentially meant that they were turning over control of the entire economy to the IMF/WB (Bello, p. 27).

Table 1.1

Typical Conditionally for IMF/WB Loans

Area of Reform	*Suggested Reform*	*WB/IMF's Rationale for the Reform*
Fiscal Policy	* the country must reduce fiscal deficits by decreasing government expenditures (in practice this means cutting spending in: health, education and welfare)	* this reform would reduce inflation and reduce the demand for capital inflows from abroad
Trade Policy	* lift export restrictions	* encourages exports, helps to improve trade imbalances and seen as a good source of growth
	* institute incentives for domestic export industries	* encourages exports, helps to improve trade imbalances and seen as a good source of growth
	* liberalize quantitative import restrictions and cut import tariffs	* strengthen the competitiveness of domestic industries as well as improve industry efficiency
Monetary Policy	* devalue domestic currency (relative to hard currencies)	* promotes export oriented strategy (i.e.: makes exports more affordable/competitive)
Financial Sector	* improve regulatory framework (i.e. deregulate industry)	* improves confidence in the system
	* relax interest rate ceilings (allow/pressure interest rates to rise) and reserve requirements	* provides incentives for efficient use of resources
Industrial Sector	* eliminate restrictions on foreign investment in industry and financial services	* makes domestic production and business activity more efficient due to the presence of foreign competition
	* remove price controls	* Improves resource allocation
Agricultural Policy	* deregulate agricultural trade and lift any price controls	* help the agricultural sector become more efficient and to encourage exports

Note. From Bello, 1994, p. 27 and Reed, 1992, p. 27.

The overall intent of these structural reforms was to make the economy more internationally "market friendly." The *1991 World Development Report*, entitled "The Challenge of Development", cites several studies including those by Bhagwati (1978) and Kruger (1978) to demonstrate that free-market ("non-distorted") economies are the best environments for fostering a desirable level of development (Fanelli et al., 1992, p. 1).

However, Fanelli, Frenkel, and Taylor have countered that the *1991 World Development Report's* (i.e. the World Bank's) argument for their policies has "both loose ends and missing information" (Fanelli et al., 1992, p. 2). An example of this would be, blaming the underdeveloped countries for their severe debt accumulation on governmental inefficiencies and ineffective government policies, while ignoring the international conditions effect on these economies. The World Bank conducted research with hopes of explaining the causes behind the developing countries' difficulties in the mid to late 1970s. They conducted an analysis of sixty-eight developing countries, and they analyzed the impact of labor and capital on the level of output.

> Since the sum of the contributions of those two factors of productivity (labor and capital) fails to account for overall growth, the residual or "total factor

productivity" (TFP) growth is identified with the efficiency of using inputs - in standard neoclassical fashion. The *WDR* (*World Development Report*) tries to explain variations in residual "efficiency" in terms of the market friendliness of economic policy (Fanelli et al., 1992, p. 2).

The *1991 WDR* also singles out other factors for determining growth, and the first and most important of these is education. The *WDR* statement that the returns from education are high is largely indisputable (World Bank, 1991, p. 43).

The second factor is the domestic policy adopted. Specifically, the WB believes that a strategy of import-substituting industrialization (ISI) is detrimental to long run development. ISI strategies according to the World Bank have, for the most part, experienced disappointing results because, among other factors, protected industries have failed to mature and the anti-export bias from protection has impeded growth in exports especially in the area of agriculture (World Bank, 1991, p. 42). Fanelli et al. found in the *1991 WDR* (p. 45) that, "A strategy of import-substituting industrialization may artificially increase investment at the outset but may have grave long-term costs in terms of low efficiency and slow technical progress, i.e. low productivity growth" (Fanelli et al., 1992, p. 2).

In many cases this philosophy fails to hold much weight. As I will discuss in Chapter 3, countries like Mexico experienced their best rates of growth under ISI strategies. In the ISI years from 1965 through 1980, the country experienced an average growth rate of 6.5% per year (World Bank figures from the *1988 WDR*). Mexico has failed to come close to those figures since then.

The third suggested WB factor necessary to obtain growth and high productivity is external openness (Fanelli et al., 1992, p. 2). The fourth WB factor is that economic instability diminishes the return of investment and growth of output (World Bank, 1991, p. 42).

The WB's fifth growth contributing factor is one I have great difficulty in rationalizing or accepting. According to the WB, "external factors such as changes in terms of trade, growth of OECD economies, international interest rates, and capital flows are asserted not to account for differences in the performance of individual countries" (Fanelli et al, 1992, p. 2). Although the *1991 WDR* does not provide much supporting evidence for this claim (see the effects of external factors page 46-47 in the *1991 WDR*), it does however cite one case study. They cite a bank sponsored research project by Mitra et al. (1991) which found no statistical association between exogenous factors, such as those mentioned above, and the level of output (World Bank, 1991, p. 42). However, as will be shown in Chapter 2, there is overwhelming evidence to the contrary.

The *1991 WDR* compares the 1960-1973 and the 1973-1987 periods. They argue that slower output growth almost everywhere after 1973 was due to a lower residual, or a less friendly atmosphere for investment (World Bank, 1991, p. 43 & 45). As I will argue later in this paper, this view that the problems that the Third World experienced in the 1970s were caused by their own "unfriendly markets" or by inefficiency in production, is flawed. Exogenous factors such as the Third World debt crisis, two oil price shocks, and two world wide recessions had a detrimental effect on the Third World economies and have been major factors in their difficulties.

Stabilization Procedures

The IMF/WB loans came with two sets of conditions: Policies intended to bring about economic stabilization, and policies which insist on significant economic structural changes. The stabilization policies focus on cutting the inflation rate and the trade deficit by restricting aggregate demand through cutting governmental expenditures, and through monetary restrictions (Taylor, 1994, p. 40-41).

> Without fundamental changes in international credit conditions there is still a risk that IMF-inspired adjustment policies will drive their recipients toward prolonged "stabilized stagnation," because these policies ignore crucial macroeconomic factors such as linked foreign exchange and fiscal constraints,

> financial fragility, and the dynamics of the inflation process (Fanelli et al., p. 15).

For example, the IMF/WB paradigm operates on the assumption that increases in prices are caused by increases in the money supply. If the price increases are caused by supply rigidities, then tightening the money supply is the wrong prescription.

The *1991 WDR* states on page 8 that when government spending has gone too far (excessive years of fiscal deficits), the result is excessive borrowing, overvaluation of the currency, a high level of inflation, and a loss of export competitiveness (World Bank, 1991, p. 8). This view follows the logic that fiscal equilibrium is sufficient and necessary to bring about stabilization. Following this path can be very dangerous, "because it ignores structural features linking the saving, external and fiscal gaps and thereby understates the complexity of stabilization, especially if stagnation is to be avoided" (Fanelli et al., 1992, p. 15).

