HOW DOES CHINA CHALLENGE THE IMF’S POWER IN AFRICA?

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The Expert Group for Aid Studies - EBA - is a Government committee analysing and evaluating Swedish international development aid. This report can be downloaded free of charge at www.eba.se

Printed by Elanders Sverige AB
Stockholm 2016

Cover design by Julia Demchenko
Summary

How does China challenge the power of Western donors in Africa? This question has been raised by policy makers, scholars and pundits alike ever since the Chinese presence in Africa started to grow at the turn of the 21st century. However, few attempts have been made to explore this issue in a systematic way. This paper summarises a groundbreaking contribution in this regard, namely the PhD dissertation “When Chinese development finance met the IMF’s norms for public debt management in DR Congo” by Johanna Malm, defended at the Department of Social Sciences and Business at Roskilde University in Denmark in April 2016.

The dissertation addresses the subject matter by exploring how the commercial loans extended by China to African countries challenges the IMF’s power. The specific aspect of the IMF’s power that the dissertation focuses on is its power to set norms in terms of public debt management. This issue has been at the heart of the power relations between the IMF and African countries for decades, because public debt management is a key part of the conditions attached to IMF loans. It is therefore a pertinent issue to focus on when seeking to explore whether China challenges the power of Western donors in Africa. The dissertation’s main case study is the Democratic Republic of Congo (DRC), and the analysis draws on primary data gathered during a total of six months of qualitative field work in the DRC.

The dissertation shows that China’s commercial loans fundamentally alter the power dynamics of the international development finance arena, challenging the IMF’s power in African countries and beyond. The dissertation develops this argument through an empirical analysis in three steps.

First, the dissertation shows that the IMF and China’s financial institutions conceive of the relation between debt and development differently. The IMF’s public debt norm, embodied in its debt limits framework, posits that low-income countries should primarily take up concessional, low-cost loans, because reimbursement is made via the state budget and borrowing countries often have weak state revenues. In contrast, according to the Chinese public debt norm, low-income countries can take up commercial, expensive loans – if the reimbursement of the loans is secured by profitable commercial projects such as mines or hydroelectric plants, or by revenues from export of goods such as oil and cocoa.
The second step of the dissertation’s empirical analysis consists of a case study of one specific instance where a Chinese loan challenged the IMF’s power, namely the 2007-2009 controversy around the so-called Sicomines agreement in the DRC. The Sicomines agreement brought in a multibillion loan from China Exim Bank to finance infrastructure construction and a mining project in the DRC. The loan was extended on commercial terms, thus challenging the IMF’s debt limits framework. In 2009, the IMF managed to make the Congolese government downsize the Sicomines agreement to US$ 3 billion instead of the original value of around US$ 9 billion. However, drawing on interview data and contract analysis, the dissertation reveals that the IMF also manipulated its own assessment of the Chinese loan’s cost.

Specifically, the IMF portrayed the renegotiated version of the Chinese loan as a low-cost, concessional loan. However, as shown by calculations in the dissertation, it remains an expensive, commercial loan. The dissertation argues that the IMF made this silent compromise because the political and economic importance of the Chinese loan made it impossible for the IMF to ask the DRC to downsize the Chinese loan even further. This compromise was the only way for the IMF to help the DRC move forward in its debt relief process, which was blocked by the Chinese loan.

The third and final step in the dissertation’s empirical analysis entails minor case studies of Chinese challenges to the IMF’s public debt norm in Angola (2009) and Ghana (2011-2012), and of the formal revisions to the IMF’s debt limits framework in 2009. In all three cases, the dissertation identifies compromises on the side of the IMF similar to that made by the organisation in the DRC.

In conclusion, the dissertation argues that Chinese commercial loans do indeed challenge the IMF’s power in African countries. However, the dissertation also shows that the Chinese loans will only have this impact to the extent that they materialise. The loans are not rolled out as part of an attempt to challenge and altogether replace the IMF’s public debt norm. Rather, they are extended for commercial reasons, and only if Chinese companies and banks deem a specific commercial opportunity worthwhile. The dissertation shows that from 2010 onwards, Chinese commercial actors in the DRC have grown more prudent, and this seems to be the trend across the African continent. Thus,
even though Chinese loans do challenge the IMF’s power, fewer such challenges are likely to materialise in the future.

