The IMF and capital controls: towards postneoliberalism?

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ABSTRACT This article examines whether the International Monetary Fund (IMF) is moving towards a postneoliberal policy stance on capital controls. After a historical outline of the IMF’s formal and informal position on capital controls, the article will focus on the IMF’s view after the global financial crisis. In particular, a policy framework proposed by the staff in March 2011, will be rigorously scrutinized. While the crisis may have played a role, it will be suggested that the framework is the outcome of a process that has been going since at least the Asian crisis in 1997. Moreover, whereas the changes of the IMF’s position are often stressed, the continuities have been underemphasized. It will be argued that these continuities demonstrate that the IMF in general, and its policy stance on capital controls in particular, still contain a neoliberal bias. As such, the IMF policy framework can be characterized as an example of the ‘new constitutionalism’, an attempt to prevent that states would deviate from neoliberal prescriptions.

Keywords: IMF, capital controls, neoliberalism, new constitutionalism

In April 2011 the International Monetary Fund (IMF) proposed its first ever guidelines for using capital controls (Harding, 2011). The legitimation of certain controls was seen as a major turnaround by many commentators (e.g. Rastello, 2011, Talley & Reddy, 2011). This new policy stance has contributed to observations that the IMF is turning its back on the neoliberal ideas that it had promoted and pushed through in the past decades (e.g. Faujas, 2010; Rodrik, 2010; Stiglitz, 2011). However, while some analysts have offered a more nuanced view on the IMF guidelines (e.g. Gallagher, 2011), the details of this proposed policy framework and the IMF’s position in general have up to now been scarcely analyzed in a comprehensive way, and have not been properly theorized. This article will try to fill this void.

The first section will give an historical oversight of the IMF’s point of view on capital mobility and capital controls. In the second section, the new framework will be rigorously scrutinized. We will examine why capital controls could be legitimate, what kind of capital controls are endorsed, in what circumstances and for what reasons. The third section will present a profound critical analysis of the IMF’s view and offer some theoretical considerations. Three arguments will be made. First, the global financial crisis has not marked a sea change in the Fund’s thinking on capital controls. The continuities in the IMF’s position have been underemphasized. Second, the IMF still contains a neoliberal bias in general, and on capital controls in particular. Third, the framework can be considered as an example of the ‘new constitutionalism’, that could prevent emerging markets (EMs) from deviating from neoliberal policy

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prescriptions. The final section will summarize the arguments of this article and draw some implications for a postneoliberal policy framework on capital controls.

1. HISTORY OF THE IMF’S FRAMEWORK ON CAPITAL CONTROLS

In this section we will give an historical overview of the evolution of the IMF’s framework on capital controls. Two points must be noted. First, we will consider both the formal framework, codified in the Articles of Agreement and other official documents, and the informal framework, such as the IMF’s staff actual approach of capital account liberalization. Both are essential for an accurate understanding of the changing policy framework. Second, this section is mainly a descriptive account. Theoretical considerations will be dealt with in the third section of this article.

The original Articles of Agreement

During the Second World War, when the negotiations on the post-war economic order were settled, a combination of forces was in favor of installing capital controls that would remain in place for at least quite some time after the war. Harry Dexter White for the US and John Maynard Keynes for the UK led the Bretton-Woods negotiations on a post-war economic order. They agreed on two things: first, substantial control over international capital movements would be necessary, and second, controls would be most effective if countries cooperated with each other in enforcing regulations (Helleiner, 1995; Crotty & Epstein, 1996). Keynes proposed voluntary cooperation, while White projected mandatory cooperation (De Cecco, 1979). Whereas White thought of capital controls as a temporary solution to the post-war economic problems, Keynes believed that they had to be a permanent feature (Chwieroth, 2008, Panitch & Gindin, 2008). In any case, the ‘common sense’ assumed that international capital movements had to be actively managed (Ikenberry, 1992; Chwieroth, 2007b). As economist Arthur Bloomfield (1946; italicized in original) wrote: “a substantial measure of direct control over private capital movements, especially of the so-called “hot money” varieties, will be desirable for most countries not only in the years immediately ahead but also in the long run as well.”

There was strong opposition to the proposals, mainly from New York bankers who had strong influence in Washington (De Cecco, 1979; Panitch & Gindin, 2008). Eventually, financial communities succeeded in removing all references to potential mandatory cooperation (Eatwell, 1996; Helleiner, 2001). This reflected the continuing power of financial capital in the US (Panitch & Gindin, 2008). The final version of the IMF proposals “contained watered-down formulae relating to capital controls”, and there were few references to private international capital transactions (De Cecco, 1979). Most significant was that the burden of enforcing capital controls fell on countries with outgoing flows instead of controls ‘at both ends’. However, the Articles of Agreement of the IMF (1945) still sanctioned the use of extensive capital controls (Kirshner, 1999; Chwieroth, 2008). Article VI, section 3 stated: “Members may exercise such controls as are necessary to regulate international capital movements (...)” (IMF, 1945). Moreover, Article VI, section 1 prescribed: “A member may not make net use of the Fund’s resources to meet a
large or sustained outflow of capital, and the Fund may request a member to exercise controls to prevent such use of the resources of the Fund.” To sum up, member states were given the right to use controls, and the IMF could even request governments to use them as a condition for IMF financing (Chwieroth, 2008; Joyce & Noy, 2008).

Some quite remarkable aspects deserve further highlighting. First of all, the focus was clearly on the control of capital outflows (Helleiner, 2001). Arthur Bloomfield (1946) wrote that some management of inflows could exist to reduce excessive accumulation of foreign debt, or restrict foreign ownership in specific domestic industries. Still, controls on capital inflows were not frequently debated. As De Cecco (1979) writes: “Clearly, short-term capital movements were not regarded as an essential part of the adjustment mechanism foreseen by the Agreements; in fact, they were a nuisance, to be restricted rather than fostered. But all the burden of establishing controls was to fall on the countries from which capital flees and none on those to which it goes.” Two explanations are worth mentioning. First, the introductions of capital controls on inflows would “probably not be necessary, largely because these movements are likely to be closely restricted in their countries of origin” (Bloomfield, 1946). Economists were mainly preoccupied with controls on capital outflows by nationals. Capital inflows were just not really considered a problem, in contrast to outflows. Second, for opponents of capital controls putting the burden of enforcement on countries with outgoing flows meant that the effectiveness of the controls could be undermined.

A second noteworthy facet is that the controls were mainly to be quantitative. There was no indication of a preference for market-based controls (such as taxes), neither in the Articles of Agreement nor in debates of the economists at that time. The interwar experience had demonstrated that indirect controls were inadequate. As Bloomfield (1946) stated: “It would appear, then, (...) that the only practicable solution (...) is the imposition of direct controls.”

Third, while most commentators interpret the Bretton Woods agreements as a commitment to capital controls even in the long term, other authors have a different interpretation. They believe that the foundation had already been established for a more laissez-faire regime of international capital movements (Konings & Panitch, 2008; Panitch & Gindin, 2008). For instance, Article I lists as one of the purposes of the IMF “to assist in the establishment of a multilateral system of payments in respect of current transactions between members and in the elimination of foreign exchange restrictions which hamper the growth of world trade” (IMF, 1945). Article VIII, section 2, states that, after a transition period, “no member shall, without the approval of the Fund, impose restrictions on the making of payments and transfers for current international transactions”. This has been interpreted as a commitment to capital account liberalization in the long term (Quinn & Inclán, 1997).

In this respect, the position of the US was of great importance. Despite the New Deal regulations, financial capital was still a powerful force in American society (Helleiner, 1994). Partly because of its economic and financial strength, capital controls were never an issue in the US (Panitch & Gindin, 2008). Moreover, large segments of the US state thought of capital controls in other countries as a temporary feature of the post-war economic order, that would disappear after a short transition period. So, it could
be argued that “US policy all along was to dismantle currency and capital controls once adjustment and 
catch-up had occurred” (Newstadt, 2008).