The second feature of the stabilization process is monetary policy "reform." Over the last fifteen to twenty years, unsustainable current account positions, governmental instability, financial crashes, capital flight, and high levels of inflation or hyper-inflation (particularly Latin America) have been the salient features of economic instability in the underdeveloped world (Fanelli, et al., 1992, p. 16).

The *1991 WDR* does acknowledge that these difficulties can be part of the economic problems of the underdeveloped world, in the short run, but there is little discussed about it. The long-term effects of these difficulties are not recognized (see *1991 WDR* p. 44-45).

Despite the acknowledgment that these problems can have detrimental short-run effects on the economy, a major reform is the devaluation of the domestic currency relative to hard currencies. This generally has the obvious economic effects: Imports become more expensive and therefore citizens can not afford what they once did (e.g.: U.S. exports to Mexico have fallen in 1994-95 due to devaluation's of the Peso); exports become cheaper; anyone (primarily the low income sectors) who holds domestic currency (as opposed to capital or hard currencies) has less buying value now and cannot afford to buy as much food/commodities as they once did, let alone save anything.

The third stabilization procedure is an effort to bring about anti-inflationary policies. The WB places a high priority on this (Fanelli et al., 1992, p. 17).

Fanelli, Frenkel and Taylor lay out five general methods of reducing inflation on p. 17-18.

(A) Relative prices can be manipulated. e.g.: the exchange rate can be allowed to appreciate in real terms or the real wage to fall (by allowing the nominal exchange rate or wage to rise less rapidly than a general index of prices).

(B) Imports can be increased to ease local supply bottlenecks. Often, purchases abroad must be financed by the central bank as it spends reserves to support an exchange rate pegged as a price anchor.

(C) Income policies and other forms of market intervention can be deployed to muffle the most conflicting social claims. The most obvious is the "social pact" to reduce wage inflation while holding profit claims in line.

(D) In a more extreme case, a price freeze plus contract deindexation - "heterodox shock" in the jargon - can be attempted as a policy surprise.

(E) Austerity can be applied, i.e.: a cut in the government expenditures coupled with the monetary restriction based on increased interest rates and credit restraint.

As seen in Table 1.1, the IMF/WB usually leans toward the austerity approach (cut government expenditures, devaluation, and increase domestic interest rates). Obviously each one the above five techniques is unique, just as each one of the Third World countries is unique. I find it far fetched to believe that the austerity approach is the only effective approach. Perhaps it would be more prudent to examine each country individually and to then determine the best course for action. As noted by Lance Taylor, austerity is more effective in economies in which prices are free-floating, which does not describe many of the Third World countries in question (Taylor, 1994, p. 58).

In actual practice, the IMF combines austerity with real wage cuts and reductions in income support programs and subsidies (for the poor and needy) (Taylor, 1994, p. 58). The end result is a reduction in demand (partly due to laid off workers), output contraction, and a lower trade deficit (due to the decrease in imports because the people can no longer afford them due to the devaluation of the currency and because of their lower income) all in the name of inflation fighting (Fanelli et al., 1992, p. 18).

It is not just the fiscal restraint approach that can harm individuals. The real problem exists when policies such as austerity are combined with domestic currency devaluation, efforts to raise interest rates, and the elimination of income support programs. This hits the poor disproportionately. First with respect to the devaluation, since low-income sectors generally hold much of their wealth in cash (domestic currency), their "nest egg" is now not worth what it used to be. Then the government is forced to cut expenditures including food assistance programs, health assistance programs, and small business (like small farmers) assistance. Then interest rates are pushed up, which discourages the poor from applying for loans for a small business or to buy a tractor (a technological improvement).

As an example, the implementation of austerity programs in Latin America has resulted in reduced levels of earnings for the working class. Between 1980 and 1985, the average per capita income in 23 Latin American countries fell 9% while austerity were implemented (this was also due to the world recession from 1980-82) (Hakkert & Goza, 1989, p. 74). On an individual country basis other workers have been devastated. In Costa Rica, during the implementation of an austerity program, real wages fell 40% between 1979 and 1982.

Exchange rate policy is the fourth procedure necessary, according to the IMF/WB philosophy for economic stabilization. The *1991 WDR* states that it is necessary to maintain a competitive exchange rate, in order to close the external gap (balance of payment difficulty) and this involves an early devaluation (Fanelli et al., 1992, p. 18). The costs associated with importing goods have now gone up because of the "weaker" domestic currency.

"Problems arise in coordinating devaluation with other policies, in both stabilization and adjustment contexts" (Taylor, 1994, p. 59). If this process of devaluation is combined with a expansionary policy, it could be very beneficial for the economy (Fanelli et al., 1992, p. 19). But this is not the case under the IMF/WB paradigm. As shown in Table 1.1, a key element to the program is that government budgets must be slashed for the benefit of a balanced budget.

When contractionary fiscal policy is combined with currency devaluation the outcome can be devastating.

> When devaluation is added to this policy of monetary and fiscal austerity to promote exports and earn foreign exchange, it escalates the contractionary effects by raising the local cost of imported capital and intermediate goods, leading to the policy "overkill" for which the IMF is justly famous [or infamous] (Bello, 1994, p. 36).

This economic contraction scares off private domestic investment and if left to itself, the economy usually does not provide signals to renew investor confidence in the economy (Bello, p. 36).

The *1991 WDR* defines stabilization procedures as methods that "work mainly on the demand side to reduce inflation and external deficits," while "structural policies are concerned with the supply side; they address the efficiency of resource use, the emphasizing of reforms in specific sectors -- especially trade, finance, and industry" (World Bank, 1991, p. 113).

Structural Change

Liberalization of trade is one of the IMF/WB's priorities in their structural reform procedures. The IMF/WB believe that the "free market" approach is absolutely necessary in order to solve the problems of underdeveloped "distorted" economies. Others feel that trade liberalization should be a less important procedure, or not a procedure at all, in order to bring about growth and prosperity to these underdeveloped countries. "Trade policy orientation, while important, may not be a dominant determinant of growth and may not therefore deserve the attention the World Bank and others have given it" (Hellinger, 1990, p. 884).

Walden Bello echoes these arguments; he also argues that trade liberalization does not spark investment and growth. He uses the example of the agricultural sector. The IMF/WB philosophy focuses on lifting price controls on commodities and ignores the more important deep rooted problems such as: structural, technological, and infrastructural deficiencies that must be addressed in order to increase efficiency and productivity (Bello, 1994, p. 36). The difficulties are usually addressed by way of state-supported programs, which are being slashed in order to bring about fiscal equilibrium (Bello, 1994, p. 36). Bello cites cases in Africa in which the WB, through their deregulatory policies, allows the free market to determine the price for fertilizers. In many cases this led to reduced applications, lower yields, and lower agricultural investment because of the absence of state-supported credit systems (Bello, p. 36).

