Aeon Investment Management
long term wealth creation

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South Africa, the IMF and European bailouts

"I would not join any club that would have someone like me for a member."
-- Groucho Marx

Earlier this year, emerging markets reacted with giddy excitement at the prospect of being given greater representation and voting rights at the IMF. Several, including South Africa, put forward their own candidates to head the IMF after Dominique Strauss-Kahn's resignation. While a small emerging market country such as South Africa may feel exalted to sit at the table with the world powers, it is going to come with a steep bill. Given the level of indebtedness of the developed economies; it is clear which way money is going to flow in the coming years. After his return from the IMF conference in Washington, South African finance minister Pravin Gordhan has recently stated that South Africa would contribute "a couple of hundred million US dollars" to the EU rescue package.

This 'contribution' cannot be allowed to happen for two reasons. Firstly, it effectively involves the transfer of wealth from the poor to the rich. South Africa is a developing market with a per capita income of around 6000USD, and a highly skewed income distribution. The per capita income of Europe at over 30000USD is at least 5 times ours. Why our Finance Minister feels that we should 'contribute' to improving the living standards of those 5 times richer than ourselves is inexplicable. The second reason we should not be willing to contribute to any EU bailout package is due to the fact that IMF bailouts have always been creditor bailouts, with the focus on repaying bank loans. These country "bail outs" are simply bank bailouts in disguise, and the proposals being floated for the EU 'rescue package' are no different.

The term 'bailout' was used to define the IMF involvement in the 1997 Asian financial crisis in order to imply that the they were "bailing out" or assisting countries with their economic problems. However, the nature of the programs implemented by the IMF merely served to bail out the western banks who had taken excessive exposure to companies in Thailand, South Korea and Indonesia during the years of high growth. The prescribed IMF policies of high interest rates, maintaining currency pegs and allowing the failure of weak banks served to exacerbate the economic crisis. With IMF policies designed to increase the ability to repay western debtors, it is hardly surprising that per capita income in countries such as Thailand, Malaysia and South Korea fell around 10%. The 20% fall in Indonesia was particularly severe, with the impact in their country similar to that of the great depression.

When the credit crisis hit the developed world in 2008, policies were and continue to be precisely the opposite of what was implemented in emerging markets in 1997. The prescriptions are now currency devaluation instead of currency pegs, zero interest rates instead of rate hikes, and bank bailouts instead of failures. The IMF has always existed to forward the interests of the US and Europe, and it is particularly galling that after years of being victims of IMF policies, emerging markets are now expected to contribute to funding the organisation. South Africa has its own pressing economic concerns, and any funds which the South African treasury intends to send to Europe are better used to aid our own development.

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