To sum up, the Bretton Woods arrangements did limit the extent of financial liberalization during the 
first years of the post-war period in order to secure the (European) economic reconstruction, as the 
negotiators had envisaged. But this was conceived as a temporary evil by large segments of the US 
capitalist class and state officials (Konings, 2008). This is why the IMF’s framework on capital controls 
has never been that one-sided, and has been rather ambiguous from the IMF’s very foundation. Panitch 
and Gindin (2008) argue: “So while Bretton Woods recognized that states could operate capital controls, 
what was more significant was the US state’s own refusal to use such controls, and the expectation both 
in Washington and New York that other states would use them only for a transition period of 
reconstruction.”

The norm adoption of capital account liberalization

This ambiguity intensified as the years passed by. The opinions of the IMF staff in the early post-war 
period are subject to different interpretations. While most analysts believe that the staff’s ideological 
commitment to Keynesianism secured the use of controls as a legitimate policy instrument (Chwieroth, 
2008), some authors argue that the staff’s position was definitely not that one-sided (De Cecco, 1949). 
In any case, their attitude towards capital controls gradually changed. During the early post-war years, 
under the influence of the US state and Wall Street bankers, the IMF was reshaped into a protector of 
financial interests (Felder, 2008). Individual country experience and the growing trade and development 
facilitated by the gradual liberalization of controls encouraged the staff to become less favorable 
history, covering the period from 1945 to 1965, noted the resurgence of the view, dominant before the 
1930s, that freedom of capital movements was highly desirable in itself”. Nevertheless, in the first post-
war decennia, the staff largely ignored the issue of capital account liberalization (Chwieroth, 2007b).

As the contradictions during the post-war period grew during the 1960s and 1970s, a combination of 
forces placed heavy pressure on the original IMF framework that legitimated capital controls as a policy 
instrument. The first is the internationalization of productive and financial capital, which united both 
industrial and financial capital in their opposition to restrictive capital controls. Especially the US, where 
the support for capital controls had never been very strong, became very hostile to international capital 
controls (Helleiner, 1994; Crotty & Epstein, 1996; Chwieroth, 2008). A second consequence of the 
internationalization of capital was that governments faced the question of what to do about heightened 
capital mobility (Chwieroth, 2008). As unilateral capital controls appeared to be ineffective, and as 
cooperative action was blocked by US opposition, governments in advanced countries decided that they 
had little choice but trying to reap the benefits of international capital flows (Goodman & Pauly, 1993; 
Andrews, 1994; Helleiner, 1995). The third reason was domestic: in many advanced countries labor was 
getting stronger and more radical. The elimination of capital controls would be a good way to discipline 
organized labor (Crotty & Epstein, 1996). A fourth key source of change was the neoliberal academic
environment (Helleiner, 1995). As Chwieroth (2008) writes: “By the 1970s, most academic economists had come to define capital account liberalization as desirable, and the Fund—which recruits almost exclusively from the economics profession—saw its behavior affected accordingly.” The emergence of the neoclassical synthesis, monetarism and new classical economics meant that few academic economists now doubted the long-run desirability of open capital accounts.

This combination of forces meant that the support in favor of changing the IMF’s formal and informal rules on capital mobility gradually grew. A first indication came in 1956, when Britain faced a speculative attack on the pound sterling in the aftermath of the Suez crisis (Boughton, 2001). Whereas the Articles of Agreement prohibited the use of the Fund’s resources for financing capital outflows, this was swiftly put aside by the staff and the Executive Board. Against the spirit of the Articles, for the first time IMF financing was used for capital account difficulties, instead of for current account problems, and the staff did not use its power to impose a strengthening of capital controls. Afterwards, it has never used this power when a country facing large capital outflows applied for IMF resources (Galbis, 1996; Polak, 1998). This informal policy was institutionalized in 1961, when the Executive Board approved new rules that allowed the Fund to finance capital outflows (Polak, 1998; Chwieroth, 2008).

A second indication of the norm adoption of capital account liberalization appeared in 1972. A group of experts appointed by the Committee of Twenty\(^1\) concluded that capital controls should not be a permanent feature of the international monetary system, in contrast to what Keynes had defended thirty years earlier (Pauly, 1995). They recommended the adoption of a code of conduct monitored by the IMF to govern the future use of capital controls. In the end, however, the Committee of Twenty could not agree on such a framework, so formally nothing changed. In 1976, the IMF’s Articles were amended so that the promotion of capital mobility became one of the essential purposes of the international monetary system (Chwieroth, 2007b). Yet they did not state that the Fund should promote capital mobility, and the formal rules of the IMF’s framework on capital mobility remained unchanged.

Nevertheless, by the mid-1980s most of the advanced countries had loosened or eliminated controls (Crotty & Epstein, 1996). The capitalist classes were fairly unified in a new, neoliberal policy program, that was implemented in various ways by national politicians. In contrast with earlier decades, the IMF has given greater attention to capital account issues from the late 1980s on (IEO, 2005). The Fund actively began to encourage the liberalization of capital controls (Polak, 1998; Abdelal, 2006; Chwieroth, 2008; Weisbrot, Cordero & Sandoval, 2009). The staff had by now fully internalized the goal of capital account liberalization. As Chwieroth (2008) explains: “In the mid-1980s, recruitment and promotion patterns brought a new cadre of staff members, who were inclined to view liberalization as desirable, to senior positions and consequently shaped the Fund’s adoption of the norm of capital freedom.” By the early 1990s, the staff’s internalization of capital freedom as a norm was more or less complete.

Although the norm of capital account liberalization was not formally institutionalized, and therefore the IMF could not use it in its conditionality packages, there is evidence that IMF program participation is correlated with capital account liberalization, particularly during the 1990s (Polak, 1998; Chwieroth,

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\(^1\) In full: “Committee on Reform of the International Monetary System and Related Matters”, established to study the monetary system after the collapse of the Bretton Woods-system in 1971.
2007b; Joyce & Noy, 2008; Takagi, 2010). This is also confirmed by the Independent Evaluation Office (IEO) of the IMF, which stated in an evaluation report that the IMF “did not hesitate to support capital account liberalization as part of the of the authorities’ overall policy package as expressed in program documents”, which may indicate ‘pressure’, although the report did not find evidence for such pressure (IEO, 2005). The IMF may in any case have been instrumental for neoliberal economists and capitalist classes in EMs and developing countries to strengthen their position and push through liberalizations of the capital account (Soederberg, 2001; IEO, 2005; Chwieroth, 2007b).

**Institutionalizing capital account liberalization?**

In the mid-1990s, proponents of capital account liberalization pursued the institutionalization of the new policy stance in the IMF’s formal rules. One of the big catalysts was the European governments internalization of the norm of capital mobility. While before the US was the main adherent of capital freedom, European governments became very supportive of capital freedom in the early 1990s (Chwieroth, 2008). The project of the European Union was very influential in the acceptance and internalization of the norm of capital mobility by the member states in general and France in particular (Abdelal, 2006). After the adoption of capital freedom as a norm in the EU (1988) and the amendments to the Code of Liberalization of the OECD (1989), European policy makers played a central role in promoting the institutionalization of capital mobility liberalization.

A first step to institutionalization emerged in October 1994, when the Interim Committee² issued a statement in the ‘Madrid Declaration’ welcoming the trend toward full capital mobility (IEO, 2005). The Executive Board directed the staff in 1995 to strengthen their work in encouraging and supporting liberalization (Chwieroth, 2008). In April 1997, the IMF’s Interim Committee announced its intention to revise the IMF Articles of Agreement. At the Hong Kong meeting in September 1997, the Interim Committee adopted a statement that asked the Executive Board to complete work on the modification of the Articles (Kenen, 1998). Two revisions were proposed (Interim Committee, 1997; Wade & Veneroso, 1998; Abdelal, 2006). The first proposed revision would change Article I to include the promotion of the orderly liberalization of capital accounts as one of the main purposes of the Fund. A second proposal would give the Fund jurisdiction over the capital account of its members. Legitimation for these revisions was found in the changed economic reality of large amounts of private international capital flows (Wade & Veneroso, 1998). In practice, the changes would have given the Fund much greater power over EMs and big developing countries. They would have permitted the staff to employ conditionality to encourage capital account liberalization (Abdelal, 2006; Chwieroth, 2008).

