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THE INTERNATIONAL MONETARY FUND: IMPLICATIONS FOR ISRAEL

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Saudi Arabia is using economic power to expand its role in the international system even as the source of that power is being undermined. The growing Saudi role in the International Monetary Fund is a case in point. Israel must develop strategies to prevent this influential institution from being transformed into another anti-Israel forum.

In early January, Jacques de Larosiere, the Managing Director of the International Monetary Fund, headed a mission to Saudi Arabia to ask that country to lend the Fund about $5 billion, in addition to the $10 billion which the Saudis' have provided over the past two years. This growing dependence of what has been called "the world's most effective international institution" on the generosity of Riyadh has had important consequences for the workings of the IMF. It is ironic that the standing of OPEC's leading member should finally be institutionalized just before the price of oil began its current collapse. In any case, and whatever the power of Riyadh in the long run, it is certain to be a thorn in Israel's side for some time to come. As Foreign Ministry and Bank of Israel sources have confirmed, Israel has had to gird itself for the political repercussions of the Saudis' new power.

In 1978, Saudi Arabia's currency, the *rial*, was one of what the Fund terms its most "usable currencies." That is, the sum available for lending was greater than that of most other currencies deposited with the Fund. By virtue of this, the Saudis were given the right to appoint an Executive Director who would represent them in the Fund's Executive Board. In 1979, Arabic was recognized as an official language of the Fund. In 1981, Saudi Arabia's quota --which is the size of the subscription each member is required to deposit with the Fund -- was increased from about $1.1 billion to $2.1 billion. Because this represented a relative increase in the Saudis' "assessed net worth," as it were, and not merely an increase in

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their "costs" of membership in the Fund, this increase helped pave the way to an increase in Saudi voting power, which doubled to the very respectable level of 3.5% of the total. Finally, last September, at the annual meeting of the IMF (which occurs jointly with its sister organization, the World Bank), held in Toronto, the Kuwaiti Minister of Finance, Abdel-Latif al-Hama, became the first Arab chairman of what is undoubtedly the world's most important banker's convention.

The Trappings of Power

But the Saudis' most impressive achievement was made the previous year, when they were admitted as permanent members of the Board of Executive Directors. When Yusuf Nimnatullah assumed the dignities of his office he joined the representatives of thw world's five leading economies: the U.S., Great Britain, West Germany, France and Japan. These states alone are privileged in not having to share their Directors with others. Together with the 16 additional Directors, they represent the interests of the Fund's nearly 140 members, each of whom enjoys a proportion of the total voting power, which amounts to some 640,000 votes.

One can grasp the significance of this honor by noting that Canada, which with 20,650 votes has 97% of the Saudis' weight, shares its Executive Director with eight other countries. The entire contingent from French-speaking Africa, which has 23 members in the Fund, disposes of only two-thirds as many votes as the Saudis, and has but a single Director in the Fund.

Israel belongs to a group including the Netherlands -- which has the greatest voting power -- Cyprus, Romania, and Yugoslavia. Israel has maintained the most cordial relations with the group and has cooperated very closely with the two Communist countries.

The enhanced role of the Saudis in the world economy is not the only reason for their rising prominence in the councils of the IMF. The Saudis were able to squeeze the Fund into increasing their voting power, after which they cashed in a number of political debts to vote themselves a permanent seat on the Board. Saudi cash, which had for some time been a potent tool in the political wheeling and dealing at the IMF, has become even more powerful now that the Fund finds itself with most of its own usable currency committed to a variety of schemes designed to prop up countries which are having difficulties in repaying their external debts.

Changing U.S. Policy toward the IMF

The immediate future is hardly bright either. The international edition of Business Week reported on December 20 that the "sudden drain on the IMF kitty from the expected (now accomplished - ed.) $11 billion in loans to Mexico, Argentina, and Brazil is cutting dangerously close to the Fund's current resources." These loans come in the wake of several years' heavy extension of balance-of-payments assistance to countries such as India, which obtained a $4 billion drawing -- at the time the largest in the Funds's history (the current record is held by Brazil, which recently received nearly $6 billion). Were such Third World countries to default on their debts, the entire fabric of the international financial system might well be torn apart, a fact which seems to have taken the industrial states rather by surprise. The Reagan Administration, for example, which came into office with a strong antipathy to the IMF, the World Bank, and the entire panoply of international economic institutions, has abruptly changed its tune in the wake of the near-default of Mexico, the unfortunate bearer of the world's greatest external debt. Less than seven months ago, the U.S. was still opposed to any recourse on the part of the Fund to borrowed resources, which are more and more coming to supplement the regular quota subscriptions of members. The U.S. similarly opposed any increase in the Fund's activities in aiding beleaguered Third World countries. According to Business Week, it was the threat to American banks which a disaster such as a Mexican default posed which made the Administration reverse itself on the issue of IMF activitism and borrowing. In the end, with U.S. support, the IMF was able to negotiate a $3.9 billion package deal for Mexico.

