

CHAPTER I

INTRODUCTION

This chapter includes Background of the Research, Research Question, Theoretical Framework, Hypothesis, Methodology, Scope of Research, and Organization of Writing.

A. Background

The International Monetary Fund (IMF) was formed at a United Nations (UN) conference in Bretton Woods, New Hampshire, United States, in July 1944. The goal of IMF establishment was to create an economic cooperation arrangement in order to avoid another devaluation caused by the Great Depression in 1930s. Through negotiations and agreements from all 44 non-communist nations, they decided to create a structure and operation of the international monetary system. Therefore, the main purpose of the IMF is to ensure the stability of the international monetary system. It is a currency exchange system and international payment system that allows countries to trade each other. Today, there are 189 members in IMF and the Fund's mandate was updated in 2012 to include all macroeconomic and financial sector issues that bear on global stability (Horsefield, 1961, pp. 38-39).

In IMF, there are some departments that have been divided into their own particular matters. One of the most important division is the Executive Board. Its concern is taking responsibility to conduct the everyday business. The Board members are selected through the amount of their country's contribution to IMF.

Therefore, the Board has a higher status in IMF for being the decision maker which likely to approve any policies or any related business towards debts and loans to all country members. Although the decision making process outcome had to be approved through voting system in the Board and IMF members, it must be still considered by Article IV Consultations (IMF, 2015).

Having to know that IMF like most other International Organizations was established in order to gain closer relationship among states and also to help solving several problems happening in some countries, there must have been several requirements or conditions to follow in order to get the assistance needed by the country. In IMF particularly, the financial assistance is given to the country experiencing an economic crisis called as Structural Adjustment Programmes (SAPs). Surely, these SAPs do not come for free. For the country that experiences economic crisis and needs some financial aids from IMF, there are some conditions to follow in order to get those aids (IMF, 2016).

Loans and related conditions are well known as the macroeconomic system to reduce the budget deficit, devaluation and domestic conditions. The regular preconditions and regulations for debtor states are credit expansion and structural conditions such as controlled release, prices and interest rates (raising the price of public services), reducing trade barriers, privatization of state enterprises (Easterly, 2003, p. 5). These terms also include eliminating food subsidies and cutting wages. The logic of the appropriate conditions for IMF loan intended to help countries address the macroeconomic instability. However, this condition does not fully

respect the national sovereignty and somehow approaching the neo-colonialism (Barkin, 2006, p. 96).

Egypt became the permanent member in IMF since 27 of December 1947 (IMF, 2017). In 1987, Egypt was in its journey to a huge crisis during Hosni Mubarak regime. The crisis arose due to the low income from foreign exchange and the world oil price has fallen to less than \$10/barrel, which led to an openly huge unemployment, low productivity, high rates of inflation, and accumulating public debt (Ibrahim, 1991). Thus, Egypt decided to ask financial assistance program to IMF in order to reduce public expenditure, liberalize private sector, and improve performance financial market.

However, Egypt did not abide by the terms of the agreement, and the contract collapsed in the end of 1987. This agreement was canceled after only half of the support fund was dispatched (Nagarajan, 2013). By 1990, Egypt was starting to enter virtual bankruptcy and it kept on asking IMF to approve their debt request. According to IMF conditions, Egypt still failed in fulfilling the requirements and was still not eligible to receive some loans.

Although in 1991 IMF finally approved Egypt financial assistance request, the IMF staff expressed dissatisfaction with the efficacy of lenient agreements, particularly when many of its prescribed preconditions and conditions were ignored from the Article IV Consultations (Momani, 2004). Unfortunately, Egypt still allowed to get the loans even though the credit did not come for free. There were still some several requirements to fulfill which made Egypt have to conclude a

structural reform agreement with IMF. At this time, a serious attempt to implement the program closely monitored by Egypt began (Reuters, 1991).

B. Research Question

Based on the background of the research, the research question of this undergraduate is: Why did IMF finally approve the debt request from Egypt in 1987-1991 although it was not qualified to receive the financial aids?