Why has the IMF/WB placed such a high priority on the removal of any "market distorting" trade policies? Fanelli, Frenkel and Taylor (1992) seem to feel that the IMF/WB rationale is based on textbook theories. The World Bank uses the example of a country that has been under long-term ISI strategy. This country usually exhibits a high and complicated tariff structure and/or strict import quotas (Fanelli et al., 1992, p. 21). Most economists feel that this complicated protectionist structure could be simplified, streamlined and reduced, but how far to go and how quickly are the questions that are very controversial. The IMF/WB policies require a swift and severe approach to reduce trade restrictions.

Fanelli et al. suggest that the problem with the IMF/WB paradigm is the set of underlying assumptions. For instance, consider the belief that the free-market will alleviate market distortions and inefficiencies. As Fanelli describes it, "Their deficiencies lie in the incompatibilities between their underlying assumptions and the world as it really functions" (Fanelli et al., 1992, p. 22). In the real world the free-market can lead to distortions such as trans-national corporations, local monopolies, and the divide-and-rule tactics of the domestic entrepreneurs that take severe advantages of labor (Fanelli et al., 1992, p. 22).

Also the IMF/WB's empirical basis relies on models with assumptions of full employment and investment determined by savings (Taylor, 1994, p. 66). When protectionism is placed into an investment-driven growth model, it can be easily lead to faster overall expansion (Fanelli et al., 1992, p. 22). Obviously protectionism can be effectively utilized, which is more than can be said for the orthodox reforms demonstrated in Argentina in the late 1970s. The IMF/WB got their signals wrong, and their reforms led to aborted economic growth for at least a decade (Taylor, p. 66).

Economist David Evans uses Chile as an example of effective protectionism. The governments protection of the fruit, forestry, and fishing industries led to an economic export boom in 1985 (Evans, 1991, p. 10). This was done in part through governmental support of technological investments, financial support through subsidized loans, and through informational/educational means. This was a relief after 12 years of disastrous stabilization supported by the IMF/WB (Evans, 1991, p. 12).

Although there have been protectionist failures too, the point is that there should be debate over the issue for each individual country, because it is not such a cut and dry situation as the IMF/WB lays out. One of the key intents of a liberalized market is to increase technical efficiency. Rodrick suggests that if "truth in advertising were to apply to policy advice, each prescription for trade liberalization would be accompanied with a disclaimer: Warning! Trade liberalization cannot be shown to enhance technical efficiency; nor has it been empirically demonstrated to do so" (Fanelli et al., 1992, p. 23).

Another reform in the IMF/WB philosophy is financial reform. The basic strategy is to increase interest rates and deregulate the financial system which would in turn increase allocative efficiency (Fanelli et al., 1992, p. 23). "Just as price liberalization does not ensure that firms will efficiently produce commodities there is no particular reason to expect that removing wedges separating rates of return will guarantee a low-cost supply of financial services" (Fanelli et al., p. 23). At times, when applied, this financial reform leads to reduced efficiency in finance, which lead to increased credit costs (Fanelli et al., p. 23). This is true in part because the IMF/WB method of removal of state interventions/distortions at times leads to market distortions such as monopolies and oligopolies which have great power in the control of credit. Because of the lack of competition the financial institutions take advantage of their market power and charge excessive rates. Also, a rise in interest rates may lead to a decrease in domestic investments and capital improvements, thus contracting the economy.

In addition, the policy of financial reform becomes difficult in the context of other loan restrictions. "Reform of the financial sector often calls for distressed financial institutions to be restructured; in the short-run this may raise public spending and make it harder to cut the budget deficit" (World Bank, 1991, p. 115).

Chapter 2:

Was there a Misdiagnosis of the Problems in the Third World and Were the New Adjustment Procedures the Wrong Prescription?

During the late 1970s and early 1980s many countries of the underdeveloped world began to experience significant difficulties. They began to have serious debt burdens, declining levels of export earnings, increasing fiscal deficits, increased levels of inflation, increasing levels of unemployment, as well as slower economic growth. Why were these countries having such great difficulties?

The IMF's economists have blamed the governments for all of the problems experienced by Latin America in the pre-1982 period (Pastor, 1993, p. 291). They point to restrictive trade practices, price supports, fiscal expansion and exchange rate overvaluation (Pastor, p. 291). As discussed in Chapter 1 the WB describes it as a high level of "inefficiency" or in other words it was due to an increased level of "market distortions."

It is true that the governmental policies and their management are partly to blame for these problems. But to point to governmental management of the economy (as indicated by the IMF/WB philosophy) as the sole reason for the difficulties is just not realistic. Other factors on the international economic scene during this time period had their effects. Is it possible that exogenous factors such as severe amounts of Third World debt accumulation, a world-wide recession, two severe oil shocks, an overall drop in agricultural commodity prices had an effect on these Third World countries? My answer is yes. These external factors did play a major role in the problems associated with the underdeveloped world.

The IMF/WB's view was that the difficulties in the "South" were internal and that serious adjustment needed to be made. Structural adjustment was introduced in 1980 by Robert S. McNamara, formally the U.S. Secretary of Defense, and then the President of the World Bank (George and Sabelli, 1994, p. 58). This structural adjustment (SAP) would become a requirement if a country wished to receive financial assistance from either the World Bank or the IMF (George and Sebelli, p. 58). Also the power of the IMF and the WB wield is evidented from the fact that if these countries refused to accept this SAP, other private financial institutions would likewise generally refuse to loan funds to these countries. In order to deal with an increasing debt burden, many countries were left without an alternative.

One of the obvious exogenous factors that should be considered, is the debt crisis of the Third World. The growing debt crisis surfaced visibly and unavoidably in 1982, when Mexico threatened default on their debt (Walton and Seddon, 1994, p. 15). As Table 2.1 indicates, non-oil exporting developing countries began accumulating large amounts of debt by the late 1970s and the early 1980s. Total external debt increased nearly five fold between 1973 and 1982 (Cline, 1984, p. 1). When adjusted for inflation, the total debt does not look as severe, but none the less there is a 210% increase in total debt over this time period (Cline, p. 1).

Table 2.1

Indicators of External Debt of Non-oil Exporting Developing Countries 1973-1982 (Billions of Dollars)

	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982
External debt:										
Total	130.1	160.8	190.8	228.0	278.5	336.3	396.9	474.0	550.0	612.4
Long Term	118.8	138.1	163.5	194.9	235.9	286.6	338.1	388.5	452.8	499.6
Total('75 prices)	169.0	175.7	190.8	218.0	250.9	281.0	294.7	308.6	331.3	357.8
Exports	112.7	153.7	155.9	181.7	220.3	258.3	333.0	419.8	444.4	427.4
Debt/Exports (%)	115.4	104.6	122.4	125.5	126.4	130.2	119.2	121.9	124.9	143.3
Debt service/ exports (%)										
Reported	15.9	14.4	16.1	15.3	15.4	19.0	19.0	17.6	20.4	23.9
Adjusted	N/A	-1.6	6.5	10.5	9.4	11.0	6.9	4.9	11.7	22.3
Debt/GDP (%)	22.4	21.8	23.8	25.7	27.4	28.5	27.5	27.6	31.0	34.7
Oil as a % of imports	5.9	12.6	13.3	15.6	15.1	13.9	16.2	20.4	21.0	19.9

Note. From Cline, 1984, p. 2-3. Exports were goods and services only. Debt service figures include interest but not amortization on short term debt. The adjusted figures for debt service as a percentage of exports subtracted the inflationary erosion of debt.