From a policy perspective, the dissertation highlights that the Chinese approach to development finance is a fully fledged alternative to the IMF’s approach. According to the Chinese perspective, external debt and FDI should be leveraged to develop commercial opportunities in the natural resources sector, thus maximising their developmental impact. The debt sustainability concerns often raised in relation to Chinese loans to African countries may be exaggerated, considering that Chinese banks are prudent and will only disburse loans that they are certain of recovering. The revisions made by the IMF to its debt limits framework in 2009 were certainly made for realpolitik reasons, but it also seems to be the case that IMF officials have adopted some of the Chinese thinking around debt and development. This represents a significant instance of norm change in Western development policy. However, while the Chinese loans have important developmental potential, this potential will only be realised fully if the host state steers the investments actively and ensures that the loans are used where they have the best impact.
1. Introduction

In September 2007, an agreement was signed in Kinshasa, capital of the DRC. The signatories were Pierre Lumbi, the Congolese Minister of Infrastructure, Public Works and Reconstruction, and Li Changjin, head of one of China’s biggest conglomerates, state-owned China Railway Engineering Corporation (CREC). The agreement sketched a financing arrangement which stipulated that a consortium of Chinese companies, led by CREC, would mobilise finance to capitalise a mining project and infrastructure projects of a public goods character such as roads, hospitals and schools in the DRC. Public goods infrastructure worth a maximum of US$ 6.5 billion would be financed (Protocole 2007).

The agreement also provided the consortium of Chinese companies with mining titles in the DRC’s mineral-rich, most south-easterly province, Katanga. The loan that would finance the infrastructure projects and the mining project was, the agreement stated, to be reimbursed by means of the profits generated by the mine (ibid.). The latter would be operated by a joint venture company, formed by the consortium of Chinese companies and a number of Congolese companies (Convention de Joint Venture 2007). The joint venture company was given the name *la Sino-Congolaise des Mines* - Sicomines.

The Sicomines agreement would enable the war-torn, resource-rich DRC to access significant funds for post-conflict reconstruction, while the consortium of Chinese companies would seal a good business deal. At first sight, this may seem like any other commercial transaction. In certain respects it was, but it was also extraordinary in structure and magnitude. The agreement immediately became the subject of an intense debate and stirred up controversy for a number of reasons. This dissertation focuses specifically on the element of the controversy that concerned public debt management. Namely, the credit line to be extended by means of the agreement was offered on commercial terms. Thus, it challenged the IMF’s debt limits framework.

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1 Katanga province was split up in 2015 and now consists of four provinces: Haut-Katanga, Haut-Lomami, Lualaba and Tanganyika. This dissertation uses the term ‘Katanga’, because the region carried this name during the time period under study.

2 The notion of ‘commercial terms’ here refers to non-concessional terms as per the IMF’s definition. As we shall see in chapter six of this dissertation, the terms of the Sicomines agreement’s infrastructure financing facility certainly remain more beneficial than the terms upon which a country with a sovereign credit rating as low as the DRC (B3 as rated by Moody’s (2013)) would be able to access purely commercial credit on the market.
This challenge was perceived as particularly problematic by the IMF and the Western donors at this time, because at this time, they were working to restart the IMF programme which would eventually enable the DRC to gain debt relief. The Sicomines agreement threw a spanner in the works of this process, because the DRC would not be allowed to start a new IMF programme if it was simultaneously contracting large amounts of non-concessional debt from a Chinese bank.

After more than a year of discussion and debate, the agreement was renegotiated in October 2009 to conform to the IMF’s requirements, and in July 2010 the DRC was subsequently granted $12.3 billion in debt relief. This paper, and the dissertation that it is based on, explores this controversy, seeking to shed light on the broader question of how China challenges the IMF’s power in Africa.

2. Background: the IMF’s power in Africa

Since the end of the Cold War, the power of the IMF, the World Bank and Western donors in Sub-Saharan African (henceforth ‘African’) countries has grown. This is a paradoxical development given that the paramount *leitmotif* for contemporary Western bi- and multilateral development assistance is that of ‘recipient ownership’. In the normative paradigm of ownership, policy conditionalities are no longer supposed to be defined and enforced by external donors, but shall be drawn from the recipient country’s own development policies (OECD 2008, p.20).