The institutionalization almost succeeded, but the Asian crisis threw sand in the wheels of international finance (Abdelal, 2006; Chwieroth, 2008; Gallagher, 2010). The proposed revisions to the Articles of Agreement were rejected by 1999, due to resistance from developing countries, but also from more progressive policymakers in the core countries (Sarai, 2008). As Chwieroth (2008) writes: “Opposition

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² Now the International Monetary and Financial Committee (IMFC), a body which is composed of central bank governors or (finance) ministers, and which reflects the composition of the Executive Board.
among and within the Fund’s principals led consideration of the amendment to be suspended indefinitely.” Probably pragmatic motivations were also important. For instance, in the perception of some US policymakers, a multilateral regime might have empowered the IMF, potentially increasing its power at the expense of the US, while the US was at the center of a less rule-based regime (Abdelal, 2006). While the formal rules may not have changed, it might be useful to examine whether the Asian crisis has altered the ideas and informal practices within the IMF on capital controls.

The Asian crisis as a turning point?

It is broadly accepted that the IMF was very unfavorable towards capital controls in the early 1990s (e.g. Quirk, 1994). The staff tended to be supportive of any development that would increase developing countries’ access to international capital markets (IEO, 2005). It emphasized the benefits of open capital accounts, such as greater resources for investment, more efficient capital allocation, lower interest rates and “discipline on economic policy” (Johnston & Ryan, 1994; see also IEO, 2005). As it thought of capital inflows as typically advantageous, it paid few attention to the potential risks, or it understated them (e.g. Mathieson & Rojas-Suarez, 1992). Thus, due to ideological prejudgments, the Fund overemphasized the benefits of capital account liberalization, and downplayed the risks. Moreover, it labeled capital controls as largely ineffective, especially in the long run (e.g. Mathieson & Rojas-Suarez, 1993; Johnston & Ryan, 1994; Quirk et al., 1995; Dooley, 1996). It also strongly highlighted the long-term costs of capital controls (e.g. Schadler et al., 1993; Johnston & Ryan, 1994; Galbis, 1996). The staff expressed a “general distaste for such controls (...)” (Quirk et al., 1995) and consistently argued for other policies to deal with the consequences of large capital inflows. These policies included fiscal tightening, greater exchange rate flexibility, and in some cases tightening of prudential regulation and liberalization of capital outflows (e.g. Calvo et al., 1993; see also IEO, 2005).

However, despite these recommendations, even before the Asian crisis the Fund’s policy stance was never entirely dogmatic (e.g. Calvo et al., 1993). There has always been a certain awareness that capital account liberalization implicates risks (e.g. Mathieson & Rojas-Suarez, 1992; Quirk et al., 1995) and that herding behavior exists (Calvo et al., 1993; Schadler et al., 1993). The IEO report (2005) observes: “From the beginning of the 1990s, the IMF’s management, staff, and Executive Board were aware of the potential risks of premature capital account liberalization (...).” Even before the Mexican crisis of 1994 there was some approval of capital controls now and then. After the Mexican crisis the Fund gave greater attention to the potential vulnerabilities of countries with large inflows (IEO, 2005). In 1995 two notes were issued saying that temporary capital controls could in certain (exceptional) circumstances be justified (IEO, 2005). A working paper found that both theoretically and empirically there was no robust correlation between open capital accounts and the rate of growth (Grilli & Milesi-Ferretti, 1995). After 1995 the turnaround was more evident (IEO, 2005). Still, only market-based controls on capital inflows were endorsed to a certain extent. Administrative controls, and controls on capital outflows were strongly rejected (e.g. Quirk et al., 1995; Galbis, 1996; see also IEO, 2005).
Although a gradual change was thus already proceeding, the Asian crisis had a profound impact (IEO, 2005). The staff still believed in the advantages of open capital accounts (e.g. Rossi, 1999), but it now started to pay greater attention to the risks of open capital accounts (IEO, 2005). First Deputy Managing Director Stanley Fischer (1998) wrote shortly after the Asian crisis that “markets are not always right”, and that “usually, these swings are rationally based, but they may on occasion be excessive, and they may sometimes reflect contagion effects.” A more cautious approach on capital account liberalization became trendy, with orderly liberalization, sequencing and gradualism as new key words (e.g. Prasad et. al., 2003; see also Lee, 2002; IEO, 2005). However, Wade and Veneroso (1998) note: “It is difficult to escape a sense of déjà-vu: for just the same was said after the disasters following the opening of capital accounts in the Southern Cone in the early 1980s.” Besides, the Asian crisis was at first interpreted not as a consequence of herding behavior, but as the result of ‘crony capitalism’ and national policy mistakes (Soederberg, 2001). Moreover, capital controls were still considered as largely ineffective for dealing with large capital flows (e.g. Laurens & Cardoso, 1998; Nadal-De Simone & Sorsa, 1999), and/or very costly (e.g. Johnston & Tamirisa, 1998; Nadal-De Simone & Sorsa, 1999; Ariyoshi et al., 2000). Strengthening the financial and macroeconomic environment was preferred over controls (e.g. Laurens & Cardoso, 1998). The Fund did not at all abandon the goal of full capital mobility (Fischer, 1998; Lee, 2002; IEO, 2005; Chwieroth, 2008). Behind the scenes, the Fund often still pushed through capital account liberalization (Gallagher, 2010).

Nevertheless, there was more openness to the use of temporary capital controls under certain conditions (e.g. Rossi, 1999; see also Chwieroth, 2008). The IEO report (2005) observes: “As a general rule, the IMF staff, in line with the evolution of the institution’s view, became much more accommodating of the use of capital controls over time, albeit as a temporary, second-best instrument.” Eichengreen and Mussa (1998) stated that market-based controls were not incompatible with “the still-desirable goal of capital account liberalization”. Controls on outflows were far less accepted (e.g. Loungani & Mauro, 2000; see also Polak, 1998), although even on outflows the IMF’s position became more accommodating after the Asian crisis (e.g. Rossi, 1999; see also IEO, 2005). The IMF still opposed the imposition of currency controls, however. In 1998, Jacques Polak summarized the view of the IMF on capital accounts after the Asian crisis: “A fair representation of the current consensus on the subject would seem to be that (1) most capital controls, especially those on capital outflows, are both ineffective (except in the short run) and harmful to the country imposing them, (2) some controls on inflows of short-term funds can be helpful in preventing excessive domestic demand, and (3) some other controls (in particular on inflows of direct investment and portfolio investment) have both negative effects (...) and potential benefits of a prudential or political character.”

**In the run-up to the crisis**

As the years went by, even more subtle changes became visible. Whereas before the beneficial effects of capital account liberalization were presumed, some important papers now recognized that the empirical evidence was meager. Edison et al. (2002) conclude: “There is mixed evidence that capital account liberalization promotes long-run economic growth.” In an influential paper, that is frequently
referred to, Prasad et al. (2003) recognize that “it is difficult to establish a robust causal relationship between the degree of financial integration and output growth performance”. Two papers observed that developing countries do not benefit considerably from international financial integration, even when they receive a lot of inflows (Gourinchas & Jeanne, 2004; Epaulard & Pommeret, 2005). Likewise, while it had always been accepted that open capital accounts carry more risks, these risks were more and more highlighted in the staff’s analyses (e.g. López-Mejía, 1999; Prasad et al., 2003; Gupta et al., 2003; Ötker-Robe et al., 2007). It was also acknowledged that herding behavior and contagion could exist, bearing no relation to country fundamentals (e.g. Ariyoshi et al., 2000; Borensztein & Gelos, 2000; Bikhchandani & Sharma, 2001; Gelos & Wei, 2002; Bayoumi et al., 2003). Moreover, more staff members now accepted that capital controls, both on inflows and outflows, could be effective in temporarily achieving particular objectives (e.g. López-Mejía, 1999; Ariyoshi et al., 2000; Tamirisa, 2004). There was even some sympathy towards longer-term capital controls, such as in China (e.g. Ariyoshi et al., 2000; Prasad et al., 2005).

