IMF struggles to conceal glee

By Alan Beattie in Washington

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Though International Monetary Fund officials try to conceal their excitement at the thought of another country sliding towards financial disaster, there is no doubt that leading **a rescue effort for Greece** will be an enormous prize.

Decried a couple of years ago as too small to be useful, the **IMF** has expanded its lending capability rapidly thanks to a string of higher contributions from member governments, and led a series of rescues in troubled east European countries. Taking primary responsibility for designing and financing a lending programme to prevent Greece defaulting on its debt would be the first IMF crisis loan to a big west European country since the UK and Italy in the 1970s.

Arvind Subramanian, a fellow at the Peterson Institute think-tank in Washington, says: “When the IMF started increasing its firepower, it looked like the Brussels backyard clean-up fund. Now they are moving into the front yard as well.”

As it has often done in the past, the IMF’s involvement will allow government officials – in this case, those from Germany in particular – to import credibility from the fund’s involvement while palming off the unpalatable task of asking for painful economic reforms.

Uri Dadush, a former World Bank official now at the Carnegie Endowment in Washington, says: “It is much easier for the IMF to impose tough conditions than for Germany or France.”

Berlin, which is likely to provide much of Europe’s share of a rescue package, is much keener on the fund’s involvement than is Paris, where matters are complicated by persistent **rumours of political rivalry** between Dominique Strauss-Kahn, the French socialist who heads the IMF, and Nicolas Sarkozy, the centre-right French president.

Though the IMF is likely to play a vital gatekeeper role in co-ordinating a programme, it is not clear what share it could itself provide of the estimated $25bn-$40bn that Greece may need.

Still, there are some advantages in borrowing direct from the institution. The fund lends at a relatively cheap rate, based on an average of interest rates from the world’s leading currencies plus a premium that rises with the size of the loan.

Eswar Prasad, a former IMF official now at Cornell University and the Brookings Institution, says: “By borrowing from the IMF, Greece can get higher credibility with lower costs.”

Conditions are likely to be stringent. The IMF has focused recently on getting large amounts of money, with relatively few strings attached, to economies hit by financial contagion from abroad.

That description does not fit Greece, which is regarded widely as the architect of its own misfortune, and its borrowing is likely to involve the tough conditions set under traditional stand-by arrangements.

Those demands will have only a very limited set of policy tools. As a eurozone member, Greece is in the unusual position of not controlling its currency or its interest rates.

A severe tightening in fiscal policy remains as the sole means of returning it to solvency and stability, recalling the old saying that IMF stood for “It’s Mostly Fiscal”.

“Since it can’t ask for any action on the exchange rate, the fund will have to impose very tough conditions on fiscal policy,” Prof Prasad says.

Given the role of **misleading accounting in hiding Greece’s past budget deficit**, the fund will probably also ask for guarantees of transparency in public accounting.

When the IMF co-ordinated a rescue operation for Latvia in late 2008, it was accused by some observers of going soft on the country under pressure from the European Union. But in Greece’s case the EU and the eurozone have come to the fund after failing to agree their own rescue, so it is likely to have a freer hand this time.

“The IMF will be in a much stronger position than it was in Latvia, which came at a time when the fund was scrambling for business," Prof Prasad says.

To go within two or three years from near irrelevance to leading a financial rescue operation for a west European country marks a striking change in fortune for the IMF. It is an opportunity that the institution is determined to grasp.