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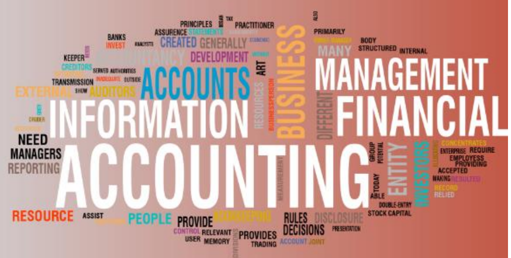
Subject: Management



Production of Courseware

e-Content for Post Graduate Courses

Paper: 08, International Business Operations

Module: 13, Objectives and Functions of IMF

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Items	Description of Module
Subject Name	Management
Paper Name	International Business Operations
Module Title	Objectives and Functions of IMF
Module Id	Module no.13
Pre- Requisites	Basic knowledge International Business Environment
Objectives	To study the basic concepts of functions and objectives of IMF
Keywords	International Monetary Fund

QUADRANT-I

	Module 1: Objectives and Functions of IMF
1.	Learning Outcome
2.	Introduction
3.	History of IMF
4.	Governance and organization of IMF
5.	Working of IMF
6.	The major functions of IMF
7.	SDRs
8.	Summary

1. Learning Outcome:

After completing this module the students will be able to:

- The History and Purpose/ objectives of the IMF.
- Working and Functions of IMF.
- Knowing the IMF's current role

2. Introduction

The great depression of 1930's resulted in the downfall of various economies. Less availability of foreign exchange with the economies was a major issue to be tackled to sustain the economic systems. Therefore most of the economies increased trade barriers and devalued their currencies in order to compete in the export markets. The repercussions of all such measures were increasing unemployment, deteriorating standard of living of people, decline in world trade and slowing down of the economies as a whole.

Therefore in 1944 under an agreement; International Monetary Fund was created to reach upon a framework which could promote economic cooperation there by leading to a prosperous global economy. In this module you will be able to understand that why and how the IMF was created and what are the basic functions which IMF performs to promote/foster and establish economic cooperation in world economies.

3. History of IMF

International Monetary fund is also called as Bretton Woods Institutions. The basic objective behind the creation of IMF was to support the economic and financial system of world economy. After the great depression of 1930's various economies of the world increased trade barriers thereby a huge fall in the world trade was seen. Various economies resorted to devaluation of their currency also to sustain. To boost and support the economies to increase their world trade an agreement which is famously known as Bretton Woods agreement was entered into with various nations.

The IMF was conceived at a United Nations conference which was convened in Bretton Woods, New Hampshire, United States, in July 1944. The governments of 44 countries at the Bretton Woods conference unanimously represented on a fact that a framework should be established at a world level so that the economies do not get trapped in a vicious circle of devaluation of their currencies due to depression in economies. All agreed to support and increase economic co-operations in order to boost world trade, dipping living standard of people leading to dropping of the world trade to a great extent. In 1944 at Bretton Woods an agreement was done to establish a new international monetary system.

The basic objective to establish IMF was to-

1. Promote/ foster International Financial Stability and
2. To extend and encourage Monetary cooperation among nations

These two objectives were established with a vision to promote, contribute, encourage and achieve the following-

a. Increased International trade
b. High level of Employment opportunities in countries
c. Achieve sustainable economic growth
d. Reduce the level of poverty worldwide
e. Reduced trade barriers

Finally IMF was created in 1945. Presently the IMF is governed by and is accountable to the 188 countries that make up global membership.

Therefore we can say that IMF is an international organisation with a membership of 188 countries which helps in fostering monetary cooperation, achieve financial stability and facilitate international trade to achieve its various objectives. Formally it started in 1945 with 29 countries. Its headquarters are in Washington DC.

According to the official website of IMF (www.imf.org), "The International Monetary Fund (IMF) is an organization of 188 countries, working to foster global monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth, and reduce poverty around the world. Created in 1945, the IMF is governed by and accountable to the 188 countries that make up its near-global membership."

4. Governance and organization of IMF: (As given on official website of IMF)

The IMF is responsible to the governments of its member nations. At the top of its organizational structure is the Board of Governors, which consists of one Governor and one Alternate Governor from each member country. The Board of Governors meets once each year at the IMF-World Bank Annual Meetings. Twenty-four of the Governors sit on the International Monetary and Financial Committee (IMFC) and normally meet twice each year.