Despite these more mixed visions on capital account liberalization, there was still a broad disapproval of capital controls. For instance, Bello and Guttal (2005) note: “Even when the IMF admitted that capital controls worked to stabilize the Malaysian economy during the 1997 financial crisis, it remained generally opposed to capital controls. The IMF refused to endorse even the gentlest capital controls.” This is admitted by the IEO report (2005), which concludes: “The documents prepared by the IMF staff in the context of multilateral surveillance during 1990-2003 consistently favored capital account liberalization.” And on capital controls: “It is possible here to make a broad characterization that the IMF staff was in principle opposed to the use of such instruments, either on inflows or outflows.” The staff assumed that there are better solutions to the problems associated with capital account liberalization than controls. For instance, Ariyoshi et al. (2000) conclude: “The evidence presented in this paper supports the conclusion that capital controls cannot substitute for sound macroeconomic policies.” The emphasis was on macroeconomic ‘soundness’, the quality of domestic institutions and the depth of financial markets (e.g. Prasad et al., 2003; Le Fort, 2005; Ötker-Robe et al., 2007; Zakharova, 2008). There was still a lot of skepticism on the (long-term) effectiveness of controls (e.g. Le Fort, 2005; Prasad et al., 2005; Ötker-Robe et al., 2007), and it was still emphasized that the costs are large (e.g. Prasad et al., 2005; Wei & Zhang, 2007). The most significant observation is that the absence of empirical evidence on the beneficial growth effects of capital account liberalization did not lead to the abandoning of the theoretical view that open capital accounts are beneficial (e.g. Prasad et al., 2003; Kaminsky & Schmukler, 2003). On the contrary, the staff attempted to find new evidence that would demonstrate the theory and nuance earlier empirical material. For instance, it was argued that capital account liberalization would boost productivity growth instead of output growth, which would only be fully evident in the long run (e.g. Kose et al., 2006; Kose et al., 2008). Another argument was that open capital accounts are generally beneficial, but mostly when certain threshold conditions are met (e.g. Kose et al., 2006).
**Conclusion**

Although the Articles of Agreement of the IMF were not as straightforward as has been largely accepted, they were important in the legitimation of post-war capital controls. Nevertheless, over the years capital controls became more and more out of fashion, both in (advanced) member states and within the IMF.

The institutionalization of capital account liberalization failed, however, after the Asian crisis in 1997. Even if the IMF was never entirely dogmatic on capital controls, the Asian crisis was influential in pushing the staff to gradually become more open to certain controls. On the last two decades before the global financial crisis broke out in 2007, three observations are essential for the next sections:

1. The IMF has always recognized that open capital accounts bear risks and that the benefits of liberalization are not always larger than the costs. As Carvalho (2002-2003, italicized in original) writes: “Most researchers seem to start from a *parti pris* in favor of liberalization to such an extent that they seem embarrassed by this conclusion.” Despite the IMF’s traditional partiality in favor of liberalization, the empirical evidence gathered by the staff has always been dubious.

2. Still, the emphasis in the IMF’s discourse has gradually changed over time. At first, it overemphasized the benefits and underemphasized the risks. Then, the risks were acknowledged, sequencing became the new buzzword, but it was maintained that controls were ineffective and/or very costly. Moreover, it was argued that there are better solutions to the risks associated with open capital accounts. Finally, after 2003 it was increasingly admitted that the benefits of liberalization are not that large. The views on temporary, market-based controls in extraordinary circumstances became more accommodating, but more permanent controls and controls on outflows were still broadly rejected. The modification of the original discourse was a gradual process, but the Asian crisis clearly had some influence: “From around 1994, and certainly after the Mexican crisis, some within the IMF became more cautious in their policy advice on capital account issues in country work, but it was only after the East Asian crisis that the whole institution’s approach clearly changed” (IEO, 2005).

3. Despite these gradual changes, “the staff team still clearly retain a belief in the long-run desirability of liberalization” (Chwieroth, 2008). It is fair to say that the Fund still acts as a “cheerleader” of capital account liberalization (IEO, 2005). Besides, before the global financial crisis there were some indications that the staff had regained some of its confidence in its positive view on open capital accounts.

**2. THE NEW FRAMEWORK: THE GLOBAL CRISIS AS A TURNING POINT?**

In this section, we will revise the current IMF framework on capital controls. This study will be largely based on the policy framework on managing capital inflows, proposed by the staff in March 2011, which received quite some attention in the media. It is important to recognize the limits of the IMF’s framework. First, the framework is designated for EMs and low-income members. It is assumed that advanced economies do not need capital controls. Second, the framework only takes in consideration measures on capital inflows. For this reason, and to see to what degree the framework is internalized by
the staff, we will also rigorously examine working papers, staff position notes and other official IMF
documents.

Is an open capital account advantageous?

A first observation is that capital mobility is still seen as advantageous for the world economy in general
and for receiving countries in particular. In a staff position note that was an important step on the way
to the proposed policy framework, the authors compare the benefits from capital mobility to the
benefits from free trade, although they also found empirical evidence that countries with capital
controls were able to avoid the worst growth outcomes associated with financial fragility (Ostry et al.,
2010). The policy framework explicitly expresses the view that “inflows are typically beneficial for
receiving countries” (IMF, 2011b; see also Mody & Murshid, 2011; Matheson, 2011; Ostry et al., 2011).
This was also stressed by former Managing Director Strauss-Kahn (IMF, 2010c). Furthermore, the
authors of the framework are convinced that the present wave of inflows to EMs is going to be
persistent, and will bring important investment and growth benefits (IMF, 2011b). One of the
advantages of capital inflows would be a lower cost of capital for both the public and corporate sectors.
As such, capital account liberalization should be the purpose of every country. In this manner, the
framework does not deviate from the earlier policy stance on capital account liberalization, and even
overemphasizes the benefits from open capital accounts in comparison to earlier papers that were
published after the global financial crisis (e.g. Deléchat et al., 2009; Mitra, 2011).

However, the framework also acknowledges that inflow surges “can carry macroeconomic and financial
stability risks” (IMF, 2011b). Broadly, four risks are detected. The first is that capital inflows could lead to
upward pressure on exchange rates that causes a loss of competitiveness. This could result in an
unsustainable current account deficit (IMF, 2011b; also Cardarelli et al., 2009; Atoyan, 2010; Ostry et al.,
2010). A second risk that is identified by the authors is that capital inflows complicate monetary policy
(IMF, 2011b). For example, capital inflows make interest rate policy less effective. However, the
framework does not really address this risk in detail, and in staff papers this risk is more or less ignored
(e.g. Ostry et al., 2011) or downplayed (e.g. Pradhan et al., 2011), although sometimes it is recognized
that capital flows complicate monetary policy (e.g. IMF, 2011a). Third, there is the possibility of
overheating, as manifested by a closed output gap and inflation pressure (IMF, 2011b; also Ostry et al.,
2011; Pradhan et al., 2011). Capital inflows may lead to persistent inflation and worsening inflation
expectations, making it difficult to attain inflation targets.