One could point to the fact that export earnings have also increased four fold over this time period. But, this is less convincing when debt-service burden as opposed to debt itself is calculated (Cline, 1984, p. 2). The debt service burden became a problem primarily because of rising interest rates. Debt service (interest on short and long term debt plus amortization on long term debt) rose from 15.9% of exports of goods and services in 1973 to 24% in 1982 (Cline, 1984, p. 3).

The overall trend in Table 2.1 shows that while the increase in debt burden is not as severe when measured in the real terms relative to the export base (Cline, 1984, p. 4). But, by 1981 the burden of debt rose significantly according to three principle measures: Ratio of debt to exports, real (adjusted) debt service ratios, and ratio of debt to GDP (Cline, p. 4). In the following year 1982, these burdens rose even further to levels never experienced before (Cline, p. 4). Despite these warning signs, the massive accumulation of debt in the Third World continued during the 1980s.

The problem is seen more clearly when the countries involved in the debt crisis are broken down into income categories. Middle income countries as a whole increased their debt to GDP ratio from 36.1% in 1980 to 46.1% in 1989. Lower-middle income countries increased their debt to GDP ratio from 37.7% to 67.7% (Walton and Seddon, 1994, p. 15). However, the most shocking figures are seen in the lower-income category (other than India and China). These countries increased their ratio from 27.0% in 1980 to 71.0% in 1989 (Walton and Seddon, p. 16).

A primary cause of the sharp deterioration in growth in 1982 was a decline in the nominal value (by 3.8%) of exports even as total debt continued to rise (10.3%) (Cline, 1984, p. 5). Export stagnation was driven by three factors: A global recession (which caused export volume growth to decline), by appreciation of the U.S. dollar (which lowers the dollar value of export earnings), and by commodity price erosion (Cline, p. 5). As Table 2.1 illustrates, the issues surrounding debt burdens played an important role in plunging non-oil exporting countries further into trouble. A closer look at some selected countries up shows it played a much larger role. In Table 2.2 export growth of goods and services is compared to the LIBOR + 1%. The LIBOR (London Interbank Offer Rate) is an international interest rate which many international loans including many IMF/WB loans are set.

For the most of 1973-80 period, the LIBOR + 1% averaged 10.2%, while export growth averaged 21.1% (Cline, 1984, p. 8). This growth in exports was obviously covering the average interest rate of 10.2% the country's were paying. The interest rate was being clearly met and overfulfilled.

As the table indicates the first incident occurred in 1975. Countries that were experiencing prosperous export activity (Argentina, Venezuela, Chile, and Mexico) were plunged into severe export difficulties. The 1975 downturn would turn out to be quite deep, and at the time was the most severe economic downturn since the Great Depression (Cooper, 1992, p. 2). The market eventually recover by the year 1978.

Table 2.2

Export Growth Compared With Interest Rates,

1973-1982 (Export Growth is in a Percentage Form)

	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982
LIBOR + 1 percent	10.2	12.0	8.0	6.6	7.0	9.7	13.0	15.4	17.5	14.1
Export growth, nominal										
non-oil LDC's	N/A.	36.4	1.4	16.5	21.2	17.2	28.9	26.1	5.8	-3.8
net oil importers	N/A.	33.1	1.6	16.3	21.9	16.9	26.8	24.2	5.4	-3.8
net oil exporters	N/A.	57.3	-0.1	18.9	18.8	18.0	40.4	35.4	7.8	-3.6
Brazil	56.1	33.2	6.1	13.5	19.7	7.2	24.2	29.3	15.7	-13.4
Mexico	26.8	31.6	-0.2	13.3	14.0	39.1	40.2	54.3	21.9	7.3
Argentina	61.6	25.8	-23.9	30.8	43.6	16.3	26.6	13.0	5.1	-15.7
Korea	85.6	29.4	9.7	60.8	38.2	31.3	13.8	15.6	21.7	2.3
Venezuela	54.4	126.8	-15.7	2.8	5.5	-0.8	50.2	36.4	10.1	-22.0
Chile	49.0	60.1	-21.7	31.7	8.1	13.8	59.0	32.2	-2.6	-3.8

Note. From Cline, 1984, p. 6-7. Exports were goods and services only.

But the problems of the downturn were not as severe as the one that occurred in 1981-1982. "The difference between the interest and export-growth was smaller (6.6% in 1975 compared with an average of 14.8% in 1981-82), reflecting that the 1975 recession was shorter and less severe. Moreover, the relative severity of the debt burden was milder going into the 1975 recession (as measured by debt relative to exports and GDP, and the debt service ratio, Table 2.1)" (Cline, 1984, p. 8).

The world recession in 1981-1982 period was in many respects more severe than the one experienced six years before (Cooper, 1992, p. 4). This was due to the extremely high interest rates in the early 1980s, which can be seen by the movement of the LIBOR during this time period.

Overall, the relative debt burden sharpened severely in the 1981-82 period, in addition to the milder recession of 1975 (Cline, 1984, p. 8). The debt problems experienced were also affected by endogenous factors, such as: Interest rate decisions, domestic budgetary policies, governmental inefficiencies, and corruption. But it is quite clear that exogenous variables played a powerful role in accelerating the debt burdens.

Another one of the exogenous factors that led to difficulties for these developing countries was the two oil shocks. This had the most powerful negative effect on their debt difficulties.

In December of 1973 the Organization of Petroleum Exporting Countries (OPEC) ministers increased the market price of oil from $3.60 per barrel to $11.65 per barrel (a three fold increase) (Cooper, 1992, p. 1). In 1970 oil was only $1.35 per barrel (Cooper, p. 1). This began the first episode of international financial instability. This occurred at a time when the demand for oil was quite high because the world economic growth up to the 1972-73 period was quite rapid, as compared to post-1973. From 1968 to 1973 the quantity of oil demanded increased from 19 million barrels per day to 30 million barrels per day (Cooper, p. 2). This was the largest per unit oil-shock ever experienced.

Cooper argues that we are still feeling the effects of the first oil shock today, in the form of accumulated debt and the memories of the subsequent turbulence (Cooper, p. 2). These effects will continue to affect policies for years to come (Cooper, p. 1).

