IMF reform has been on the policy agenda for as long as most of us can remember. Since the breakdown in the early 1970s of the Bretton Woods System that the IMF had been created to oversee, observers have questioned whether the Fund still has a mission and tools appropriate to the task. For the older among us, recalling these earlier discussions, it seems like the IMF is always in search of a new job description.

In the last year, however, reform discussions acquired a new sense of urgency. Developing countries, flush with dollars, no longer needed the IMF. Currently the Fund has only six arrangements under which it lends money, down from 21 such programs in 1998. Since the institution derives income from its lending, this creates the delicious prospect that it may have to undergo the kind of painful structural adjustment that it typically prescribes to its clients. In addition, the IMF has been impotent in the face of the global imbalances that pose the main threat to international financial and economic stability. On both counts it has seemed increasingly irrelevant. The danger, as Mervyn King of the Bank of England put it, is that the Fund will slide into obscurity.

By all accounts, serious discussion of these problems took place at the IMF’s annual meetings in Washington, D.C. last month. For the first time in memory, delegates departed from their prepared statements in favor of real debate on the issues. The Fund’s steering committee, made up of leading finance ministers and central bank governors, agreed that IMF surveillance should focus more on global economic issues. Surveillance should be multilateral, rather than country by country, and it should focus on international spillovers. The intent, evidently, is to give the Fund a mandate to address the problem of global imbalances.

But does this expanded role come with the power to actually do anything? The IMF is not going to be able to force the United States to raise taxes or China to change its exchange rate. If a country doesn’t borrow from the Fund, the latter is notoriously unable to do more than politely suggest some modest policy changes. Especially if the country is a large shareholder in the Fund, like the United States is and China soon will be, its government will simply tell the institution to mind its own business.

A feuding husband and wife will often say the same to those who offer them gratuitous advice. But sometimes the dysfunctional couple, if it recognizes that the marriage is at risk, will seek professional help. A marriage counselor similarly has no power to compel the husband and wife to change their behavior. But sometimes a neutral venue and intervention by a neutral referee, who has seen similar problems before, may encourage constructive changes in behavior.

Can the IMF succeed as marriage counselor? Can it get the U.S. to agree to raise taxes and China to increase spending on education, health care, and infrastructure in order to keep global demand stable while redistributing spending away from the United States before the current pattern of imbalances unwinds abruptly? Not all marriages can be saved, especially when the partners see things differently. But divorce is costly, not least for the smaller members of the household. And there is no better venue for counseling than the IMF. China and other emerging markets are not part of the G7. And larger groupings like the G20 lack experience and legitimacy.
Is there still a role for the Fund in providing its services to emerging economies? With so many emerging markets running current account surpluses and accumulating international reserves, the fashionable answer is no. Emerging markets, in this view, are now in a stronger financial position, and they no longer need subject themselves to the painful and embarrassing conditions involved in securing financial assistance from the IMF.

What this view neglects is that emerging markets are enjoying, for the moment, extraordinarily favorable conditions. Global growth is stronger than in 35 years. Interest rates are still low for this stage of the business cycle. International investors flush with liquidity are pouring money into emerging markets because there is nowhere else left. And despite all this there are countries on the verge, from Iceland to Hungary. As interest rates rise further, their problems will deepen, and the list of problem countries will lengthen.

Moreover, holding reserves against the possibility of financial instability is expensive. Poor countries have better uses for their scarce resources. The sensible solution is for them to pool their reserves at an international institution, which could lend them to countries in need. The resulting institution could act like a credit union. Why, we could call it the IMF!

Alas, on this front there was no progress at the spring meetings. The Fund’s own proposal for a new facility that would automatically disburse funds to countries that had been prequalified for assistance went nowhere. As it should have: prequalification is problematic, and disqualifying a previously prequalified country is especially problematic since nothing is more certain to precipitate a crisis. A better approach would be to streamline existing procedures for extending assistance and increasing existing credit lines, the IMF’s so-called quotas, by pooling countries’ reserves at the Fund. Since countries with larger quotas get more votes in the IMF, the emerging markets the currently have ample reserves but may need assistance in the future should be happy to contribute.

Giving the IMF a role as marriage counselor is a first step in rescuing it from irrelevance. But it also has a role as manager of a credit union for emerging markets. Only when the institution’s management and shareholders acknowledge this will the institution truly be saved from obscurity.

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