The day-to-day work is overseen by its 24-member Executive Board, which represents the entire membership; this work is guided by the IMFC and supported by the IMF staff. The Managing Director is the head of the IMF staff and Chairman of the Executive Board and is assisted by four Deputy Managing Directors.

The Board of Governors, the highest decision-making body of the IMF, 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 governor of the central bank. All powers of the IMF are vested in the Board of Governors. The Board of Governors may delegate to the Executive Board all except certain reserved powers. The Board of Governors normally meets once a year.

4.1 The responsibilities of IMF

4.1.1 According to the Charter of IMF, “The IMF's primary purpose is to ensure the stability of the international monetary system—the system of exchange rates and international payments that enables countries (and their citizens) to transact with each other.”

5. Working of IMF

All the countries who are the members of IMF create a pool of funds by a quota system as a fund of IMF. Those countries which have deficit in payments can borrow from that fund. IMF helps to improve the status of member economies by carrying out several activities pertaining to research, development.

So the primary source of the IMF's financial resources is its members’ quotas. These quotas are based on the members’ relative position in the world economy. In addition, the IMF can borrow temporarily to supplement its quota resources. IMF has also created “The New Arrangements to Borrow (NAB)”, which was expanded in 2011 and can provide supplementary resources. The member countries of IMF have also agreed recently to increase the resources through borrowing agreements.

As per the articles of agreement of IMF its objectives are-

“to promote international economic cooperation, international, employment, and exchange-rate stability, including by making financial resources available to member countries to meet balance-of-payments needs.”

The IMF is the vital organization of the international monetary system. It is not a development agency. It acts as a source of last resort for the member economies in order to gain short term stability.

6. The major functions of IMF

With the advancement of the technology the world shifted from the industrial era to information era. The need of information flow for the success of business is as the flow of blood for the life.

The importance of the communication in the business can be understood after analysing the following points:

6.1 The Surveillance system of IMF:

Any country at the time of joining IMF enters into an agreement to go for scrutiny of its economic and financial policies at the international level. It also promises and commits to provide all the data to IMF pertaining to its economy. The member nation will have to undertake and pursue all those policies which lead to bring price stability, avoid manipulation of exchange rates for unfair competitive advantage.

The IMF's also regularly monitors economies and tries to identify weaknesses that are causing or could lead to financial or economic instability. This process is known as surveillance.

So, IMF follows a unique set of system to become proactive in order to avoid any type of crises in international monetary system, which is called as surveillance. Under this system IMF timely and periodically reviews the policies of member countries. It also keeps a check on various financial developments of the member nations. A proper review is undertaken of various national, regional as well as global policies. IMF carries surveillance at three levels-

6.1.1 **Country surveillance –** where regularly usually annually comprehensive discussions with member countries are done as and when needed. This consultation is known as “Article IV Consultation”. In this a team of economists visit a member country to assess their economic and financial developments. Then they carry out discussions with policy makers and central bank officials. The team brings out a report which is later presented for the discussions of executive board. The summary of views of executive board is then informed to the government of that very country.

6.1.2 **Regional surveillance**-It involves assessment by the IMF of policies pursued under currency unions—including the euro area, the West African Economic and Monetary Union, the Central African Economic and Monetary Community, and the Eastern Caribbean Currency Union. Timely Regional economic outlook reports are also prepared to discuss economic developments and key policy issues in Asia Pacific, Europe, Middle East and Central Asia, Sub-Saharan Africa, and the Western Hemisphere .(www.imf.org)

6.1.3 **Global surveillance-**The IMF keeps a regular check on global trends as well. It publishes the following reports for analysing and assessing the various macroeconomics and economic developments throughout the world:

1. The World Economic Outlook
2. The Fiscal Monitor
3. The Global Financial Stability Report

It carries out the following in order to create a balance in international monetary system-

1. It advises member nations so as to how various policies can help to foster economic stability.
2. It guides the member nations as to how they can reduce susceptibility to economic and financial crises.
3. Through its Global Financial Stability Report it regularly assesses the global prospects of emerging economies.
4. It regularly publishes a series of regional economic outlooks.
5. It helps the low income economies to develop policies which can help them improve their fiscal position, standard of living, reduce level of poverty.