World oil markets had become relatively calm by mid-1978, and oil prices had actually declined somewhat in real terms from 1974. Then turmoil developed in Iran. Oil field workers went on strike in December of 1978, which caused about five billion barrels of crude per day to be removed from the market (Cooper, 1992, p. 21). Oil workers eventually returned to work but production levels would never be as high as they were before. Subsequently, other producers reacted and oil prices rose again. At that time, there was great disagreement in the OPEC community about production levels and prices. By March of 1981 prices reached $33 per barrel. This was an increase of 150% over two years.

Needless to say oil importing countries found themselves in great difficulties, much like they had experienced in the first shock. But, this time there were additional factors that made the situation much worse, including higher real interest rates. At the time, a great portion of their overall debt was maintained at market rates, rates that were unusually high. Their debt was usually pegged to the LIBOR (two-thirds of the Third World debt was pegged to the LIBOR) or the U.S. prime rate (Cooper, 1992, p. 22). The LIBOR averaged 17.5% in 1981.

Oil importing countries had some decisions to make. They had to decide how much to contract imports and how much to borrow to cover the additional import bill (Cooper, 1992, p. 22). In most cases, these oil importing countries found themselves in severe debt difficulty. Because of the instability in their respective countries and also the world wide recession, few private banks or institutions were willing to loan funds. These countries were forced to deal with the IMF/WB to get the necessary funds to cover their debts.

The effect of relatively high oil prices and interest rates can also be seen by the value of oil imports to these Third World nations. As Table 2.1 indicates the value of oil imports rose from 6% of total merchandise imports in 1973 to 20% in 1980-82 (Cline, 1984, p. 8).

Table 2.3 shows the cumulative additional costs of oil imports on the oil importing developing countries (Cline, 1984, p. 10). The second column shows actual net oil imports of these countries over the ten year time period, 1973-82. The third column shows the price that they would have paid if oil would not have risen more than the U.S. wholesale price index after 1973 (Cline, p. 10). As you can see by the table, the cumulative additional costs were $260 billion over the decade.

Table 2.3

Effect of Higher Oil Prices on Debt of Non-oil Developing Countries (Net Oil Importers Only) in Billions of Dollars

Year	Oil Imports Actual (A)	Oil Imports Hypothetical (B)	Additional Cost (C = A - B)
1973	4.8	4.8	0.0
1974	16.1	5.3	10.8
1975	17.3	5.7	11.6
1976	21.3	6.8	14.5
1977	23.8	7.5	16.3
1978	26.0	8.6	17.4
1979	39.0	10.9	28.1
1980	63.2	11.9	51.3
1981	66.7	12.1	54.6
1982	66.7	11.9	54.8
Total: 1974-1982	344.9	85.5	259.5

Note. From Cline, 1984, p. 10. Column B is based on the assumption that oil prices did not rise any more that U.S. wholesale prices.

If we accept Cline's figures, then we have to recognize that oil-price increases alone accounted for over a fourth of the debt incurred by the Third World countries (George, 1988, p. 24) Obviously the effect was greater on the non-oil countries.

> Those outside the charmed circle of oil producers had no choice in the matter: Either they increased borrowing or they allowed their energy starved economies to come to a screeching halt. The option of paying for oil by

dramatically increasing their own exports was not open to them (George, p. 29).

It is not entirely clear what the total effect of the oil shocks was on the developing countries' debt burden or the overall economic standing of the country. What is clear is that the effect was significantly negative, and these shocks should have been considered before the IMF/WB structural reforms were imposed.

Two additional factors that were important in contributing to the crisis were the rise in interest rates and a world wide recession in the 1980-82 period. Borrowers had become adjusted to low real interest rates in the mid to late 1970s. Normally, interest rates are tied to inflation. They tended to rise and fall together (George, 1988, p. 28). But in the mid to late 1970s, interest rates did not rise as much as inflation, thus making the real rate negative (George, p. 28). In some years interest rates were as low as -3% to -4% in real terms (George, p. 28).

But the rub was that in the 1980s interest rates didn't fall as much as inflation leaving debtors holding the bag (George, 1988, p. 28). Every additional point increase in the real interest rate caused the country to incur extra billions in debt service (anywhere from $2 billion to $6 billion per point according to varied estimates) thus forcing these countries to get new loans to pay for their interest payments (George, p. 28). It is easy to see why the indebtedness of these countries began to grow quickly.

Coincidentally with the relatively higher interest rates, the international economy experienced a severe recession in 1980-82 (Cline, 1984, p. 12). "From 1973 to 1979 real growth in industrial countries averaged 3.2% annually. It fell to 1.2% in 1980-81 and -0.3% in 1982" (Cline, p. 12). As a result of the slowdown, the developing countries experienced a drop in the prices of their primary exports. "With 1980 = 100, export unit values fell to an index of 94 in 1981 and 90 for 1982 in non-oil developing countries" (Cline, p. 12). The resulting effect was a loss of $25 billion in export unit values and an import cost increase of $9.6 billion in 1981, and a loss of export unit value in 1982 of $44 billion, with no increase in 1982 import costs (Cline, p. 13). Cline then calculated the total loss to non-oil developing countries due to deteriorated terms of trade, for 1981-82 he estimated this loss to be $79 billion (Cline, p. 13).

In addition, real export volumes (with constant prices) from developing countries fell as a result of the international recession. On average real export volume growth for non-oil developing countries averaged 8.1% from 1971-80, rose to 9.9% in 1981, and in 1982 fell to 1.8% (Cline, 1984, p. 13). This implies a net loss of $21 billion from the trend in real exports (with no price changes), given the average shortfall for the two years (Cline, p. 13).

As shown in Table 2.4 the combined effect of these exogenous factors (on an ex ante, or potential basis) was to increase the debt of non-oil developing countries by $401 billion over the 1973 to 1982 time period (Cline, 1984, p. 13). Table 2.4 shows the actual increases in debt over the time periods in question.

Table 2.4

Effects of Exogenous Shocks on External Debt on Non-oil Developing Countries

Effect	Amount
Oil Prices increase in excess of U.S. inflation, 1974-82 cumulative	$260
Real interest rate in excess of 1961-80 average: 1981 and 1982	$41
Terms-of-Trade loss, 1981-82	$79
Export volume loss caused by world recession, 1981-82	$21
Total	**$401**
Memorandum Items	
Total Debt: 1973	$130
1982	$612
Increase: 1973 - 1982	**$482**

Note. From Cline, 1984, p. 13. Net oil importers only.

Although these numbers can not be directly identified with actual increases in debt (because countries did pursue adjustment measures to reduce external deficits and debt from levels they would otherwise would have reached) these figures do however show the exogenous factors of two oil shocks, abnormally high interest rates, declines in the terms of trade for these developing countries, and falling export volume associated with the global recession did play a dominant role in the debt crisis of non-oil exporting developing countries.

What about the oil exporters such as Mexico, Venezuela, and Nigeria? Didn't they profit from these high prices and enjoy lower debts than they would otherwise would have incurred (George, 1988, p. 29). Didn't relatively higher revenues from oil exports, at least help to prevent the $260 billion debt increase from growing even more (George, p. 29)?