The fourth risk recognized by the authors is that inflows “have tended to reverse suddenly and in a
synchronized manner, in the past” (IMF, 2011b). Although there are some critical voices, most IMF
papers acknowledge the existence of herding and/or unsustainable asset bubbles (e.g. Mecagni et al.,
2009; Ghosh et al., 2009; Blanchard & Milesi-Ferretti, 2009; Atoyan, 2010; Ostry et al., 2010; Mitra,
2011; Gelos, 2011). In the policy framework, variations in capital flows are described as “a normal
cyclical phenomenon”, but they have been magnified by both policy mistakes and herding behavior in
financial markets (IMF, 2011b). On the one hand, it seems that the authors still keep national policy
mostly responsible for cyclical capital flows. On the other hand, it is admitted that herding behavior may exist and that asset price bubbles may develop. The possibility of sudden reversals of capital flows is recognized, and the authors suggest that push factors, which are not influenced by EMs policy, are dominant in these reversals (see also Frank & Hesse, 2009). For example, the framework implicitly posits that a rise in US interest rates could result in a reversal of capital flows to EMs. The existence of contagion is also admitted.

Can capital flow management (CFM) decrease risks?³

As the IMF identifies several risk to capital inflows, a second question to be asked is whether capital controls can mitigate the risks associated with large and persistent inflows. The framework suggests that “it may be appropriate for several countries, based on their current circumstances, to consider prudential measures or capital controls in response to capital inflows” (IMF, 2011b). However, some qualifications are required.

First of all, the authors question that capital controls may lead to the preferred outcome. In general, the staff sometimes emphasizes that controls can be effective for reaching some particular objectives (e.g. Clemens & Kamil, 2009; Ostry et al., 2010; IMF, 2010a), sometimes argues that the effectiveness is limited in general (e.g. Cardarelli et al., 2009; Shah & Patnaik, 2011), and is sometimes more ‘optimistic’ on the effectiveness on controls (e.g. Binici et al., 2009; Reinhardt et al., 2010). Strauss-Kahn said in November 2009 that “the problem is that most of the time it does not work”. (Guha, 2009). In the proposed framework, evidence on the effectiveness of capital management techniques is defined as “mixed” (IMF, 2011b; see also IMF, 2010).

Second, the costs of capital controls are almost certainly very high (IMF, 2011b; also Cardarelli et al., 2009; Shah & Patnaik, 2011; Ostry et al., 2011). The development of capital markets in EMs may be adversely affected, the cost of administration is high and likely to increase over time, suppression of exchange rate volatility could have negative consequences, and finally, capital controls may cause capital outflows, market turmoil, and a decreased future willingness to invest in the country that applies capital controls. Maybe the largest cost of all, from the viewpoint of the authors, is that capital management may be used to “substitute for appropriate macroeconomic policies” (IMF, 2011b).

Third, capital controls can only be used as a ‘last resort’ and in very specific circumstances. The first priority should be to enact reforms that “increase the capacity of domestic capital markets” and that “enhance the resilience of the financial system”. A prudential framework is considered as the most important instrument to deal with capital flows and to prevent crises (see also IMF, 2011d; Cardarelli et al., 2009; Clemens & Kamil, 2009; Atoyan, 2010; Mitra, 2011).

In the second place, macroeconomic policy responses are also perceived as superior (IMF, 2011b; also IMF, 2011a; IMF, 2011d; Cardarelli et al., 2009; Atoyan, 2010; Magud & Sosa, 2010. Mitra, 2011; Ostry et

³ The framework uses the term capital flow management, which broadly corresponds to capital controls. We will use them as synonyms.
A first macroeconomic policy response is to allow the exchange rate to strengthen, except when there is evidence that the exchange rate is overvalued. In practice this will exclude a large segment of countries from using CFM. A second macroeconomic policy response is to accumulate foreign exchange reserves when these reserves are inadequate from a precautionary perspective. Although it is admitted that this is associated with large costs, sterilized intervention is considered superior to CFM. A third macroeconomic policy response is to use monetary and fiscal policy. Interest rates should be lowered when the economy is not overheating and if it is consistent with inflation targets. However, as large capital inflows often cause overheating, it is difficult to use interest rates as an effective policy instrument. Fiscal policy should be tightened as a countercyclical measure, although it is admitted that this may not always be very effective, particularly in the short run. A figure from a staff position note summarizes the circumstances in which capital controls could be used:
Figure 1. Coping with Surges in Capital Inflows: Macroeconomic and Prudential Considerations 1/

1/ From the perspective of an individual country, without taking account of multilateral considerations; on the effectiveness of controls, see Section III.

(From Ostry et al., 2010)
Thus, while capital controls may possibly decrease risk, they are most of the time ineffective, and the costs are very high. Additionally, certain circumstances have to be fulfilled before capital management techniques may be used: the exchange rate should not be undervalued, reserves should be adequate or sterilization costs excessive, the economy should be overheating so that expansionary monetary policy is not advisable, and fiscal policy should have been tightened.

*What kind of capital controls are legitimate?*

Even though the framework clearly reveals a preference for macroeconomic and prudential policy measures to deal with capital inflows, it states that capital controls could be used. Other papers have also called capital controls ‘legitimate’ in certain circumstances (Atoyan, 2010; Ostry et al., 2010; Ostry et al., 2011; Pradhan et al., 2011; IMF, 2011d). This section will explain which kind of capital controls are considered legitimate by the IMF policy framework. It is important to acknowledge that the Fund does not always legitimize certain controls and delegitimize other controls. The staff takes a pragmatic stance, arguing that specific circumstances need specific measures. For instance, a staff position note states that “there is no “one-size-fits-all” approach to capital control design”, that “measures need to be targeted to the risks at hand” and that “the design of capital controls needs to be tailored to country circumstances” (Ostry et al., 2011). Nevertheless, we can discern an obvious preference for some techniques over others.

First, as described above, the framework only deals with restrictions on capital inflows. Restrictions on capital outflows have always been more controversial (see Soederberg, 2004). The authors suggest that future work will focus on dealing with capital outflows for EMs and low-income members (IMF, 2011b). Other IMF documents indicate that controls on capital outflows will not be legitimized anytime soon. There are few working papers on outflow controls, and in documents such as the World Economic Outlook (IMF, 2011d) they are ‘ignored’ as well. The few papers that refer to outflow controls reject them. For example, Ghosh et al. (2009) write: “Controls on outflows would at best de facto “freeze” credit lines at their current levels while almost surely leading to a collapse of fresh inflows.” There is one document (IMF, 2011b) that states that some countries facing a balance of payments crisis could use outflow controls: “(...) controls on capital outflows may be necessary in circumstances where the potential level of outflows exceeds both the member’s adjustment capacity and the financing available from the official sector.” Thus, according to the Fund, in ‘normal’ circumstances only controls on capital inflows may be legitimate.

The second classification of CFMs is based on the type of capital flows involved. As the composition of inflows in the current wave has generally shifted towards portfolio flows, the IMF focuses mostly on portfolio inflows (IMF, 2011b). It is acknowledged that “the shift toward portfolio flows could be structural in nature and imply continued volatility”. According to the authors, this is problematic as portfolio flows have in the past been more volatile than other types of capital flows and as their volatility has recently risen. In the first place, the framework is concerned with portfolio debt inflows. Second, controls on portfolio equity inflows could also be endorsed. Restrictions on foreign direct
investment (FDI) are not mentioned in the framework. It is reasonable to assume that the Fund disapproves of restrictions on FDI. This is consistent with the ‘common sense’ view that FDI are less volatile than portfolio flows and foreign loans (e.g. Tong & Wei, 2009), although this is challenged in other documents (e.g. IMF, 2011d).

Third, the framework prefers non-residency-based controls (e.g. reserve requirements on foreign exchange deposits) over residency-based controls (e.g. reserve requirements on nonresidents deposits) (IMF, 2011b). The motivation is that “non-discriminatory application of measures to resident and nonresident investors and the absence of restrictions on mobility of flows generally provide reassurances to markets that countries remain receptive to inflows”. Only in the last instance may residency-based CFMs be appropriate, when other options have not been effective or are infeasible.

