House Committee on Financial Services

Hearing Entitled: “Examining Policies to Counter China”

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Witness Statement

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Introduction

Mr. Chairman, Ranking Member Waters, and Members of the Committee, thank you for inviting me as a witness to today’s hearing.

My name is Martin Mühleisen. Before joining the Atlantic Council’s GeoEconomics Center as a Nonresident Senior Fellow, I retired from the International Monetary Fund (IMF) in 2021. I was Chief of Staff under Managing Director Christine Lagarde, and I served as Director for Strategy, Policy and Review between 2017 and 2020. The following are my personal views, not those of the Atlantic Council.

Multilateral financial institutions

International Financial Institutions (IFIs), such as the IMF, the World Bank, and regional Multilateral Development Banks (MDBs), have been important tools for the United States to exert its global leadership. Unlike the United Nations with its “one country, one vote” system, these institutions are shareholder-owned, and voting power is determined by shareholdings. The United States, in almost every circumstance, owns the largest share and, especially in the case of the IMF and World Bank, is the only country that holds a veto over changes to the institutions’ fundamental governance arrangements and lending capacity.

The institutions are chartered for specific, narrow purposes. The World Bank and MDBs borrow in global capital markets to finance economic development in emerging and developing countries. The IMF’s mandate, financed by issuing reserve assets to its member countries, is to preserve global economic stability by addressing external imbalances and serving as a lender of last resort to prevent balance of payments crises.

China’s role in the IFIs

The People’s Republic of China assumed China’s seat at the IMF and World Bank in 1980, and it joined other MDBs over the course of the following decades. It has broadly supported the mandates of these institutions and, like many other shareholders, contributed

supplementary resources to help fund training, technical assistance, or interest rate subsidies for the poorest countries.

As China's economy has grown to rival that of the United States, its voting share in the IMF and World Bank has not risen accordingly. Relative to its size, China is now significantly underrepresented in these institutions, along with a number of other emerging markets. This has been the subject of intense debates about IFI governance arrangements in recent years. Nevertheless, China joined a broad consensus last year to increase the IMF's capital ("quotas") without any realignment of voting shares.

China As a Sovereign Lender

As it grew in size, China has also become the largest sovereign lender to emerging and developing countries over the past two decades, spurred on by President Xi's Belt-Road Initiative (BRI) that started in 2013. China's lending volume since 2000 is estimated at $1.3 trillion, approaching the total amount provided by the G7 over the same period.[1] More recently, the People's Bank of China has also acted as a lender of last resort, offering about $600 billion worth of bilateral renminbi swap lines to some 30 countries.[2]

China did not grown its loan portfolio out of altruistic motives. It has used its creditor relationships with emerging markets and developing countries to export construction and other services; to obtain access to naturals resources, ports, and other facilities; and to attract diplomatic support for its geopolitical objectives. For example, about 70 countries, many of them in the Western Hemisphere, have officially endorsed China's sovereignty over Taiwan.[3]

What This Committee Could Encourage

Hold China responsible for bad lending decisions

As a large and relatively new international lender, China has repeated many of the mistakes of other countries that went before it, including in the design of its lending programs and in the way that it manages relations with distressed borrowers.

BRI loans and the associated projects have been plagued by quality problems, lack of transparency, and quasi-commercial financial terms. Many loans have become distressed as a result, contributing to rising debt vulnerabilities in low-income countries. [4] In a number

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[1]Gregory Makoff, Théo Maret, Logan Wright, "Sovereign Debt Restructuring with China at the Table: Forward Progress but Lost Decade Risk Remains," Harvard Kennedy School, January 27, 2025.
[2] International Monetary Fund, *External Sector Report: Imbalances Receding*, July 2024.
[3] The Economist, "China's stunning new campaign to turn the world against Taiwan," February 9, 2025.
[4] International Monetary Fund, "Debt Vulnerabilities And Financing Challenges In Emerging Markets And Developing Economies—An Overview Of Key Data," IMF Policy Paper 2025/002, February 20, 2025.

of cases, this has put an effective stop to lending by multilateral lenders, who cannot lend to countries with an unsustainable debt burden.

A number of borrowers have remained in limbo for several years because China refused to participate in collective debt restructuring exercises, preferring instead to bilaterally extend maturities or modify interest rates rather than providing comprehensive debt relief.

Since China has joined the G20 Common Framework for Debt Restructuring in 20200, the speed of debt workouts has picked up somewhat. Nevertheless, there is still a lack of coordination among China's state lenders, and there is a fundamental unwillingness to agree to loan write-downs that are sometimes necessary to restore countries' solvency (not unlike under Chapter 11 of the U.S. Bankruptcy Code), resulting in long workout periods that put an undue burden on debtor countries and other lenders.[5]

The United States should use its voice in the IMF to adopt a more forward-leaning approach when it comes to the restructuring of Chinese loans. Besides insisting on improved transparency, the U.S. Treasury should encourage the IMF to adopt a more forceful approach in cases where China's reluctance to engage in meaningful restructuring effectively grants it a hold over IMF program loans.