C. Theoretical Framework

In order to answer the research question, the writer decided to use the concept of International Organizations from J. Samuel Barkin and Theory of Liberal Intergovernmentalism by Andrew Moravscik.

1. International Organizations Concept

International organizations (IOs) are voluntary or similar to the international community on the basis of organizations aimed at creating world peace in the governance of international relations. Therefore, most of IOs in the world were established by the post of World War II and through the agreement or treaty signed by more than two countries. In addition, since all countries decided to unite and realize that they are depending to each other.

According to J. Samuel Barkin, IOs establishment is supported by several causes such as sovereignty, globalization, power, and interdependency (Barkin, 2006, p. 3). Sovereignty is the traditional starting point of the theory of international relations in which world politics is used as a power struggle for sovereign states. Furthermore, international organizations can be regarded as a

state institution to promote the power of globalization, or can be considered as the use of state agents to protect themselves from the forces of wider globalization.

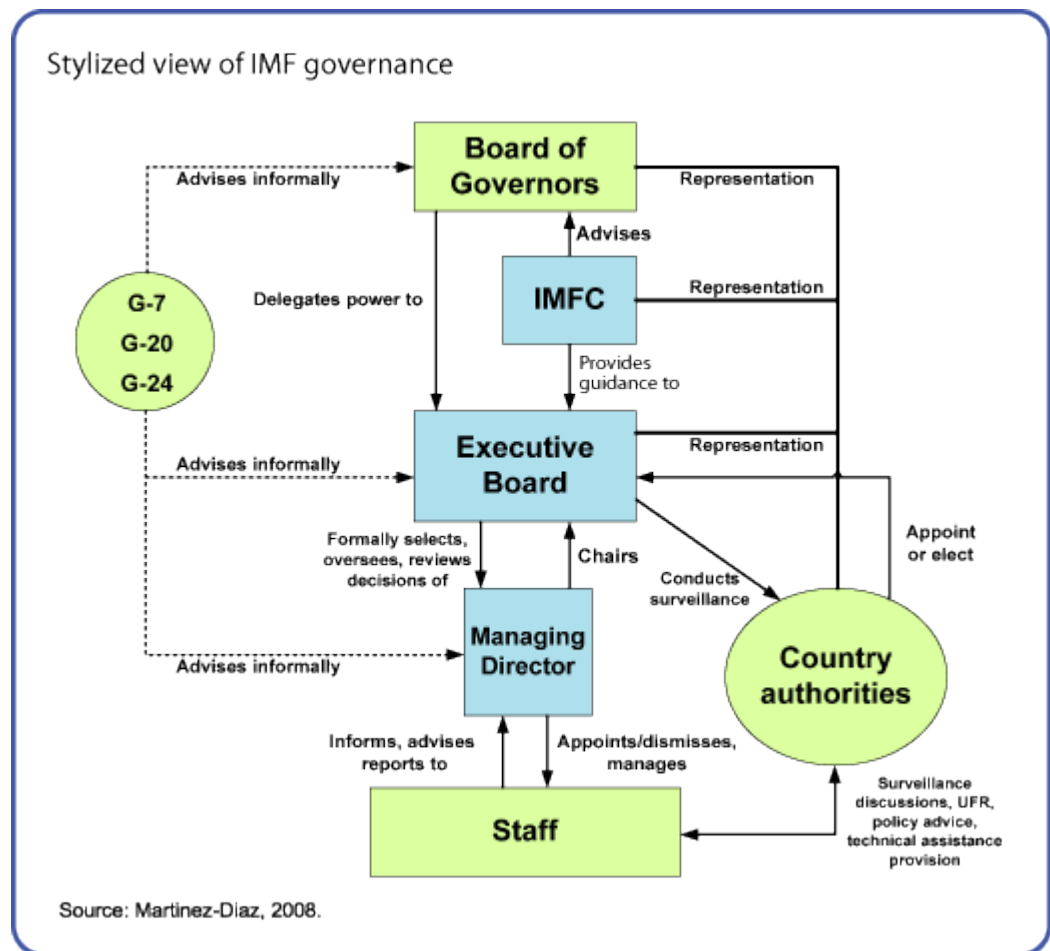
Globalization is due to changes in technology, communication and economy making the country become more interdependent. Some analysts of IOs certain that joining the international organization is the most effective way for countries to deal with interdependence. They are the media through which states pull together for promoting the best outcomes for everyone in an interdependent world. However, many argued that IOs are not neutral agents of cooperation, but they represent certain countries and mechanisms in which powerful states control less powerful interests (Barkin, 2006, p. 3).