The idea of recipient ownership is the most important of the ‘partnership commitments’ laid down in the 2005 Paris Declaration. This declaration, together with the 2008 Accra Agenda for Action and the 2011 Busan Partnership Declaration, lays down the international norms3 that currently govern the provision of development assistance from Western donors (OECD 2008; Busan High-Level Forum 2011).

In existing scholarly literature, three main reasons are put forward as to why the power of the IMF, the World Bank and Western donors has grown in the ownership era. First, during the Cold War, the leaderships of African countries were, to a greater or lesser extent depending on the geostrategic importance of the country, able to balance the

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influence of Western donors by using the strategy of ‘switching’ – playing the Western donors and the Soviet regime off against each other to improve their chances of getting financial or military support. However, when the Cold War ended, the Soviet alternative disappeared and African countries could no longer use this strategy (Fraser 2009; Kragelund 2012; Plank 1993).

The second reason is that despite the rhetoric of ‘recipient ownership’ and ‘partnership’, recipient countries’ so-called ‘own development policies’ from which donor conditionalities are supposed to be drawn, most notably the Poverty Reduction Strategy Papers, are in actual fact drafted in donor-driven processes (Fraser 2005; Whitfield & Fraser 2009).

The third reason why the power of the IMF, the World Bank and Western donors has grown in the ownership era is the debt relief process that has been underway in many heavily indebted poor countries since 1996 (Whitfield & Fraser 2009; Woods 2008). The power that the IMF, the World Bank and Western donors have over a heavily indebted poor country is the most tangible just before debt relief is granted, because the country then has the most to lose from ignoring their policy prescriptions. Namely, in order to benefit from full and irrevocable debt relief, a country must adopt and implement a Poverty Reduction Strategy Paper, fulfil the conditions stipulated in the country’s IMF programme, and implement certain key reforms (IMF 2013b).

This is the backdrop against which the Chinese presence in African countries started to grow at the turn of the 21st century. Given that China is not a member of the OECD-DAC, scholars have suggested, or even hoped, that the Chinese presence may challenge the power of the IMF, the World Bank and Western donors in African countries (e.g. Harrison 2010; Tan-Mullins et al. 2010). In broad terms, this is the subject matter that the dissertation devotes attention to.

However, it is important to be precise in terms of the specific focus of the investigation. Harrison refers to China’s ‘indirect and direct investment in the form of credit and aid’ (2010, p.10); Tan-Mullins et al write about ‘aid from emerging donors’ (2010, p.859); and Whitfield and Fraser discuss Chinese ‘development finance’ (2009, p.97). However, development finance and aid are two different facets of the contemporary Chinese presence in African countries, and the ‘investment’ notion as used
by Harrison is misleading since credit and aid are not investment. Thus, it has to be clear which specific element of the power of the IMF, the World Bank and Western donors is being explored, and which facet of the Chinese presence in African countries that is in focus.

2.1. Problem formulation

The dissertation focuses on the power of the IMF, which is an influential organisation in African countries because of its gatekeeper role. Many of the programs of bi- and multilateral donors rely on the IMF’s assessment of a country’s commitment to reform or of its macroeconomic performance as conditions precedent to decisions on disbursement of loans or grants. The organisation’s assessments may also matter for the decisions of lenders from private capital markets. Thus, because of the ripple effects that the IMF’s assessments have in terms of the disbursement decisions taken by other donors, the IMF has a prominent position in African countries. (Evans 1999; Harrison 2010; Whitfield 2009; Bird 1996; Williams 2002; Buira 2003) This dissertation focuses specifically on the aspect of the IMF’s power that regards its power to set norms.

In order to identify a specific element of the norms governing development cooperation on which to focus the investigation, Brautigam’s (2010, pp.11–17) classification of the existing normative frameworks within the international aid architecture is helpful. She identifies five areas for which clear normative frameworks can be discerned: transparency; tied aid and export credits; social and environmental protections; corruption and governance, and the management of debt.

This dissertation focuses on the latter, because it has been at the heart of the political tug-of-war between African countries and the IMF, the World Bank and Western donors for decades. Specifically, public debt management has formed part of the conditions attached to IMF loans ever since that organisation started to practice conditionality in 1952 (Buira 2003). Public debt management is therefore a pertinent issue to focus on in order to shed light on the broader query of whether China challenges the IMF’s power in Africa.