A fourth classification on which CFMs can be classified, is direct (quantitative) restrictions, which limit the amount of a certain type of capital inflows, versus indirect (market-based) restrictions, for instance taxes on capital inflows. The latter does not prohibit transactions, it only discourages investors by increasing the cost. As the IMF identifies market-based restrictions as more transparent, they are to be preferred (see also Ostry et al., 2011). While it is clear that the IMF favors market-based controls, specific country circumstances may justify the use of quantitative restrictions (also Ostry et al., 2011). Additionally, it is also clear that restrictions on convertibility are unmentionable for the Fund.

Fifth, the framework considers capital controls to be a temporary measure, not a permanent feature of the world economy. As such, measures to limit capital inflows are still conceived as “being deployed temporarily in reaction to an inflow surge” (IMF, 2011b). They should not be used as a permanent solution, and should be reversed as the pressure of capital inflows eases. A staff position note even more explicitly states that capital controls are only justified if the capital inflows are likely to be transitory (Ostry et al., 2010). This was also underlined by Strauss-Kahn (IMF, 2010c). Moreover, it should be assessed on a regular basis if the capital controls are still ‘appropriate’ (Ostry et al., 2010). Nevertheless, in a later note the authors leave open the possibility that controls could be used against more persistent inflows (Ostry et al., 2011).

Finally, and related to the fifth feature, the Fund sees controls as a ‘unilateral’ measure, in two ways. First, it does not want controls to be a widespread phenomenon. The IMF writes “it is important to be cognizant of the multilateral risks if CFMs where to be broadly and indiscriminately adopted, for example through a process of imitation or diffusion” (IMF, 2011b). These ‘risks’ are more explicitly stated in a staff position note (Ostry et al., 2010): “In addition, controls imposed by some countries may lead other countries to adopt them also: widespread adoption of controls could have a chilling longer-term impact on financial integration and globalization, with significant output and welfare losses.” The paper points out that the multilateral dimensions need to be taken into account in the assessment of the capital controls. It is not surprising, then, that a moderate proposition such as the multilateral Securities Transaction Tax is disapproved of, because it is “an inefficient instrument for regulating financial markets and preventing bubbles” (Matheson, 2011). The Fund does certainly not see capital controls as a possible feature of the multilateral international monetary system (e.g. Blanchard & Milesi-Ferretti, 2009; Mateos y Lago et al., 2009). A second way in which the IMF does not consider controls as
a bilateral or multilateral measure, is that there are no suggestions on obligations for other countries (IMF, 2011b). In a certain way this is logical: as the IMF’s emphasis is on receiving countries, obligations for source countries would imply a restriction on outflows, which is rejected by the IMF. Thus, a country may in certain conditions use capital controls, but it must not expect cooperation on the task of effectively enforcing them.

**Conclusion**

The IMF still considers full capital mobility to be advantageous for the world economy and for countries that receive capital inflows. However, it is recognized that inflow surges can carry considerable risks, and that markets may be prone to herding behavior. This does not mean that capital controls are the ‘right’ answer. The effectiveness of controls is questioned, and the costs of capital controls are very high. Thus, prudential measures are to be preferred over controls. Moreover, capital controls may only be used when the exchange rate is not undervalued, when reserves are adequate or sterilization costs very high, when the economy is overheating so that expansionary monetary policy is not advisable, and when fiscal policy is profoundly tightened. If controls should be used, they should be temporary, preferably non-residency based, market-based, country-specific and designed to target the specific risk, which is mostly caused by some sort of portfolio debt or equity flows.

To sum up, while there are signs of a relaxed standpoint on capital management techniques, the importance of the framework should not be overstated. In this respect, it is illustrative that the framework itself recognizes that only one-quarter to one-third of the countries studied in the policy framework study would currently meet the criteria to potentially validate the use of capital controls (7 out of 22 countries, 9 out of 39 countries). This is also evident in a staff position note, which states that almost all examined countries (10 countries in Asia, Turkey, Brazil and South Africa) would have to pursue more orthodox macroeconomic policies, before they could legitimately use capital controls (Pradhan et al., 2011). Moreover, the IMF itself admits that the controls that are so far implemented, and that are seen as legitimate by the Fund, are considered “at the margin” by market participants, and that they will not hold back investors (IMF, 2011b).

### 3. A POSTNEOLIBERAL IMF POSITION ON CAPITAL CONTROLS?

In this section, we will theorize the policy framework and the new policy stance of the IMF on capital controls. The analysis presented in the second section raises several questions. First, what is the novelty of the policy framework? Second, what role did the global crisis play? Third, does the staff fully support the new policy stance?
How innovative is the new framework? 

A first question is to what degree the policy framework differs from the IMF’s earlier view on capital controls and capital account liberalization. While a lot of analysts underline the novelty of the endorsement of controls, the continuities have been underemphasized. Although there may be a change in stress on some aspects, the principles that are underlined by the IMF have not changed much. First, the Fund still presumes that open capital accounts are typically beneficial. Second, it also acknowledges that open capital accounts and inflow surges may carry risks, which was already recognized at the height of the liberalization era in the first half of the 1990s. Third, while capital controls may possibly decrease the risks of open capital accounts, they incur large costs and are most of the time ineffective. Fourth, there are better instruments than controls to deal with large capital inflows. Thus, this is clearly not “the end of an era in global finance”, as Rodrik (2010) has called the IMF’s changed policy stance.

However, while the basic assumptions may not have changed, there has been a gradual change in the practical management of controls. Contrary to common sense interpretations, the role of the global financial crisis in this transformation was not enormous. Already in 1995 the IMF “cautiously argued for the occasional desirability of controls on inward capital flows to developing economies” (Crotty & Epstein, 1996). After the Asian crisis there were internal differences within the IMF on the use of controls on short-term capital inflows (Wade & Veneroso, 1998). As early as 2004, there were observers that wrote that the IMF seemed “to be softening its stance toward capital controls” (Epstein, Grabel & Jomo, 2004; see also Soederberg, 2004). Change was thus already underway before the global financial crisis (see IEO, 2005). Thus, both the novelty of the IMF’s vision and the impact of the global financial crisis on this vision should not be exaggerated.

The crisis probably had some influence though. Especially the changing circumstances may have been essential, with EMs and developing countries experiencing first large capital outflows after the crisis broke out, and then large capital inflows when the US introduced monetary easing policies. But the crisis did certainly not mark a sea change in the economic thinking within the IMF, just as the Asian crisis did not create a great transformation. In capital account liberalization terms, the IMF’s changing position has been a ‘gradual’ process, not a ‘big bang’ process. However, the crisis may have speeded up a process that was already underway, or it may have avoided that the process was reversed. Ilene Grabel and Ha-Joon Chang (2010) give a good description of the development: “Like most transformations, this reform has been gradual. Reform in the IMF view of capital controls actually began soon after the Asian crisis, as countries such as Chile, China and India imposed controls. Most analysts found that these controls were beneficial in key respects. This success led the IMF to soften its hardline stance: it admitted that controls might be tolerable in exceptional cases provided they were temporary, market friendly and focused strictly on capital inflows. (...) What was just a trickle of controls before the current crisis is now a flood.”

However, while the changes are more gradual than abrupt, and while the basic assumptions still remain the same, the framework does present two innovations. First, it is the first time in a long time that the Fund explicitly and officially calls capital controls in certain circumstances ‘legitimate’. This is now the dominant position within the IMF, whereas before it was just one position. Second, it is the first time
that the IMF has presented guidelines on when controls are possible, and what controls may be used
(Harding, 2011). Although there have been more attempts (see e.g. Fischer, 1998), this is the first time
that a framework has been established by the Fund.