In fact, far from criticizing the Fund for handing out "easy money," the Administration has recently been scolding it for attaching too many strings to its payments assistance. Clyde Farnsworth of the New York Times recently cited U.S. Secretary of State George Shultz as having blamed the IMF's imposition of "austerity programs" on those who would accept its aid as having had the effect of discouraging consumption and slowing world recovery from the recession. He quotes U.S. Treasury Secretary Donald Regan as saying "debtor countries are being told one thing by the IMF: to import less and export more. How can the whole world do this simultaneously and still maintain a trading system?" The question has posed itself to many influential policymakers and ex-policymakers, who have in the past not been noted for their interest in economic affairs. In early January, for example, Henry Kissinger wrote in Newsweek that over 40% of America's exports go to Third World countries, particularly the newly-industrializing ones such as Brazil and Mexico, which are precisely the holders of the greatest debts. The U.S. has every reason to deplore austerity programs at this time.

THe Fund, for its part, has denied that it has been serving as an impediment to growth. In the above-cited Times article, Farnsworth quotes a high IMF official as saying, "We are not imposing austerity. We are providing additional resources to limit the decline in economic activity that is threatened by financial collapse." In any case, the Fund is stretching its resources to the very limit in trying to accomplish what it sees as its goals.

The IMF exerts far more influence than its resources would seem to justify by serving as a lender of last resort. Its stringent requirements can provide an ailing economy which agrees to cooperate with what amounts to a clean bill of health. This encourages other investors to add their money to the deal. This explains why even a rather modest drawing granted by the Fund can help a country with severe payments difficulties -- for after getting the Fund's money it can obtain more in the international money markets than would otherwise have been the case. Furthermore, the fund can supplement its own rather meager financial endowments with its considerable political resources, and pressure cautious commercial bankers to cooperate in what is eupehmistically referred to as the "re-scheduling" or "rolling over" of debts.

Down to its Last Lendable Dollar

But the IMF has always had trouble in persuading its members to increase their quota subscriptions rapidly enough to meet its challenges as it sees them. Quotas are supposed to be the Fund's major source of finance, as was reiterated in an Executive Board decision last year: "Quota subscriptions are and should remain the basic source of the Fund's financing. However," it goes on to say, "borrowing by the fund provides an important temporary supplement to its resources. In present circumstances, it facilitates the provision of balance of payments assistance to its members..." It has become clear that without further borrowing from the industrialized countries and Saudi Arabia -- especially the latter, which has money to burn -- the Fund will be down to its last lendable dollar when present and planned assistance packages are implemented. At that point, the fund will have only $26 billion in usable currencies, a sum which just barely covers mandatory reserve requirements. The IMF must be able to supply a certain portion of each member's quota in usable currencies within two days of receiving a request; as it must maintain the $26 billion against the possibility that all countries might demand their reserves, the IMF is left with practically no flexibility to reply to unforeseen contingencies.

The Saudis' 1981-82 success in doubling their voting power came as a result of this chronic lack of discretionary funds. Apparently, Mr. de Larosiere had previously secured some vague assurance from the Saudis that they would agree to loan the Fund another $10 billion for that period. When the Managing Director came to collect the money, the Saudis themselves decided to cash in on the Fund's own vague promises about an "adjustment" of the Saudis' voting power.

Why do the Saudis want to lend such vast sums to the IMF, and at slightly below market rates? An official in the Foreign Ministry explained this as the result of the Saudis' desire to find a suitable field for risk-free investment, in addition to their desire to exercise political influence. Were the Saudis to lend the money directly to the final users, their chances of getting it back in one piece would not be so good as in the case of the absolutely blue-chip IMF. In addition, there is apparently some desire on the part of Saudi Arabia to reduce its dependence upon assets denominated in dollars, for the IMF loans are denominated in Special Drawing Rights -- a unit of account unique to the Fund and a few of its associated institutions, which is itself based on a basket of five major currencies.