In essence, states in an international organization have the same position and level, as a member. According to Articles on the Responsibility of International Organizations (ARIO) in 2011, Member State can have a possible position that can be relevant with international organizations (Gaja, 2011). However, there are still several hidden identities, even though the country has already qualified as a member state. ARIO made international organizations into a strong entity that international organization sets up for helping, coercing or guiding the Member States to the possibilities (Nijhoff, 2015). At the same time, states acting in the capacity as members are also empowered by the rule of international responsibility.

Consequently, it is very important to be careful in examining the member states responsibilities in international organizations. First, the position of a Member State can be closely related to the organization, since the act of complaint can be associated with both subjects at the same time. Second, an organization may make a decision on a member's wrongful act, such as giving assistance, or a commissioned control component of a command and misconduct, or through a binding decision on a member State to achieve each action. Lastly, in some cases, Member States intended that they are responsible for the conduct to be associated with the organization (Nijhoff, 2015, p. 20). Thus, it can be concluded that the international organization also has its own system in regulating its members including in International Monetary Fund.

International Monetary Fund (IMF) has its own governmental system. The Board of Governors is made out of one representative and one alternate from each of the IMF's state member which usually came from the central bank governor. It meets once every year for a couple of hours and directs the Executive Board (the Board), to which it has appointed most of its forces.

Figure 1 IMF Governance



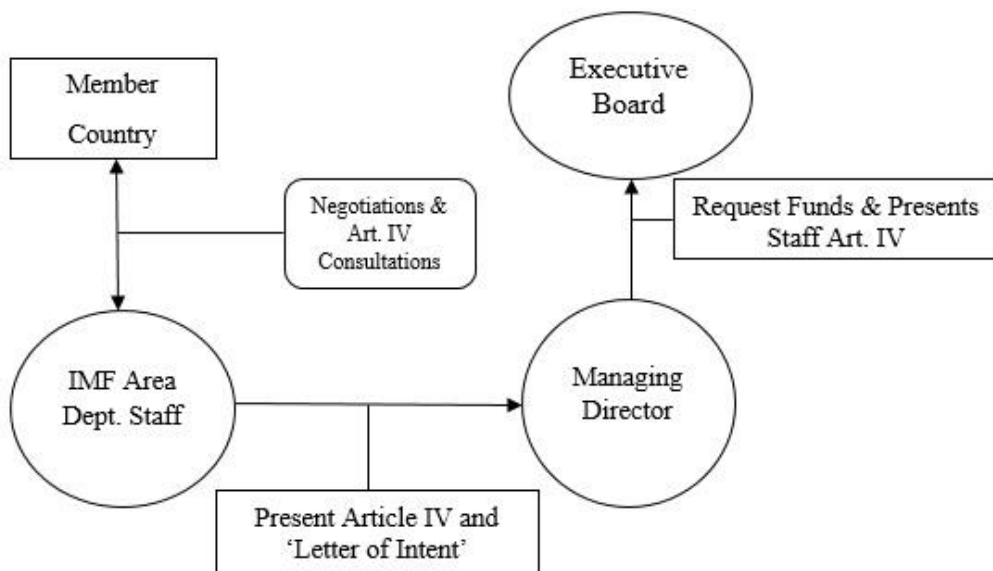
Source: (Martinez-Diaz, 2008)

The Board is made out of 24 Executive (Directors), five of whom are delegated by the IMF individuals having the biggest quotas. Furthermore, 19 of whom are chosen by alternate individuals and composed in voting demographics. Voting power on the Board is dictated by individuals' shares. Administration is made out of the Managing Director (MD) and three delegates.