The IMF’s debt limits framework lays down the organisation’s public debt norm. This framework is central to the IMF programmes that countries have to follow in order to
benefit from the organisation’s support and gain debt relief. It establishes limits for – or even prohibits, depending on the country’s debt vulnerability – new loans on commercial terms. Permitted loans are those which are extended with low enough interest rates, long enough grace period, and long enough total repayment period. The IMF terms such permitted loans ‘concessional’, meaning that they are extended at low enough a cost for the borrower. The IMF uses the term ‘grant element’ to express the level of concessionality of a loan. (IMF 2013a)

The Chinese presence in African countries is a multifaceted phenomenon. It comprises numerous facets, including development aid and a variety of commercial activities, some backed by the Chinese government, others not (e.g. Jansson 2012). The only element of the Chinese presence in African countries that challenges the IMF’s power to set norms in terms of public debt management are the loans proposed on commercial terms to those countries. These credit lines, a facet of the Chinese presence in African countries that is backed by the Chinese government, come about as follows.

Beijing’s ambitions in terms of the internationalisation of the Chinese state-owned enterprises (SOE) were initially formulated in the ‘Going Global’ strategy in 2001 (zouchuqu, literally meaning ‘walk out’). The strategy encouraged the SOEs to expand overseas, capture market share and gain experience, particularly with regards to energy (Brautigam 2009; Zha & Hu 2007). To encourage this, the Chinese government can provide the SOEs with credit lines that facilitate their business development. In the case of Chinese companies developing their portfolios in African countries, such support is provided mostly by the state-owned policy bank China Export-Import (Exim) Bank and by China Development Bank, the former policy bank that was nominally commercialised in 2008 (Downs 2011; Xu 2008). Such credit lines are extended to the SOEs at market rates, on commercial terms.

On several occasions since 2000, such credit lines have been extended on commercial terms to African countries. The often large-size loans have mostly been used to finance infrastructure of a public goods character. The reimbursement of the credit lines has been linked either to the profits from a commercial venture involving an SOE, or to revenues from the debtor country’s natural resource exports. Examples of such credit lines include
those extended to Angola, Ghana and the DRC. (Brautigam 2009; Corkin 2011) As mentioned, this dissertation focuses on the case of the DRC.

These credit lines have often been wrongly understood as Chinese development aid: they are not. Certainly, the Chinese development aid portfolio does include credit lines, but they are extended on concessional terms since the interest rates for those loans are subsidised by the aid budget (Brautigam 2009). The concessional credit lines play an important role in strengthening bilateral relations between China and the beneficiary country, diplomatic ties which are important preconditions for the commercial loans to materialise.

The subsidised, concessional credit lines do not challenge the IMF’s public debt norm. By contrast, the Chinese loans extended on commercial terms challenge the said norm, because they do not qualify as concessional as per the IMF’s grant element requirements. Thus, in order to investigate whether China impacts on the IMF’s power to set norms in terms of public debt management in African countries, the dissertation focuses on the latter category of credit lines: the commercial development finance offers. The main research question guiding the dissertation’s research endeavour is:

- To what extent, how and why do Chinese commercial development finance offers impact on the IMF’s power to set norms in terms of public debt management in African countries?

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4 It is important to note that in empirical terms, the relation between ‘China’ and the ‘IMF’ is by no means dichotomous. China is the IMF’s sixth largest member country and an important part of China’s foreign policy ambition is to be a responsible international actor and contribute actively to the work of the IMF and the World Bank (Chin & Thakur 2010; IMF 2014). However, as chapter five of the dissertation shows, there is a tension in Chinese foreign policy making processes between these ambitions and the market-driven considerations that underpin the provision of commercial credit lines to African countries.
3. Empirical analysis

The dissertation generates insights in terms of the research question by means of an empirical analysis in three steps, each of which is summarised below. The empirical analysis draws on a wide range of primary and secondary sources. References to these are not included in the brief summary below, but can be found in the dissertation document (Malm 2016, chapters 4-7, pp. 84-163).

