

International Monetary Fund - IMF

[UPSC Notes]

When was IMF Established?

The IMF was founded at a UN conference in Bretton Woods, New Hampshire, United States, in July 1944. The International Monetary Fund (IMF) was established on 27th December 1945 with 29 member countries with the objectives of boosting economic growth and eradicating poverty across the world.

IMF: Member Countries

Initially, there were 29 members of the International Monetary Fund (IMF) including India as the founding member. At present, the organization has 190 members that govern the IMF, also known as the 'Fund'.

The Principality of Andorra is the 190th member of the IMF.

Objectives of IMF

The IMF is regarded as a key organization in the international economic system which focuses on rebuilding the international capital along with maximizing the national economic sovereignty and human welfare. The IMF was founded in response to the Great Depression with the goals of boosting international economic cooperation, increasing employment generation, gaining financial stability, alleviating poverty around the world, and reorganizing the global payment system.

Some of the major objectives of the International Monetary Fund (IMF) are discussed below:

- **Global Monetary Cooperation:** One of the major objectives of the IMF is to promote international monetary cooperation with the support of the members.
- **Financial Stability:** IMF aims to secure financial stability by eliminating or minimizing the risks of exchange rate fluctuations.
- **Employment:** The objective of the IMF is to promote employment generation through economic assistance and sustainable growth.
- **International trade:** It aims to facilitate a balanced international trade.
- **Poverty:** Eradication of poverty across the world is one of the primary objectives of the IMF.

Functions of IMF

The functions of the International Monetary Fund (IMF) are categorized into three major types:

Surveillance Function:

- The primary function of the IMF is to monitor the international monetary system along with the economic and financial policies of the 190 member countries. This surveillance process happens at regional, global, and country levels.
- The International Monetary Fund (IMF) analyzes stability and growth risks and suggests and assists the countries in essential policy adjustments for sustainable economic growth and financial and economic stability.

Financial Function:

- Economic crises can arise anytime in any form. It can be a balance of payment crisis, high fiscal deficits or debts, etc.
- The International monetary fund provides financial assistance to the countries that are hit by the crisis and help them to restore the economic stability in the country.
- It also provides precautionary financial advice to the members to prevent and get prepared for the crisis.

Technical or Capacity Development Function:

- The International Monetary Fund also provides training and capacity development assistance to the central banks, tax authorities, finance ministers, and economic institutions of the member countries.
- These efforts help the countries to achieve the objectives of sustainable growth and development.
- The capacity development efforts of the IMF focus mainly on the following parameters:
 - **Public Finance:**
 - IMF guides the countries on the better mobilization of revenues and effective management of expenditure by using fiscal instruments such as tax & custom duties, budget management, public finance, debt management, etc.
 - The training helps the countries to improve the infrastructure of the country such as better schools, hospitals, roads, etc, attract foreign direct investments, ensure fiscal health, foster transparency, mitigate the risk of climate change, and reduce the risks of exchange rate fluctuations, etc.
 - **Monetary and Financial Policies:**
 - The IMF works with the central banks of the countries on modernizing the monetary and financial policies so that they can cope with the crisis.
 - Recently, the IMF has also started providing capacity development on cyber-risk and fintech.
 - **Legal Framework:**
 - The IMF also guides the countries to align their legal and governance framework with the international standards to support financial reforms, address the issues of money laundering and black money, etc.
 - **Statistics:**

- It also helps the countries in the compilation, management, and analysis of the financial and macroeconomic data.
- This helps the countries to better understand the economy and formulate more effective economic policies that can cater to the needs of the economy.

What are the IMF Quotas?

When the country joins the International Monetary Fund (IMF), it is assigned a quota based on the economic size of the country in relation to the global economy and the existing member countries. Quotas are provided in the denominations of the Special Drawing Rights (SDRs).

The review of these quotas is conducted usually after every five years through which the IMF looks at the adequacy of quotas according to the needs of the member countries for liquidity and financial stability. The quota of the member countries determines the voting power of each member and its access to IMF financing. 250 basic votes are provided to each member plus one additional vote for each SDR 100,000 quota.

India holds the position of eighth-highest quota-holding member of the IMF.

Executive Board and Board of Members of IMF

The Board of Governors is the highest decision-making body of the IMF. It consists of one governor and one alternate governor for each member country. The governor is appointed by the member country and is usually the minister of finance or the head of the central bank. The Board of Governors is advised by two ministerial committees, the International Monetary and Financial Committee (IMFC) and the Development Committee.

The Board of Governors have delegated most of their powers to the IMF's Executive Board but retains the right to approve quota, special drawing right (SDR) allocations, the admittance of new members, compulsory withdrawal of members, and amendments to the Articles of Agreement and By-Laws.

The Executive Board of the IMF is a 24-member Board elected by the Board of Governors. It conducts the daily business of the IMF and exercises the powers delegated to it by the Board of Governors & powers conferred on it by the Articles of Agreement. The Board normally makes decisions based on consensus, but sometimes formal votes are taken.

Special Drawing Rights (SDR) of IMF

The Special Drawing Right (SDR) is an interest-bearing international reserve asset created by the IMF in 1969 to supplement other reserve assets of member countries. The SDR is based on a basket of international currencies comprising the U.S. dollar, Japanese yen, euro, pound sterling and Chinese Renminbi.

The currency value of the SDR is determined by summing the values in U.S. dollars, based on market exchange rates, of an SDR basket of currencies. The SDR basket is reviewed every five years.

The SDR is not a currency. It is a potential claim on the freely usable currencies of IMF members. As such, SDRs can provide a country with liquidity. SDRs are only allocated to IMF

members that elect to participate in the SDR Department. Currently, all members of the IMF are participants in the SDR Department.

India's current quota in the IMF is SDR (Special Drawing Rights) 5,821.5 million, making it the 13th largest quota holding country at IMF and giving it shareholdings of 2.44%.

IMF: Criticism of the Organization

The criticism of IMF is widely publicized as they are more, outnumbering the success of the organization in recent years. The main areas of criticism are:

- Conditions placed on loans are too intrusive and compromise the economic and political sovereignty of the receiving countries.
- IMF imposes the policies on countries without understanding the distinct characteristics of the respective country.
- The organization allows for inflationary devaluations
- The IMF policies are imposed all at once, rather than in an appropriate sequence.

IMF and India

India is a founding member of the IMF. India had a serious balance of payments deficit, particularly with the dollar and other hard currency countries post-partition. IMF came to the rescue. The IMF Fund granted India loans to meet the financial difficulties arising out of the Indo-Pak conflict of 1965 and 1971. Since 1970, the assistance that India can obtain from IMF has been increased through the setting up of the Special Drawing Rights.

India has also availed of the services of specialists of the IMF for the purpose of assessing the state of the Indian economy. India has occupied a special place on the Board of Directors of the Fund. The country plays a creditable role in determining the policies of the IMF Fund.

India has not taken any financial assistance from the IMF since 1993, and the repayments of all the loans taken from the International Monetary Fund were completed on 31 May 2000.

The Finance Minister of India is the ex-officio Governor on the Board of Governors of the IMF. RBI Governor is the Alternate Governor at the IMF.

IMF: Recent News

- The World Economic Outlook 2022 by IMF has been published and cut its forecast for India's Gross Domestic Product (GDP) growth in FY 2022-23 to 8.2%, making it the fastest-growing major economy in the world.
- The International Monetary Fund (IMF) increased the weighting of the US dollar and Chinese yuan (Renminbi) in the Special Drawing Rights (SDR) basket of currencies. The updated weightings will be effective from August 1st.