Another vital component in the administration structure of the IMF is in this volume only covers indirectly, it is made out of a few informal country

groupings. These countries meet frequently to arrange positions and raise issues to the consideration of the Board and most effective ones are the G-7, the G-20, and the G-24. These groupings work outside the formal structure of the IMF and their participations are self-selected, which brings up issues about their legitimacy (Martinez-Diaz, 2008).

Figure 2 IMF Decision Making Process



Source: (Momani, 2004)

While for the decision making process, IMF also has its own procedure based on Article IV Consultation (IMF, 2016). When a state member of the IMF requests a financial assistance, the IMF Staff will give the Structural Adjustment Program (SAPs) or the preconditions before getting the loans. The debtor state candidate has to fulfill the SAPs conditions. If the debtor state candidate did not fulfill the whole preconditions, the IMF staff will reject the

debt request. However, when the state member is fulfilling the whole preconditions, the IMF Staff is going to send the Letter of Intent to the Managing Director. Lastly, the Managing Director will receive the Letter of Intent and pass the request fund from the debtor state to the Executive Board for the final call. Therefore, the Executive Board is on the top of the IMF decision making process, making it the most powerful actor.

2. Liberal Intergovernmentalism

In order to answer the research question, this liberal intergovernmentalism theory is the most suited one to be applied. According to Moravscik, liberal intergovernmentalism has two main basic thoughts such as state as an actor and state as the most rational or the most logic actor in minimalizing negative impacts (Andrew Moravsik, 2009, p. 68). First, state as an actor means state can achieve their goals through negotiation and bargaining between governments directly, not through the creation of a centralized authority and enforce political decisions. Second, state as the most rational actor means that actor will calculate the need for alternative courses of action and choose the one that maximized their needs in a situation. Furthermore, agreement for cooperation or to establish international organizations affected by the collective results that depend on the state of rational selection and strategic intergovernmental negotiations (Andrew Moravsik, 2009, p. 68).

This theory explains that international organizations created from more than two countries agreements in order to overcome global issues and also to conduct more interdependency among state members which can be called as an

integration of many countries into one unity. However, it also says that a state is the main actor. It is true that these countries coming together and united creating an integration in the world, so that they could prevent or minimize any damages from serious global issues. This activity could also lead to intervention where a certain country has its own interest towards another country by using their privilege to conduct it or the emergence of hegemonic power in the system.

According to Charles P. Kindleberger's book, the role played by a hegemonic power is very important in making balance in international politics and economy. If a strong hegemonic power does not exist, it is impossible to create an international stability (Kindleberger, 1973, p. 28). In this research, the United States is the one who has the hegemonic power in IMF. Which means most of the decision and output from IMF are actually based on the United States decision since it has the largest contribution in this international organization.

For this undergraduate thesis, there was an intervention happened inside the decision making system of IMF. The decision making process in IMF is mainly laid on the Executive Board's hand. The Executive Board members included United States, Japan, Germany, France, United Kingdom, Italy, and Canada were the countries that finally decided the final outcome of each IMF policy (IMF, 1991, p. 15). These countries called as the G-7 members as they are the highest contributor in IMF and also represent 64% of the net global wealth.

The IMF decision is intended to reflect the relative position of its members in the global economy. IMF continues reforming the governance structure to ensure that it adequately reflects the fundamental changes in the world economy, including a greater role of emerging markets and developing countries play in the global economy (IMF, 2016). The decision making has to go through the voting system in Executive Board, but different way of voting from United Nations. Voting right in IMF is based on how much money the country invest in IMF, it can be said that the more contribution the country put means the more voting right the country will get.