For example, the IMF's "Lending into Official Arrears" (LIOA) policy allows the institution to resume lending to borrower countries that are in default to one of its members, provided they engage in good faith negotiations and other loan conditions are met.[6] At the moment, the burden on countries to benefit from this policy is relatively high, given the risks for them to default on one of their largest lenders and trading partners. A more robust application of the LIOA policy, however, could strengthen the negotiation position of debtor countries and provide for more ambitious debt relief from China.[7]

Focus on quality, not quantity, of IFI programs

Following the Covid epidemic, and in order to help countries respond to global climate, food, and energy crises in recent years, the World Bank and MDBs have been looking to leverage their capital base to step up climate and development loans, including with private capital, and the IMF issued $650 billion of Special Drawing Rights (SDRs) to its membership in 2021 to boost global liquidity. At the same time, the fund has channeled some of the newly created SDRs of its richer members into its concessional loan programs.

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[5] Makoff, Maret, and Wright (2025), op.cit.

[6] International Monetary Fund, "Reviews of the Fund's Sovereign Arrears Policies and Perimeter," IMF Policy Paper 2022/023, May 18, 2022.

[7] Sean Hagan, "The IMF's arrears lending policy: Just Use It", FT Alphaville blog, September 29, 2022.

These efforts were intended to meet emergency financing needs of poorer countries, often involving little or relatively weak conditionality. There is a risk, however, that an increase in debt owed to multilateral institutions, who enjoy preferred creditor status, could worsen the overall debt situation of recipient countries as it may drive away private creditors. Moreover, the increase in global interest rates from the zero rate-environment a few years ago also implies that programs and projects need to meet a higher standard to help countries escape from debt distress.

To attract private capital and decrease their reliance on Chinese lenders, recipient countries need to improve their long-term growth prospects, which should be reinforced through strong loan conditionality focused on improving legal systems, streamlining regulations, and limiting government involvement in the economy, among others.

At the IMF, the United States should insist on prioritizing "upper-credit tranche" (UCT) programs, where a country must undertake necessary economic reforms to qualify for disbursements. At the World Bank, this could involve some rebalancing of its focus on global public goods toward more ambitious growth objectives.

Given the still strong demographics in Africa and Southeast Asia, investing in these regions will open up market opportunities for U.S. exporters in the future. However, stepped-up lending by multilateral organizations alone will not be enough to win the struggle for hearts and minds in the Global South.

The United States and other large shareholders should therefore work with multilateral lenders to incentivize critical reforms and boost growth prospects in partner countries. If multilateral programs were flanked by bilateral co-financing, investment finance, specific trade preferences, or other forms of (geopolitical) incentives, they would have a larger chance to succeed.[8]

Protect the dominant role of the dollar

I have so far focused mostly on low income and developing economies, in part because large emerging market (EM) countries exhibited a remarkable degree of macroeconomic stability in recent years. Many EMs tightened monetary policy early in 2021 in the face of inflationary pressures, and they were able to relax policies quickly after the shock receded.

In most cases, there was no need for full-fledged IMF/World Bank programs during this period, as there has not been for several years, although some countries in the Western

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[8] Martin Mühleisen, *The Bretton Woods Institutions Under Geopolitical Fragmentation*, Atlantic Council, October 9, 2023.

Hemisphere made good use of the precautionary credit lines offered to IMF member countries with high-quality policies and a strong economic track record.

Two factors contributed to this positive outcome. First, many EMs acquired large foreign exchange reserves in the wake of the Asia and Global Financial Crises, making them more immune to speculative attacks; and second, countries pursued orthodox macroeconomic policies, with a focus on strong institutions, responsible fiscal policy, and flexible exchange rate management.

In principle, however, many EMs are still vulnerable to external shocks, especially under a combination of financial market volatility and rising tariffs and trade barriers. Most are not benefiting from dollar swap lines offered by the Federal Reserve, nor are they members of powerful regional currency arrangements.[9] In case of a severe crisis, these countries would need access to U.S. dollar sources to supplement their own reserves in order to avoid sharp currency devaluations.

In this case, the IMF could deploy its lending capacity of around $1 trillion to stabilize countries' balance of payments, avoid wider contagion, and thereby preserve global financial stability. These funds are available through IMF programs or precautionary lines at relatively short notice, leveraging the United States' financial contribution to the IMF by a factor of more than 5:1.

Absent the safety net provided by multilateral institutions, countries would only have two viable alternative to protect themselves against larger shocks. They would either have to acquire additional foreign exchange reserves, putting upward pressure on the U.S. dollar, or they would need to seek help from China with its large currency reserves, which could in the long run be a factor in undermining the dominant role of the U.S. dollar.

It would therefore be in the U.S. interest if Congress were to ratify the IMF quota increase agreed last year, shifting a good part of the funds already contributed to the IMF's New Arrangements to Borrowing fully into its permanent capital.

A final word

When talking about the multilateral institutions, the focus usually lies on their finances and program activities. What is often overlooked is that these institutions are at the center of a worldwide network of country officials, financial market participants, and policy experts who are committed to market-based economics, global trade, free capital flows and responsible macroeconomic policies.

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[9] In South-East Asia, the Chiang Mai Initiative (CMIM) provides for some regional support, but this is largely tied to IMF programs.

It is therefore no accident that emerging markets have become more stable in recent years. While this is an achievement on the part of each individual country, in many cases it has been spearheaded by officials that spent some years during their career working at multilateral institutions and/or continuing to benefit from close interaction with them. The transmission of knowledge through these contacts, as well as the large amount of technical assistance and training provided by multilateral institutions, are a public good that benefits the United States in many ways, and is unlike anything that China has to offer.