According to Susan George, probably not. First, countries like Mexico borrowed heavily in order to develop their oil industry (George, 1988, p. 29). PEMEX, the Mexican state oil corporation had to borrow $20 billion in 1982 (one-fourth of the Mexican debt) just to keep its program running (George, p. 29). Second, the more oil a country had, the more banks were anxious to push their money at it, confident in the belief that oil reserves would ensure repayment. "Without black gold in the ground Nigeria, for one, wouldn't have looked much like a good credit risk" (George, p. 29).

After the calamities (e.g.: the severe debt accumulation, etc.) the IMF/WB started new adjustment programs for these countries. The IMF/WB attributed difficulties to serious internal distortions. In the eyes of the IMF/WB, the only reasonable solution was to alter the economic atmosphere of these developing countries. They sought to make the market free of inefficiencies.

Were the behaviors of these countries the cause of their difficulties in the early 1980s? As the data shows, these countries were making great strides in export production during the 1970s. They were converting their economies from the WB/IMF's opinion of a "bad" or ineffective development strategy, namely import-substituting industrialization (ISI) to export-led industrialization (ELI).

It is difficult to blame these economies' problems on some product protection, import quotas, or price controls/subsidies. In many cases, these countries needed to protect their infant industries against "dumping" and other untoward practices of the multi-national corporations. Opening an economy entirely up to the market can be deadly, discussed in Chapter 3 in my country analysis section.

The IMF/WB got the issues wrong. Exogenous factors played a serious role in determining the development process of the developing countries. Internal policies needed to be analyzed and perhaps altered in many cases. But to blame internal policies for all of the difficulties that the underdeveloped nations faced in early 1980s is not realistic, and led to counter productive "adjustment" programs.

Chapter 3:

Country Analysis of Chile and Mexico After the Implementation of IMF/WB Programs.

During the 1970s, international lending by banks and multi-lateral agencies increased twelve fold (Walton and Seddon, 1994, p. 98). Latin America and the Caribbean absorbed nearly one-half of the borrowed funds (Walton and Seddon, p. 98). Countries in Latin America, namely Argentina, Brazil, and Mexico have consistently been among the world's largest debtor countries ranked by the absolute size of their external obligations.

Despite the IMF/WB's opinion that the problems of Latin American countries were attributable to unrelated "poor" policies in individual countries, the IMF recommended virtually the same reforms to all of Latin America: Devaluation, reduction in fiscal deficits, and the reduction in real wages (usually done by freezing nominal public sector wages -- and therefore indirectly public sector real wages) (Pastor, 1993, p. 297). "In addition the Fund argued for the relaxation of controls on trade and capital flows in the international sphere, as well as the elimination of subsidies and other interference" (Pastor, p. 297).

Indeed the only price the IMF wished to be regulated was the price of labor. Unfortunately, these wage reductions yielded little export advantage because developed countries were stagnant, and because every other developing country was practicing the same policies (Pastor, p. 297). A reason behind this wage suppression was to inhibit excess aggregate demand. But this would not be necessary when domestic consumption was already contractionary due to a collapsing export market (due to other countries also increasing export levels as well as the economic slowdown in the "North") (Pastor, p. 298).

All of these measures were done to remove any "distortions," in order to allow the market to alleviate any economic difficulties. It seems that the IMF/WB are placing a lot of faith in the "magic of the market."

Chile

Chile is perhaps the country with the longest running SAP in the World (Bello, 1994, p. 42). This SAP was placed into a society which at the time was characterized as implementing heavy interventionist policies (Bello, p. 42). The program took on the characteristics of a typical structural adjustment and stabilization program, including: financial liberalization, monetary devaluation, export oriented industrialization, privatization, and deregulation (Solimono, 1994, p. 130).

Prior to the stabilization and structural adjustment procedures, Chile succeeded in modernizing its institutions, fostering social mobility, and brought about economic progress (Ffrench-Davis and Munoz, 1994, p. 281). It was also known for having one of the most equal income distributions in Latin America.

Previous presidents of Chile embraced the idea of a mixed economy. This means an active state which promotes private investment and ensures the social well-being of the lower and middle classes (Ffrench-Davis and Munoz, 1994, p. 281). However, when General Pinochet overthrew the democratically elected government of Chile in 1973, he embraced the free-market and monetarist ideologies (Ffrench-Davis and Munoz, p. 280). He soon began a transformation of the Chilean economy with the help of the World Bank and the IMF. His idea was to make the economy more laissez-faire (with the exception of a 1982-5 bailout when the state came to the aid of a bankrupt financial sector) and more open to the international community (Ffrench-Davis and Munoz, p. 281).

By the end of the 1980s the Chilean economy had indeed gone through a transformation. Some six-hundred state enterprises had been sold off with fewer than 50 remaining in domestic hands (Bello, 1994, p. 42). By the end of the "adjustment" procedure, Chile was transformed into one on the most "free market" countries in the Third World (Bello, p. 42). Foreign investors saw an opportunity to take large portions of the former state enterprises. They took control over key industries such as telecommunications, airlines, and steel production (Solimono, 1994, p. 130).

Unfortunately, this privatization mainly favored the upper class. Pinochet sold off these enterprises at "slashed" prices to his "Chicago boy" clients (Taylor, 1994, p. 49).

Also, the economy indeed became more integrated into the international economy. In 1970, 35% of the nation's GDP was comprised of export earnings (Bello, 1994, p. 42). By 1990, the figure had risen to 57% (Bello, p. 42).

This new export-led industrialization (ELI) strategy by definition encouraged the export of their goods in which they had a comparative advantage: Natural resources. This was in contrast to Chile's previous development strategy ISI, which favored manufacturing sectors such as metal working and other related enterprises. As seen in Table 3.1 the manufacturing sector decreased from 26% in the 1960s, to 20% in the 1980s (Ffrench-Davis and Munoz, 1994, p. 287).

Did this transformation help the economy? Many have reported the Chilean experiment in structural adjustment a great success. The Chilean economy saw a rapid rise in exports, a positive trade balance, increased foreign investment, and a relatively low inflation rate (International NGO, 1994, p. 51). With the growing export sector of the economy (as shown in Table 3.1), Chile has been cited as "South America's tiger," a comparison with Korea and Taiwan (International NGO, p. 51). These have been guideposts in determining the success of a structural adjustment program. But a closer look at the numbers leads me to a different conclusion.