One question remains: has the staff fully internalized the use of controls as a legitimate policy
instrument? Is it true, as Grabel and Chang (2010) suppose, that “the IMF did not drive this process of
reform, but its staff have adjusted their thinking quickly in response to the exigencies of the crisis”? At
first sight, it seems that acceptance within the IMF is quite broad. For instance, since the World
Economic Outlook (WEO) in April 2010, it has been repeated in every WEO that capital controls can be a
Moreover, as noted above, various important staff position notes have repeated the legitimacy of
capital controls (Ostry et al., 2010; Ostry et al., 2011; Pradhan et al., 2011). This in stark contradiction
with the situation before the crisis. As Broome (2010) observes, “its support for the judicious use of
exchange controls in a capital account crisis such as Iceland has experienced does indicate a somewhat
greater degree of flexibility in the IMF’s approach to crisis management than in the past”.

On the other hand, there are signals that the IMF staff does not fully support or has not fully internalized
the framework. In the World Economic Outlook of April 2011, a whole chapter is dedicated to the issue
of volatile capital flows (IMF, 2011d). However, while the legitimacy of capital controls is confirmed in
the preface and the first, introductory chapter, the chapter on capital flows does not mention capital
controls, not even in the policy implications (IMF, 2011d). Furthermore, when we examine country
reports and Article IV Consultations Concluding Statement of the Mission in 2009, 2010 and 2011, it
appears that the staff has not internalized the proposed policy framework yet. There are almost no
references to the introduction of capital controls, and most references are negative\(^4\), although there
were a few (potential) endorsements of controls\(^5\) (see also IMF, 2009). Possibly, it is too early to see the
impact of the policy framework, but does not seem likely that the staff fully supports the use of controls
as a legitimate instrument (see also Weisbrot et al., 2009).

Another reading would be that the staff has fully internalized the framework, but that the conditions
that would legitimize controls are just very rare. As explained earlier, the Fund admits that the
framework would not endorse controls in many cases. Moreover, as the director of the Western
Hemisphere Department of the IMF, Nicolás Ayzaguirre, has explained, the IMF is ‘accepting’ capital
controls, it is not ‘recommending’ them (IMF, 2011c). In any case, as Grabel (2010) notes, “we should
expect to find continuing evidence of tension and equivocation in future IMF reports that preclude a
clear and decisive Fund verdict on capital controls”.

\(^4\) E.g. on Israel: http://www.imf.org/external/np/ms/2009/121409a.htm and
http://www.imf.org/external/np/ms/2010/121710.htm; on Turkey

A postneoliberal framework?

If the novelty of the framework is overestimated, can we speak of a ‘postneoliberal’ policy stance? While it would bring us to far to present a comprehensive conceptualization of ‘neoliberalism’, it is necessary to specify what is meant by neoliberalism. Broadly, neoliberalism can be defined in two ways. The first way is to define neoliberalism as an ideology, which states that capitalist markets are always rational and efficient. One of the assumptions of the neoliberal ideology is the efficient markets hypothesis (EMH), “the idea that the prices generated by financial markets represent the best possible estimate of the value of any investment” (Quiggin, 2010). If you define neoliberalism this way, it is reasonable to say that the IMF has never been entirely neoliberal in a dogmatic manner. On the other hand, Chwieroth (2007b) writes that one of the key attributes of neoliberalism is “shared knowledge about the desirability of liberalizing capital controls in the long run.” In this description, we can define the IMF staff as still neoliberal, despite the more nuanced vision of the latter years. In country reports and other documents (e.g. IMF, 2010b) it is obvious that full capital account liberalization is still an objective of the staff.

The second conceptualization defines neoliberalism as a class project, designed to support the interests of (financial) capital and to increase the rate of profit, at the cost of labor. One of the significant differences with neoliberalism as an ideology is that this conceptualization acknowledges that this class project is an adaptative project, that may incorporate or coopt subaltern classes and make certain concessions if necessary. This way it is a more flexible project than a dogmatic, ideological neoliberalism. It is this conception of neoliberalism that is used in this article. It will now be examined whether the IMF policy framework is neoliberal according to this definition.

A first essential observation is that the IMF always strongly emphasizes that capital controls should definitely not be used to diverge from orthodox economic policy (e.g. Ostry et al., 2010). The framework makes clear that “measures that affect inflows merit greater scrutiny because they can potentially be used to substitute for appropriate macroeconomic policies” (IMF, 2011b). The IEO report (2005) remarks on the staff’s diverging assessment on capital controls in two countries are interesting in this respect. It considers the support for controls in one country as related to the fact that that country already had a IMF-supported program in place, whereas the country whose capital controls are rejected did not have a IMF program in place. Former Executive Director Camdessus clarifies this idea in a speech (Interim Committee, 1997): “The point is not to encourage countries to remove capital controls prematurely or prevent them from using capital controls on a temporary basis, when justified. The objective is rather to foster the smooth operation of international capital markets and encourage countries to remove controls in a way that supports the drive towards sustainable macroeconomic policies, strong monetary and financial sectors, and lasting liberalization.” So where capital controls are not endangering the neoliberal project, they are accepted; where they could be used to put in place less orthodox economic policies, they are rejected. This is consistent with Susanne Soederberg’s (2004) critique: “In this sense,
capital controls are only to be used as a means to reach the larger end, namely, the proper (neoliberal) management of financial liberalization.”

The second indication that the IMF does not accept deviations from the neoliberal project is the IMF’s emphasis that ‘policy credibility’ must always be kept in mind when using controls on inflows. The framework makes this clear (IMF, 2011b): “Clear communication with the markets as to the policy objectives was seen as important in signaling the likely next steps to deal with inflows, and whether these were perceived to be part of a broader and longer term strategy to develop local financial markets and encourage financial integration.” In a staff position note it is emphasized that a credible exit strategy from capital controls is crucial to preserve policy credibility (Ghosh et al., 2009).

A third observation is that the ability to contain crises and to regulate crises is a crucial part of the neoliberal story. As Rude (2008) writes: “If financial instability is a means by which capital disciplines world capitalism, capital has to find a way to regulate and control it, to make a liberalized global financial system not just resilient enough to survive its own disorder but also resilient in such a way as to maintain its fundamental hierarchical structure.” While the framework is probably not able the avert crises, the endorsement of certain controls may be used to contain the worst consequences of volatile capital flows. Thus, the policy framework fits perfectly with the capacities of the US state and the international financial institutions such as the IMF to deal with crises without endangering neoliberalism. These capacities have been expanding ever since the beginning of the neoliberal project (Helleiner, 1995; Konings, 2008a).

The fourth indication that the Fund still fully supports the neoliberal class project is the Fund’s rejection of controls on capital outflows. There are several reasons why the IMF is more withdrawn on endorsing outflow controls (Soederberg, 2004). First, restrictions on outflows hinder a quick exit by speculators, while controls on inflows leave open many other options for financial capital. Second, there is a close connection between liberalization of capital outflows and net capital inflows. Thus, the more liberalized capital outflows, the more capital flows in and the more foreign capital penetrates the national social formation, which makes it harder to pursue unorthodox economic policies. Third, while inflow controls do not generally lead to substantially more policy autonomy, outflow controls could be used to increase policy autonomy. For these reasons, controls on outflows threaten the norm of free capital mobility as the only alternative. As Soederberg (2004) writes: “Indeed, by sanctioning a particular type of capital control it is engaging in a political judgement call, which is based upon certain material interests, as opposed to mere economic logic.”

This brings us to the fifth reflection. The Fund threats capital controls as a technical matter, not as a political issue. So, Olivier Blanchard, Director of the Research Department of the IMF, writes on his blog that “while the issue of capital controls is fraught with ideological overtones, it is fundamentally a technical one, indeed a highly technical one” (Blanchard, 2011). In this way economic policy is depoliticized, so that it can be left to technocrats and economists and be ‘protected’ from democratic decisions that could endanger the class-based character of neoliberalism. However, as Crotty (2000) writes: “It is clear that there are no serious technical or economic – as opposed to political – impediments to the use of capital controls.” The depoliticization of economic policy has thus been an
important strategy of neoliberalism to cope with possible resistance from subaltern social forces (Birchfield, 1999; Harvey, 2005). It also draws attention away from the power relations that are changed by capital account liberalization. Capital controls may alter the power relations between labor and capital to the advantage of the former (Crotty & Epstein, 1996). Jayadev (2007) demonstrates empirically that open capital accounts are correlated with a lower labor share in national income. By encouraging open capital accounts as depoliticized, technical ‘good economic policy’, the Fund therefore engages in a class-based project that favors internationally mobile capital.