3.1. The IMF’s power to set norms and China’s power to challenge it

First, the dissertation establishes a baseline from which the investigation departs. It does this by ascertaining whether the IMF had the power to set norms in terms of public debt management in the DRC in 2007 when the Sicomines agreement was signed, and if yes, what it was that underpinned that power. The dissertation’s general starting point is that the IMF has such power when the material clout of the organisation’s largest stakeholders outweighs the material capabilities of borrowing countries. The dissertation finds that the IMF was in a powerful position in the DRC in 2007 when the Sicomines agreement was signed, given the DRC’s need for debt relief, budget support and post-conflict reconstruction, and considering the IMF’s position as a lender of last resort and a gatekeeper for both debt relief and development finance.

The dissertation subsequently explores what it is that constitutes China’s power to challenge the IMF’s public debt norm. It starts out by showing that Chinese commercial loans, such as that extended by means of the Sicomines agreement, challenge the IMF’s public debt norm because they have lower grant elements than the loans deemed concessional within the IMF’s debt limits framework. Chinese commercial loans have lower grant elements because they have higher interest rates, shorter grace periods and shorter total repayment periods than concessional loans.

The dissertation then analyses the Chinese foreign policy making process, focusing specifically on China Exim Bank, which is conceived of as a norm entrepreneur. Through its President Li Ruogu, China Exim Bank promotes a Chinese public debt norm, a project-based approach to debt sustainability. This norm, embodied by the Sicomines agreement, is anchored in the commercial ambitions that increasingly characterises Chinese foreign policy ambitions.
The dissertation finds that China Exim Bank’s ability to successfully promote the Chinese public debt norm hinges on the financial clout of the Chinese state, which in turn derives from the economic growth and trade surplus brought about by the past decades’ changes in the organisation of production in China. The Chinese development finance offers which embody the Chinese public debt norm are able to challenge the IMF’s public debt norm because China’s financial clout outweighs that of the most influential states on the IMF’s board. Thus, when a Chinese commercial loan is extended to an African country, the material basis of the IMF’s power in that country is challenged.

3.2. The IMF’s reaction to the Chinese norm challenge

The second step of the empirical analysis is to explore one specific instance where a Chinese loan challenged the IMF’s power, namely the controversy around the Sicomines agreement in the DRC. The dissertation shows that the IMF was able to deploy norm-enforcing power and coerce the DRC into renegotiating the agreement according to the IMF’s requirements because of the DRC’s need for debt relief, budget support and post-conflict reconstruction.

However, drawing on contract analysis and interview data, the dissertation also reveals that the IMF made a ‘silent compromise’ to counter the Chinese norm challenge. Specifically, the organisation compromised its debt limits framework, conducting a grant element calculation so generous that the credit line to be extended by means of the Sicomines agreement was portrayed as highly concessional, which it is not.

The IMF did this because at this point in time, neither that organisation nor the Western donors could mobilise funds for post-conflict reconstruction in the DRC of the magnitude that the Sicomines agreement would bring in. The financial clout that underpinned the Chinese norm challenge was thus greater than that of the IMF and the most influential countries on its board, and this set political limits to the revisions that the IMF and the Western donors could coerce the DRC into making. Knowledge manipulation thus became the most appropriate strategy for shoehorning the Sicomines agreement into the debt relief process.
3.3. The Chinese challenge in Angola and Ghana, and the IMF’s norm change

The third and final step in the empirical analysis comprises of three minor comparative case studies. First, the dissertation considers challenges posed by Chinese commercial loans to the IMF’s public debt norm in Angola (2009) and Ghana (2011-2012). In both cases, the dissertation identifies compromises on the side of the IMF similar to that made by the organisation in the DRC. Namely, the IMF applied its debt limits framework in a generous way, allowing both Angola and Ghana to take up Chinese commercial loans which normally would not have been accepted within the framework of their IMF programmes.

Secondly, the dissertation analyses the formal revisions made by the IMF to its debt limits framework in December 2009. The revised framework is above all characterised by flexibility. It allows countries with low macroeconomic- and public financial management capacity and high debt vulnerability to borrow on commercial terms to a greater extent than they were previously allowed to do within the framework of their IMF programmes. The IMF notes that in the new dispensation, these countries should take up commercial loans only in exceptional cases, but the organisation does not define in more depth what this means.