Table 3.1

Growth Rates and GDP shares of Manufacturing, Exports and Agriculture in Chile

Annual Growth Rates			
Period	*Manufacturing*	*Agriculture*	*Exports of Goods and Services*
1950-61	4.8	1.8	2.6
1961-71	6.0	2.9	3.2
1971-74	-1.6	-1.8	8.4
1974-81	-1.0	1.8	9.4
1981-89	2.6	3.1	7.3
GDP Shares			
Period	*Manufacturing*	*Agriculture*	*Exports of Goods and Services*
1950-61	22.2	11.8	12.3
1961-71	25.4	9.6	12.0
1971-74	27.2	8.3	9.9
1974-81	22.0	8.6	20.2
1981-89	19.3	8.8	28.1

Note. Percentages based on 1977 prices. From R. Ffrench-Davis and O. Munoz, 1994, p. 287.

The Organization for European Cooperation and Development (OECD) asserted that the costs of the Chilean SAP were among the largest in Latin America (Solimono, 1994, p. 131).

Others agree with the OECD. Walden Bello suggests if we were to gauge the success of the program by the economic growth rates it would be deemed a failure. The growth rate during the 1974-89 period (after the installment of the adjustment program) averaged only 2.6% per year, which was much worse than the growth rates experienced under the ISI period (Bello, 1994, p. 43). Those growth rates were: 4% per year in 1950-61 period and 4.6% per year in the 1961-71 period (Bello, p. 43).

The detrimental effect on the growth rate was not the only negative effect on the Chilean economy. "The combination of a lower rate of investment and the draconian trade liberalization resulted in de-industrialization: The manufacturing sector lost ground, declining from an average of 26% in GDP in the late 1960s to an average of 20% in the late 1980s" (Bello, 1994, p. 44). Since then he manufacturing sector has failed to reach its previous levels. It was not until 1988 that the industrial value-added surpassed the absolute level attained in 1974 (Solimono, 1994, p. 130).

Even though the Chilean economy showed a more consistent growth pattern through the mid to late 1980s, few benefited. The philosophy behind the program was that the "free market" would inspire entrepreneurship, and this would foster growth which would trickle-down to the people of the lower economic strata (International NGO, 1994, p. 51). Despite their beliefs, these economic "improvements" have primarily been enjoyed by the economic elite (International NGO, p. 51). The gap between the rich and the poor sectors was amplified. This was done in part through a cutback in government spending (24% of government expenditures were cut), a tough freeze on wages, and a massive devaluation of the Chilean peso (Bello, 1994, p. 44).

This gap between the rich and the poor is seen through the increase in the proportion of families living below the line of destitution (Bello, 1994, p. 44). This figure rose from 12% to 15% (Bello, p. 44). Also the number of people living above the line of destitution but below the poverty line increased from 24% to 26% (Bello, p. 44). By the beginning of the 1990s, 41% (26% plus 15%) of the population were living below the poverty line.

Also during this time period, income distribution became even more skewed. The income share of the poorest 50% declined from 20.4% to 16.8%, and while the share going to the richest 10% went up from 36.5% to 46.8% (Bello, 1994, p. 45).

These adjustments have caused Chile to fall deeper into the "debt trap." Chile's external debt of US$ 19 billion was higher than it had been at the start of the debt crisis in 1982 (Bello, 1994, p. 42). Total debt stood at 49% of GNP in 1991 and at the time 9% of GNP was flowing out of the country to service the debt (Bello, p. 42).

In addition to the working class, the environment was also taking a hit. The effects on the environment have been dramatic. "The economic growth of Chile has taken place at the expense of the environment... The so called export boom was based on the use and abuse of natural resources, permitting the degradation of the eco-system greater than their ability to regenerate" (Spalding, 1992, p. 49).

Mexico

Mexico is another country that has been touted as the, "vanguard of structural reform in Latin America" (Bello, 1994, p. 37). But, as is the case with other Latin American countries another conclusion might be drawn from the data.

The Mexican government agreed to an SAP in 1983 after the full effects were known about Mexico's debt difficulties. A seven year plan was developed and was supposed to provide sustained growth through the reduction of state interventions, otherwise known as "market distortions," as well as to stabilize the economy. The Mexican difficulties was blamed (by the IMF and WB) on a "bad" development strategy that the Mexican government had pursued in the past (Ros and Lustig, 1994, p. 273). As Table 3.2 shows, this opinion is difficult to prove when looking at real GDP growth rates.

It was believed that price and financial stability would be gained through drastic and permanent cuts in government spending, as well as a currency devaluation against hard currencies (Ros and Lustig, 1994, p. 273).

Has the SAP been sufficient in delivering debt relief to the Mexican economy? Even as late as the 1989 debt reduction agreement and the agreement reached in early 1995, there was only a rescheduling of debt program rather than actual debt reduction.

In 1989, the IMF and the U.S. wanted Mexico to reduce their debt to the U.S. by US$7 billion (Bello, 1994, p. 37). But, during the loan process, Mexico had to borrow another US$7 billion to collateralize the debt fully (Bello, p. 37). What Mexico ended up with was a 30 year rescheduling of their old debt and their new debt.

Two years later the Mexican debt was US$98 billion which was US$3 billion more than the figure in 1989 (Bello, 1994, p. 37). However, as a percentage of GDP, a mild reduction occurred; a decrease from 53% in 1989 to 48% in 1991 (Bello, p. 38).

In addition, Mexico was also one of the first countries to undergo the privatization program under the WB guidelines. These efforts, by some accounts, have failed. Instead of improving efficiency, re-distributing wealth and breaking up monopolies, many distortions were transferred to the elite, instead of actually eliminating the distortions. Carlos Heredia, an ex-deputy director of Mexico's Ministry of Finance, stated that "Mexican privatization basically transformed public monopolies into private ones" (Avery, 1994, p. 97).

Heredia further asserts that, "privatization has worsened the already steep concentration of wealth in the country. Along with structural adjustment policies in general, privatization has benefited the friends of President

Carlos Salinas." (Avery, 1994, p. 97) The privatization efforts were supposed to improve the fiscal standing of the government, demonstrate the government's commitment to the private sector, improve efficiency of entrepreneurs, eliminate monopolies, and add to the quality of the private sector (Avery, p. 97). According to Heredia, the government has achieved the first two objectives but has forgotten the rest (Avery, p. 97).

For example, the Mexican telephone company (Telmex), was a government organization which was sold to a private entrepreneur Carlos Slim (Avery, 1994, p. 98). Slim was a close personal ally of President Salinas. Herendia says the transfer, "illustrates how the Mexican privatization has benefited a few private capitalists at the expense of consumers" (Avery, p. 98). Also reportedly the industry has not improved efficiency either. The telephone rates have skyrocketed and also much needed improvements in the system have not been made (Avery, p. 98).

But have these reforms at least helped the country? Probably not. As Table 3.2 indicates, the country has failed to achieve the growth rates they had achieved under an ISI development strategy. The period following the SAPs has been characterized as an era of stagnation and declining standards of living. Also, fixed investment declined from 21% of GDP in the 1970-1981 period to 18% in the 1982-1985 period (Lustig, 1992, p. 234).