The United States came out as the biggest and most influential voting power than any other states (IMF, 2017). Since Egypt was not able to fulfill the whole conditions to get the SAPs, the Executive Board should not agree on giving Egypt the financial assistance according to Article IV. Yet, the United States with more than 15% voting power agreed on giving the loans with another condition to follow. It can be seen that the United States was interfering the decision making with another Executive Member, because the United States tried to integrate with Egypt in order to minimize some damages and loss for both countries.

Going back to financial aids requested by Egypt to IMF, Egypt became a very strategic and important interest to Washington, D.C. The United States wanted to take Egypt's attention which in the end, they were going to allow and support the U.S. to join the Gulf War. Therefore, the United States used their position and voting power in IMF Executive Board to finally approve the

financial aids request from Egypt. There were four IMF–Egyptian loan discussions and it was found that two of the four discussions were politically determined (Weisbrot & Johnston, 2016). Two IMF–Egyptian final agreements were facilitated by the United States and Egypt finally got their financial assistance even though they were not fulfilling the whole conditions from Article IV Consultations. Therefore, it can be mentioned that the United States was interfering IMF final decision to Egypt in order to conduct their national interest in joining the Gulf War.

By linking all the theoretical frameworks to answer the research question, it can be explained that International Organizations were established and created from the states treaty to unite and conquer any global issues to come. Also, IOs came with their own ideal rules and regulations to follow by the state members. Thus, all states in IOs considered as member and equal. However, the intergovernmentalism had mentioned that state is the main rational actor, even in IOs. States are the one who conduct any policy making and related businesses in IOs that meant to integrate all country members. The integration that was going on could led into an intervention to several IOs regulations. This happened because each country has their own interest toward another country member and they will finally had to interfere the system if they simply could not find any other rational and possible ways.

D. Hypothesis

Based on the background of the study and the theoretical framework, the hypothesis of this research is: IMF decision on approving financial assistance to

Egypt in 1987-1991 was influenced by the United States hegemonic power in getting its national interest.

E. Methodology

The research method that the writer uses in this thesis is explanative research. This research is aimed to give more detail explanation about the intervention of a certain country in international organization which in this case is in International Monetary Fund (IMF) that could give tremendous impact to the outcome of IMF's policy based on reality and some valid data. The writer collected the sources or references from books. In addition, a variety of data from the Internet were also used. Since some of the relevant information and thematic data are only available through online media, such as e-books, journals, electronic news, articles and other literatures.

The writer believes that the position of each country in every international organization specifically in IMF is the same which is as members. Thus, each country should have the same amount of rights and obligation in international organization. This can be said that intervention of a certain country in the process of international organization decision making is simply not ideal. In this thesis, the writer would like to investigate the case of Egypt as a debtor states in IMF from 1987 until 1991. The writer convinced that Egypt was not eligible to get loans from IMF since they could not fulfil the requirement in asking for loans and the United States was the main reason of why IMF finally approved the debt requested by Egypt.

F. Scope of Research

In this research, a politicization happened in this specific case is explained and examined. This undergraduate thesis mainly discusses about the reason of IMF final decision in giving financial assistance to Egypt in 1987-1991, while actually Egypt did not fully fulfill the debt request requirements.

G. Organization of Writing

This undergraduate thesis consists of five chapters and each chapter is described into several sub-Chapters.

CHAPTER I This chapter includes Background of the Research, Research Question, Theoretical Framework, Hypothesis, Methodology, Scope of Research, and Organization of Writing.

CHAPTER II Chapter II describes about International Monetary Fund (IMF) objectives, origin, and role in the global contribution.

CHAPTER III This chapter describes about Egypt economic crisis in 1987-1991. The main cause of crisis, and details about their inability to fulfill IMF requirements. This chapter also explain about IMF action in facing Egypt in 1987-1991.

CHAPTER IV This chapter analyzes the main topic of this undergraduate thesis which is the intervention of the United States behind the final IMF decision making process towards Egypt

financial assistance agreements in 1987-1991 using a related theory and concept.

CHAPTER V This chapter describes about the final result of the main problem of this topic and the conclusion.