So, to conclude, in the definition of neoliberalism as a class project, capital controls are not necessarily opposed to a neoliberal project. They can be used to reproduce neoliberal power structures as opposed to a more equal and just society (Soederberg, 2002). It seems that the Fund does not deviate much from a neoliberal policy stance on capital controls. The questions then becomes: how should we conceive this framework, as it does not imply a postneoliberal position?

The policy framework as an example of the ‘new constitutionalism’

To assess how we should conceive the framework it might be interesting to take a look at the reactions on the framework by national state officials in the IMFC. Although it was suggested that there was a relatively great consensus within the Executive Board on the framework (Harding, 2011), member state reactions have been diverse in the IMFC. Ayzaguirre has explained (IMF, 2011c): “Some countries have considered that we should not have ever mentioned that capital controls are a legitimate part of the toolkit. Some others consider that even trying to have guidelines for capital controls is unacceptable.” Broadly, there were three sorts of comments on the proposed framework. First, there is a group of countries that emphasize that controls should definitely be an exception (the US⁷, Germany⁸, the UK⁹, France¹⁰, Italy¹¹, the Netherlands¹², Norway¹³) or that are very skeptical of the use of controls (Chile¹⁴, Belgium¹⁵, Switzerland¹⁶). Second, there are countries that do not really give their opinion (Canada¹⁷, Ethiopia¹⁸). Third, there are the BIC-countries (Brazil¹⁹, India²⁰ and China²¹) that welcomed the IMF’s endorsement of capital controls.

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However, while the advanced countries largely support the framework, China and Brazil are very critical of the framework. First, they argue that there is insufficient consideration to the ‘push’ factors or the policies in advanced economies, by which it is clear they target the US. Yi Gang, Deputy Governor of the Chinese central bank, said that the Fund should “strengthen macroeconomic surveillance and coordination of the major reserve currency-issuing countries”. While the focus on push countries may not be adequate to China and Brazil, it is definitely not the case that there is no attention at all on push factors (IMF, 2011b; see also IMF, 2010b; IMF, 2011d). Second, and more importantly for this article, they regard the framework as an attempt to limit the capital controls that may be legitimately introduced. Brazil’s Finance Minister Guido Mantega’s statements are clear: “We oppose any guidelines, frameworks or “codes of conduct” that attempt to constrain, directly or indirectly, policy responses of countries facing surges in volatile capital inflows. Governments must have flexibility and discretion to adopt policies that they consider appropriate, including macroeconomic, prudential measures and capital controls.”

Clearly then, Brazil interprets the framework as an instrument to restrain the policy autonomy of member states, as only certain controls may be used, and only in certain circumstances. In this regard, the renewed IMF dynamism on capital controls can be seen as an example of what Stephen Gill (1998) calls ‘new constitutionalism’. As Gill (2008) observes: “Central, therefore, to new constitutionalism is the imposition on public institutions, partly to prevent national interference with the property rights and entry and exit options of holders of mobile capital with regard to particular political jurisdictions. These initiatives are also linked to efforts to define appropriate policy, partly by strengthening surveillance mechanisms of international organizations (…)”.

The suggested amendment of the Articles of Agreement in 1997 can undoubtedly be understood as an attempt to ‘constitutionalize’ neoliberalism (Soederberg, 2001). While the IMF was already promoting and encouraging capital account liberalization, the proposed amendment would lock-in open capital accounts. The proposed policy framework can be seen as a more subtle, and more flexible form of new constitutionalism. It was developed as a way to outline the “global rules of the game” (IMF, 2010b; IMF, 2011b). Although it creates no legal obligations under Fund surveillance, the framework itself indicates that “it forms part of a broader effort to sharpen Fund surveillance (…)” (IMF, 2011b). In a paper in 2010, it was stated more explicitly that the IMF should have the mandate “to identify actions that members should take or refrain from” in designing capital account policies (IMF, 2010b). It is also remarkable that Ayzaguirre has declared that the IMF has the mandate to preserve the stability of the international monetary system, and that the Fund could use this mandate to suppress the proliferation of capital controls (IMF, 2011c).

Thus, to sum up, due to the neoliberal bias of the IMF, the framework that was developed can be understood as an example of ‘new constitutionalism’. It is an attempt to restrain the use of controls by EMs and transfer economic policy from democratic policymaking towards the IMF staff. This is probably the most important reason why Brazil and China have protested against the framework.

4. CONCLUSION:

This article has argued that the ruptures in the IMF’s position on capital controls since its foundation have been overstated, and that the continuities have been underemphasized. Even after the norm adoption of capital account liberalization, the IMF has never been entirely dogmatic on open capital accounts. Still, there has been a change of emphasis over time, especially after the Asian crisis. Despite these changes, the IMF staff still clearly believed in the long-run desirability of full capital mobility.

Just as the Asian crisis had some influence in the gradual process of a more flexible policy stance, the global financial crisis may as well have speeded up this process. There have been two innovations. First, the Fund has now explicitly called controls ‘legitimate’ in certain conditions. Second, it is the first time that the IMF has presented guidelines on capital controls. However, while the views on temporary, market-based controls in extraordinary circumstances have become more accommodating, more permanent controls, multilateral controls and controls on outflows are still strongly rejected. Thus, the novelty of the IMF position should not be overstated. Full capital mobility is still seen as advantageous for the world economy and for EMs.

It seems, then, that the Fund does not (yet) deviate from a (pragmatic) neoliberal class project on capital controls. The new IMF position should not be seen as a large turn away from neoliberalism, but as an attempt to ‘constitutionalize’ neoliberal policies. As Soederberg (2002) writes on the Chilean experience, it “should make its supporters hesitant to embrace country-level capital controls without addressing the underlying policy paradoxes and power structures (...).”

The more pragmatic IMF vision is a double-edged sword: while it may undoubtedly limit some of the most disruptive effects of volatile capital flows, it could also give the Fund more legitimacy (see also Felder, 2008). But if the conclusions of this article are correct, then a more legitimate but unchanged IMF would be a dangerous combination. Soederberg (2004) observes: “Largely due to its appearance as a pluralistic multilateral lending institution and its exclusive emphasis on the economic dimensions of capital controls, the IMF is not only able to reproduce the “common sense” assumption that free capital mobility is a natural phenomenon driven by the external forces of globalisation, but also its ability to cloud the fact that the Fund’s judgement call is primarily political in nature.”

If the IMF were truly to become a postneoliberal organization, its position on capital controls should be substantially more flexible and accommodating in at least three ways. First, the Fund should as a minimum accept controls on capital outflows, quantitative controls, and permanent capital controls. As such, the IMF would ‘permit’ countries to acquire more policy autonomy to deviate from orthodox, neoliberal policies. Second, it should give technical assistance to countries that would increase the effectiveness of capital controls, instead of questioning the effectiveness (see also Gallagher, 2011). Third, it should stress the multilateral coordination of controls, which means that IMF member states should cooperate to enforce the controls of other countries. As such, the effectiveness of controls would again be increased, and this could also help to reduce conflicts between states on the introduction of capital controls. However, for now at least, this vision looks rather utopian, and “optimism about the
emergence of a post-neoliberal IMF seems misplaced (…)” (Gabor, 2010). It may not be ‘our grandfather’s IMF’, as Grabel (2010) claims, but for now it does not seem significantly different from our father’s IMF.

5. REFERENCES