Table 3.2

Growth Rates of Real Gross Domestic Product in Mexico, Selected Years, 1965 to 1993

Year(s)	Growth Rate
1965-1980	6.5 %
1980-1986	0.4
1987	1.9
1988	1.2
1989	3.3
1990	4.4
1991	3.6
1992	2.7
1993	0.4

Note. From R.A. Blecker, 1995, p. 8. Figures were from World Development Report 1965-1986; for 1987-1993 calculated from IMF's International Financial Statistics.

The failure of the SAP to stabilize the Mexican economy is known since the financial crisis that ensued from the 1995 collapse of the peso has already caused a sharp reduction in real wages as well as environmental difficulties (e.g.: deforestation, water pollution, and air pollution).

Chapter 4: Conclusions

After the implementation of the structural adjustment programs in the early 1980s, few countries have prospered. As in the cases of the Latin American countries discussed above, income distributions have worsened, inflation has not been curtailed, real wages have fallen, and balance of payment difficulties have in many cases not improved.

The facts do not support the opinion of the World Bank and the International Monetary Fund, that all of the difficulties the underdeveloped world experienced were due to endogenous factors such as "bad" development strategies and improper governmental operations.

In addition, the policies that the IMF and the WB lays out are flawed in their reasoning. As discussed in Chapter 1, these policies are not equipped fundamentally to deal with the problems they set out to solve. It seems that the main concern of the IMF/WB is to ensure that these countries are "corrected" is such a way that they are at least able to pay their loan payment, and are vulnerable in such a way that their resources can be extracted to benefit the North as well as their multi-national corporations. This is in contrast to what should be their true goal, of actually alleviating the difficulties that these countries face.

The IMF and the World Bank need to seriously reevaluate the soundness of their policies. They also need to get other non-governmental organizations (NGOs) who deal directly with these underdeveloped nations and who know full well what their difficulties, the NGOs also need to be fully involved in the development of a more reasonable set of guidelines.

Appendix

Table A.1: Socio-economic indicators for major Latin American countries

		Population	*Percent Urban*		*Total External Public Debt $ per capita*	*Lng.-Trm. Public Debt to export earnings (%)*		*Consumer Price Index*
		1990 (x1000)	*1965*	*1990*	*1988*	*1970*	*1987*	*1990 ('85=100)*
1	Argentina	32,322	76	86	1,529	88	552	63,930
2	Boliva	7,313	40	51	64	232	743	675
3	Brazil	150,368	50	77	622	110	320	87,722
4	Chile	13,174	72	86	1,075	162	240	242
5	Colombia	31,819	54	70	437	127	179	305
6	Costa Rica	3,015	38	54	1,308	48	241	219
7	Dominican Republic	7,170	35	60	466	75	165	426
8	Ecuador	10,781	37	57	926	75	379	658
9	El Salvador	5,252	39	44	326	34	172	288
10	Guatemala	9,196	34	42	245	330	200	190
11	Haiti	6,504	18	30	108	174	156	116
12	Honduras	5,139	26	44	570	45	270	151
13	Jamacia	2,521	38	52	1,467	28	208	185
14	Mexico	88,598	55	73	970	109	278	1,405
15	Nicaragua	33,871	43	60	1,873	67	1,758	**
16	Panama	2,418	44	55	1,576	49	63	102
17	Paraguay	4,277	36	47	523	125	2,133	249
18	Peru	22,332	52	70	603	69	348	88,733
19	Trinidad/Tobago	1,283	30	69	1,431	29	91	159
20	Uruguay	3,218	81	83	953	92	184	1,794
21	Venezuela	19,735	70	90	1,352	26	197	480

Note: Taken from J. Walton & D. Seddon (1994)

Table A.2: Socio-economic indicators for major Latin American Countries (Continued)

		Earnings Per Employee Average Growth (1980=100)		*Earnings Per Employee (1980=100)*	*Percent central-government spending*			
					Education		*Health*	
		1970-80	*1980-88*	*1988*	*1972*	*1989*	*1972*	*1989*
1	Argentina	-1.5	1.4	97	20.0	9.3	**	2.0
2	Boliva	0.0	-10.3	46	31.3	20.3	6.3	6.6
3	Brazil	4.0	0.0	109	8.3	4.2	6.7	6.1
4	Chile	8.1	-1.7	105	14.3	10.1	8.2	5.9
5	Colombia	-0.2	3.2	115	**	**	**	**
6	Costa Rica	**	**	**	28.3	17.0	4.0	27.2
7	Dominican Republic	-1.0	-4.4	79	14.2	**	11.7	**
8	Ecuador	3.3	-1.3	95	27.5	23.4	1.5	9.8
9	El Salvador	2.4	-9.3	63	21.4	17.6	10.9	7.4
10	Guatemala	-3.2	-2.7	89	**	**	**	**
11	Haiti	-3.3	4.6	157	**	**	**	**
12	Honduras	**	**	**	22.3	**	10.2	**
13	Jamacia	-0.2	**	**	**	**	**	**
14	Mexico	1.2	-5.2	72	16.4	12.3	4.5	1.7
15	Nicaragua	**	-10.0	31	16.6	**	4.0	**
16	Panama	0.2	3.2	123	20.7	19.1	15.1	19.8
17	Paraguay	**	**	**	12.1	11.4	3.5	3.0
18	Peru	**	-3.0	95	23.6	15.6	5.5	5.5
19	Trinidad/Tobago	**	**	**	**	**	**	**
20	Uruguay	**	1.0	118	9.5	79	16	4.5
21	Venezuela	3.8	0.1	98	18.6	19.6	11.7	10.0

Note: Taken from J. Walton & D. Seddon (1994)

Table A.3: Latin America Under IMF -- Behavior of Certain Key Economic Variables

	Average 1969-80	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990
Growth rate of real GDP (RGDP)	5.8	-0.2	-1.1	-2.8	3.7	3.3	4.7	2.4	0.2	1.4	-0.9
Growth rate of per capita RGDP	3.3	-2.2	-3.4	-5.0	1.4	1.1	1.6	1.2	-1.9	-0.6	-2.8
Inflation rate (weighted avg.)	34.3	60.7	67.1	108.7	133.5	145.1	87.4	131.3	286.2	533.4	769.8
	Average 1978-80	**1981**	**1982**	**1983**	**1984**	**1985**	**1986**	**1987**	**1988**	**1989**	**1990**
Fiscal surplus as % of GDP weighted avg.	-1.1	-5.6	-5.8	-5.7	-4.2	-3.8	-5.0	-6.6	-5.3	-4.9	0.1
Fiscal surplus as % of GDP (median)	-2.6	-5.3	-5.4	-4.9	-4.7	-3.2	-3.4	-2.5	-3.3	-2.9	-1.8
Gross capital formation as % of GDP	23.5	23.3	21.2	17.4	17.1	18.4	18.1	19.8	20.3	20.0	18.4

Notes: Taken from M. Pastor, 1993, p. 248.

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