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Analysis: Emboldened IMF toughens tone with top benefactor

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By Emily Kaiser

WASHINGTON (Reuters) - The International Monetary Fund finally seems to be baring teeth sharp enough to bite its biggest shareholder -- the United States.

The question is how Washington will respond.

In the barrage of reports prepared for finance ministers who met this weekend, the IMF questioned whether the United States would meet a pledge to halve its budget deficit by 2013, eliciting a swift response from the Treasury Department which insisted the promise would be kept.

The IMF also took the Obama administration to task over its housing policy, and said the United States ought to count its commitments to housing finance giants Fannie Mae and Freddie Mac on its already swollen balance sheet.

"The IMF suddenly is doing its best to seem even-handed," said Eswar Prasad, a Brookings Institution senior fellow and a former IMF official.

Prasad pointed to two factors behind the tougher tone: Emerging markets have pressed the IMF to take a harder look at the advanced economies that caused the 2007-2009 financial crisis, and the United States hasn't strenuously objected to the louder criticism.

Indeed, U.S. Treasury Secretary Timothy Geithner -- a former IMF official himself -- said on Saturday that Washington welcomed "continued IMF surveillance of our fiscal and monetary policies."

The IMF's tone shifted after its internal watchdog issued a scathing report in February that said the fund failed to spot the financial crisis brewing, in part because it was "overly influenced by and sometimes in awe of" rich nations.

LOSING ITS SWAGGER

Since the crisis, the United States has lost some of its policy swagger. Emerging markets that had been on the receiving end of sometimes unwanted advice from the West have begun openly questioning U.S.-led economic orthodoxy.

"Some of the countries that are responsible for the deepest crisis since the Great Depression, and have yet to solve their own problems, are eager to prescribe codes of conduct to the rest of the world," Brazilian Finance Minister Guido Mantega told the IMF's steering committee on Saturday.

Many emerging markets have built up huge stockpiles of currency reserves, partly as a form of self-insurance so that they will never again have to come hat in hand to the IMF, whose loans come with strict conditions.

That has emboldened them to demand that the IMF treat misbehaving advanced economies the same way that emerging markets were treated when they suffered similar crises.

Domenico Lombardi, president of the Oxford Institute for Economic Policy, said the fund's "unusually harsh" tone toward the United States was a way of proving it could be fair when it reviews large countries' policies as part of a Group of 20 program announced on Friday.

The United States is one of seven countries the G20 rich and emerging economies designated for special review to determine whether their domestic policies risked destabilizing the global economy. The IMF is responsible for conducting the reviews.

"Because this mandate the IMF has just received does not come with enforcement powers, the only leverage it has is its credibility, its respectability, as an honest broker," said Lombardi, who is a former IMF executive board member.

The lack of enforcement power has always been the IMF's Achilles' heel. It can talk tough all it wants, but what recourse does it have if no one listens?

The fund has most clout when it is lending and can impose strict conditions in return for aid.

Lombardi, however, said Washington might be more willing than in the past to take IMF advice and put it into action.

Washington is already moving toward deficit reduction, and Geithner is well aware that if the IMF takes a tougher tone with the United States it will have more political cover to talk tough to China.

After two years of intensified bilateral meetings with China, the United States has had little tangible success in convincing Beijing to allow its yuan currency to rise faster in value. It could use the IMF's backing as leverage.

"Treasury secretaries in the past have discounted benefits from international cooperation," Lombardi said. "Now the U.S. has realized that it does not have the power to lead the world alone. In order to assert its leadership, it has to engage in international cooperation."

(Additional reporting by Lesley Wroughton; Editing by Tim Ahmann)