The IMF usually monitors member's country economies through regular annual consultations. During these consultations, IMF staff carries out serious discussions on various economic and financial factors with policy makers. They help to assesses risks and vulnerabilities, and consider the impact of fiscal, monetary, financial, and exchange rate policies on the member's domestic and balance of payments stability.

6.2 Technical assistance by IMF:

The IMF grants technical assistance, training and support to help member countries so that they can build, improve and strengthen their capability to design and implement effective policies keeping in view the global situations. Technical assistance is provided in the following key areas-

1. Taxation policies of the economies and its administration
2. Expenditure management of the member nations
3. Management and implementation of monetary and exchange rate policies
4. Supervision and regulation of banking and financial systems
5. Legislative frameworks pertaining to policies
6. Statistical Support

6.3 Lending/ Financial assistance: IMF provides financial assistance/ funds to member countries if they face balance of payment crises so as to solve and eradicate macroeconomic problems so as to help them in creating stability at the time of crises. The governments/national authorities of the member countries design and implement various adjustment programs with cooperation of IMF which are supported by IMF financing which is provided on the condition of effective implementation of the said programs.

After global financial crises IMF has improved its lending capacity and wet into series of reforms in its financial support mechanisms in order to fight back with global crises more effectively. IMF is focusing on mitigating and managing crises and developing various instruments in order to respond to the situations in an efficient and effective manner. A Poverty Reduction and Growth Trust has been specially created to increase financial support to the world's poorer countries. It is also providing various concessional lending's to low income economies. The ambit of which has been especially increased after crises. The access norms and limits were increased by 50 percent in 2015. Some loans are even provided interest free through end 106. IMF is funding some special lending's in case of emergency at zero percent interest rates.

7. SDRs: IMF created one International reserve in 1969 which is called as SDR. This fund supplements the official reserves of member countries. The International reserve asset known as Special Drawing Rights (SDRs) can supplement the official reserves of member countries. The value of SDR is based on four Key International Currencies SDR's are easily exchangeable for freely usable currencies. SDR was created to support the Bretton Woods fixed exchange rate system.IMF members can voluntarily exchange SDRs for currencies among themselves.

Any member country which is participating in this system needed some official reserves—government or central bank holdings of gold and widely accepted foreign currencies. These currencies could be used to purchase the domestic currency in foreign exchange markets, as required to maintain its exchange rate. But gold and US Dollar were proved to be inadequate for expanding world trade. Therefore the international community resolved to create a International Reserve asset under IMF.

The SDR is neither a currency, nor a claim on the IMF. Rather, it is a potential claim on the freely usable currencies of IMF members. Holders of SDRs can obtain these currencies in exchange for their SDRs in two ways:

1. Through the arrangement of voluntary exchanges between members;
2. By the IMF designating members with strong external positions to purchase SDRs from members with weak external positions.

In addition to its role as a supplementary reserve asset, the SDR serves as the unit of account of the IMF and some other international organizations.

7.1. SDR Basket:

SDR basket consists of the euro, Japanese yen, pound sterling, and U.S. dollar. The value of the SDR in terms of the U.S. dollar is determined daily and posted on the IMF's website. It is calculated as the sum of specific amounts of the four basket currencies valued in U.S. dollars, on the basis of exchange rates quoted at noon each day in the London market.

The SDR interest rate provides the basis for calculating the interest charged to borrowing members, and the interest paid to members for the use of their resources for regular (non-concessional) IMF loans. It is also the interest paid to members on their SDR holdings and charged on their SDR allocation. The SDR interest rate is determined weekly and is based on a weighted average of representative interest rates on short-term debt instruments in the money markets of the SDR basket currencies.

7 Summary

The International Monetary Fund (IMF) is an international organization created for the purpose of standardizing global financial relations and exchange rates. Thus The IMF generally monitors the global economy, and its core goal is to economically strengthen its member countries. It provides various kinds of assistance to its member countries in the form of technical and financial assistance. Specifically, the IMF was created with the intention of:

1. Promoting global monetary and exchange stability.
2. Facilitating the expansion and balanced growth of international trade.
3. Assisting in the establishment of a multilateral system of payments for current transactions.