The dissertation argues that this imprecision was deliberately integrated into the revised debt limits framework in order to avoid the situation faced by the IMF in the DRC during the Sicomines controversy, where the grant element limit was fixed and the organisation had to engage in knowledge manipulation in order to accommodate the politically significant Chinese credit line.

However, the dissertation argues that the IMF still seeks to set norms in terms of public debt management to the greatest extent possible, and will only compromise its public debt norm if it is faced with a specific challenge. In other words, the IMF does not make compromises to its public debt norm unless a competing public debt norm with a more significant material basis emerges, such the Chinese public debt norm embodied by a Chinese commercial loan.

In this context, the 2009 revisions to the IMF’s public debt norm were ingenious because they enabled the IMF to temporarily allow for a country to take up more commercial debt within the framework of its IMF programme. In this way, the IMF’s
public debt norm can retain political relevance even when a Chinese commercial loan is extended to an African country, thus enabling the IMF to keep a seat at the table and avoid losing face. However, if no such Chinese loans are extended, the IMF can set norms in terms of public debt management in a similar vein as it did prior to China’s emergence as a development finance provider.

4. Conclusion

China’s commercial loans fundamentally alter the power dynamics of the development finance arena. For decades, the IMF has been able to use its power as a gatekeeper and a lender of last resort to set norms in African countries, but this dissertation shows that China challenges this power. In order to summarise the results of the dissertation, we shall return to the research question:

- To what extent, how and why do Chinese commercial development finance offers impact on the IMF’s power to set norms in terms of public debt management in African countries?

This question comprises three sub-queries: ‘to what extent’, ‘how’ and ‘why’. In terms of the ‘how’ aspect, the dissertation shows that Chinese commercial loans impact on the IMF’s power in African countries by challenging the material base for that power, namely its role as a lender of last resort and a gatekeeper for public and private financial inflows.

In terms of China’s rationale for challenging the IMF’s public debt norm – the ‘why’ aspect of the research question – the dissertation argues that there are both material and normative reasons to it. In terms of normative considerations, the Chinese public debt norm is truly seen by many stakeholders in China’s financial institutions as a more appropriate approach to public debt management for developing countries. In terms of material considerations, the more permissive approach to using loans on commercial terms to finance Chinese business ventures in African countries serves the interests of a number of actors: the Chinese state, China’s banks, Chinese corporations, and those Chinese workers who can find employment by means of the business ventures that the banks finance.

The third and final aspect of the dissertation’s research question concerns ‘to what extent’ Chinese commercial loans impact on the IMF’s power in African countries. In
this regard, the conclusion is that Chinese commercial loans impact crucially on the IMF’s power in African countries, but the loans will only have this impact to the extent that they materialise. While the Chinese commercial loans embody the Chinese public debt norm promoted by China Exim Bank and other Chinese financial institutions, these offers are not rolled out as part of an attempt to challenge and altogether replace the IMF’s public debt norm in African countries. It is not a Chinese foreign policy priority to mount such a norm challenge. Rather, those loans are extended for commercial reasons, when the Chinese financiers and SOEs deem a specific commercial opportunity worthwhile.

This dissertation opens up two main avenues for further research. First, the dissertation’s case study of the challenge posed by the Sicomines agreement to the IMF’s public debt norm in the DRC could be replicated in other countries. Such case studies could verify the dissertation’s conclusions and deepen our understanding of how Chinese commercial loans challenge the IMF’s power. From this dissertation’s perspective, in-depth engagement with the two cases that were only explored briefly here, Angola and Ghana, would be of great value. Case studies of other African, Asian and Latin American countries that have experienced controversies with the IMF over Chinese commercial loans would also make valuable contributions to this emerging literature.

Second, a thorough process tracing endeavour around the 2009 revisions to the IMF’s debt limits framework could nuance and deepen the argument developed in this dissertation. Such a study could devote attention to matters such as who the key actors were during this process, what their considerations were, and to what extent the Chinese Executive Director’s office at the IMF was involved in this process. Such a case study could also delve into the theoretical tension between on the one hand the constructivist claim that it is the staff and their ideas and agency that determine the actions of the IMF, and on the other hand the Coxian tenet that IMF is a mechanism of hegemony whose power hinges on the material capabilities of the hegemonic state and the other countries with large stakes in the organisation.
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