The Fund might well have been able to find the same financing in the international money markets, but is very leery of doing so for fear of possible legal entanglements. The World Bank has been going to the money markets for years; but the Fund is different in that it is not legally constituted as a "lending institution." Its sole function is to provide "balance of payments assistance." Still, the IMF has had a proposal to borrow in the financial markets before the consideration of the Executive Board since the late 1970s, and some market borrowing has already been done.

The great international banks favor access to capital markets, and for good reason: not only do they welcome a new and reliable international customer -- they also need all the help they can get to bail out big Third World debtors to whom they have loaned vast sums. In late December, the President of Manufacturers' Hanover Trust, a major international lender, said in an interview on British television that the IMF could play a key role in nursing debtors such as Brazil back to health, and that free access to the capital markets was strongly to be urged.

The Question of a PLO Observer

For Israeli policymakers the most annoying aspect of the Saudis' new power in the IMF has been the recurrent question of inviting the PLO as an observer to the IMF/World Bank annual meetings. The issue was first raised in 1979 and has hovered over every IMF function since.

The PLO would indeed be strange company among the other rock-ribbed observers currently accredited to the Fund, including the Organization for Economic Cooperation and Development (OECD), the General Agreement on Tariffs and Trade (GATT), the UN and the Swiss National Bank (for Switzerland's policy of strict neutrality has prevented it from joining the Fund). Few, apart from the Arabs and their Communist and Third World allies, would deny that the PLO, despite its rather considerable assets (much of them in Switzerland, no doubt), is anything but an international economic welfare society. This, at any rate, was the Israeli charge.

The problem arises in the loose definition of what a "suitable observer" is -- for the Chairman of any annual meeting is entitled to invite any observer he chooses. In 1979, the proposal to admit the PLO as an observer was thwarted by a bureaucratic subterfuge: the list of accredited observers was arbitrarily limited to those invited in previous years. Similar strategems were employed to equal effect in subsequent years.

Sources in the Bank of Israel confirm that this was largely due to the activities of the U.S. and a few industrialized countries, which are anxious both to defend Israel and to preserve the IMF as one of the last of the international organizations established after the Second World War which may still be said to function. Most of the pressure that the U.S. brought to bear was behind the scenes, but a taste was provided in Washington, when then-President Carter, in his opening remarks, urged delegates not to allow themselves to be diverted from their proper business by "extraneous political disputes."

The Arabs in general and the Saudis in particular have been curiously silent in the wake of their repeated failures in getting the issue of the PLO taken seriously, let alone approved. Rumor has it that one reason for this Arab acquiescence could be found in the sharp inter-institutional horse-trading that goes on in the annual meetings of the IMF/World Bank. Apparently, the British were long overdue to be shorn of some of their shares in the Bank, so as to more accurately to reflect their diminished importance in the world economy. In order to sell these "lost" shares as dearly as possible, the West agreed to relinquish them to the Saudis as part of a U.S.-mediated deal.

Skirmish Over Costa Rica

Politics are a fact of life at the IMF, but they cannot be mentioned openly. Being an institution with no jurisdiction other than the world economy, the Fund is in theory a kind of American free-trader's utopia. This means political vengeance must be taken behind a cloak of economic impartiality. Sources in the Israel Foreign Ministry note that one small skirmish in the running Arab-Israeli battle which now mars all international discourse occured when Costa Rica asked for assistance in its balance of payments crisis. That country had just moved its embassy from Tel-Aviv to Jerusalem and was therefore attacked by the Fund's Director as not really needing the aid. IN the end, the Saudi claim was brushed aside by an overwhelming majority led by the U.S.

But Arab political clout is not, in every case, wielded to Israel's disadvantage. According to a senior Foreign Ministry official, the Bank of Israel had been trying for fifteen years to persuade the IMF to schedule its annual meetings so as not to overlap with the Jewish high holy days, receiving polite refusals with depressing regularity. Then, last year, the Arabs suddenly asked that the meetings be scheduled around the *Ramadan* holy month -- a request which won a respectful, if not obsequious, audience. When it was approved, Israel used the precedent to insure that its own religious sensibilities would be equally respected.

The Saudis may well aspire to a day when their power will enable them to dictate IMF policy according to their desires; but the limits to their prospects seem to be fairly circumscribed. Here, as is not the case in the U.N., decisions are not merely words on paper but potent tools of economic power. Fortunately, the U.S. and Europe are united in their resolve to prevent the Fund from being made into yet another arena for the kind of political posturing which has made so many other international organizations into parodies of their founders' visions.

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