

# Structure and function of the international monetary fund



## **History**

During the great depression times of 1930s the countries put a halt on the foreign trading. This act of putting barriers devalued the currency of the countries, and citizens were not allowed to keep foreign currency. This led the world to a sharp decline in the trade chart and lowered living standard of people. The establishment of International Monetary Fund was the result of economic breakdown. International Monetary Fund was formally established in December 1945 but representatives of 45 countries agreed for the framework of International Monetary Fund. Till 1975 the institution had a system called par value system, according to which the currencies of country was valuated against US dollar and US dollar was valuated against gold. This conversion of dollar into gold was stopped in 1975. From then International Monetary Fund solved the problem of balance of payments in many poor countries of the world. A loan facility program named as Structural Adjustment Facility was started in March 1986. The International Monetary Fund helped the oil exporting countries in paying their debts. These were some of the historical financial activities where the International Monetary Fund played a crucial role.

## **Overview**

The main function of International Monetary Fund is to push the cooperation in international monetary and stability of exchange rates assists the international trade to grow and provide resources for the member countries to help them in situation of difficult balance of payments and poverty conditions. Currently there are 187 countries which hold the membership of International Monetary Fund. The institution has its own organizational <https://assignbuster.com/structure-and-function-of-the-international-monetary-fund/>

structure, governance, financial assets but is a specialized component of United Nations. The members of the International Monetary Fund have their own recognition in the global economy. The International Monetary Fund keeps record of its member countries and their economic condition, alerts them about the risks involved in any particular financial activity and gives advice on creating economic policies. International Monetary Fund help countries which are in difficulty by lending them, it also provide technical help and training to improve the economic condition of the country. All these works of International Monetary Fund are monitored and supported by the surveillance and research and development team of the International Monetary Fund. The International Monetary Fund also has collaboration and partnership with many international organizations which work for the growth and to reduce poverty. Institution also keeps active communication with civil societies, researchers and the media persons. (Eichengreen., 2002)

## **Operations of International Monetary Fund**

### **Surveillance**

The International Monetary Fund supervises the international monetary system and supervises the economic and fiscal policies of its member countries. National regional and global economic developments the member countries are tracked by the International Monetary Fund and macroeconomic and financial advice are also provided. International Monetary Fund's act of monitoring of economic stability in the member countries is known as Surveillance. Surveillance is of three types: Country Surveillance, Regional Surveillance, and Global Surveillance. Country surveillance is the comprehensive consultation provided to the member

countries of International Monetary Fund. An International Monetary Fund team is formed for the process which is used to visit the country and studies the financial and economical policies of the country. The report of the country is presented to the board of members of the International Monetary Fund to get the global views on the fiscal and economical policies. Regional surveillance is the monitoring of various currency unions like euro area, and Eastern Caribbean Currency Union. Global surveillance includes the process of reviewing global economic trends and covers the areas of economic developments, policies, and prospects of the global financial market.

### **Technical Assistance**

The International Monetary Fund provides its help in practical training of the countries which enables them to manage their financial policies more effectively. This training is beneficial for a country to upgrade the system and redesign the economic, financial and structural policies of the country. Providing technical assistance to its member countries is one of the core functions of the International Monetary Fund. International Monetary Fund supplies around 80% of the assistance to the countries which are highly indebted. The International Monetary Fund provides technical assistance in many different forms according to the need of the country. Partnership with many donors is extremely important for the functioning of International Monetary Fund as they used to finance around two third of the International Monetary Fund operations of technical assistance.

### **Lending Funds**

A country can face many severe financial crises like inability to pay foreign bills, negative balance of payments, and problem with the stability of <https://assignbuster.com/structure-and-function-of-the-international-monetary-fund/>

international financial system. International Monetary Fund was established for the support of these countries in these financial crises. International Monetary Fund helps every member country in financing to pay off the balance of payments and international payments.

## **Organizational Structure of International Monetary Fund**

The board of governors is the top authority of the International Monetary fund. It has one governor and one alternate governor for each country which is member of the International Monetary Fund. The appointed governor of each country is either the finance minister or the governor of the central bank of the country. The power of authority in International Monetary Fund is concentrated to the board of governors. Certain powers of the Board of governors can be given to the board of executive. The meeting of board of governors of the International Monetary Fund happen only once in a year in normal circumstances. The executive board of IMF has 24 directors which are elected by the member countries of IMF and the managing director who is also the chairman of the board. Voting power of different member countries of IMF varies according to the matter related Departments. The managing director is selected by voting process and the member who gets the highest number of votes is appointed as the MD of the IMF. (International Monetary Fund Organization Chart)

## **International Monetary Fund Funds & Lending**

### **Nature of Lending**

In the initial decades of the establishment of International Monetary Fund it used to lend half of its funds to the countries which required industrial

growth. But by 1970s the countries make themselves capable of meeting their financial needs of the capital market. In late 70s and 80s because of the fluctuating oil prices and financial crisis many countries with lower and lower middle income borrowed from International Monetary Fund. The demands of International Monetary Fund resources increased in 1990s due the transition of central and Eastern Europe and the economic crisis in the emerging markets. By the year 2004 the global economic conditions began to stabilize so the borrowers of International Monetary Fund funds start paying their loans to International Monetary Fund hence the demand of loans from International Monetary Fund declined sharply.

### **Lend for Financial Stability**

The purpose of International Monetary Fund's funding has been changing repeatedly since the organization was established. Initially International Monetary Fund used to fund the countries for their financial aids in dealing with the fluctuations in the short term trading. Now the purpose of funds has been changed to assist the problems in balance of payments which arises due to trading fluctuations, natural tragedies, economic transitions, economic development and currency crisis.

### **Conditions of Funding**

The funding conditions of International Monetary Fund loans depend on the economic health and financial policies of the member countries. The economic policies of the countries are discussed with International Monetary Fund in order to ensure that the current issues should be addressed most effectively. The loans from International Monetary Fund are distributed in many installments and each installment has to met the conditions are <https://assignbuster.com/structure-and-function-of-the-international-monetary-fund/>

targets defined to get the next installment from International Monetary Fund. The details of the economic program of the government need to be submitted to the MD of International Monetary Fund. International Monetary Fund resources are used to finance only a small fraction of the balance of payments. The typically required conditions for IMF funding are the macroeconomic and structural policies.

## **Difference in Roles of International Monetary Fund and World Bank**

International Monetary Fund and World Bank both are completely different in many aspects like their structure, different resources of funding, different members and different goals. The major difference in the roles of International Monetary Fund and World Bank is that the bank is a development institution whereas the International Monetary Fund is an institution which maintains the system of payments between countries. Unlike the World Bank International Monetary Fund is a small institution with around 2300 people working for it. IT has no subsidiaries or branches. International Monetary Fund assists the members of the organization in their problems of balance of payments whereas the World Bank financially assists the poorer countries whose GNP is less than 865 dollars per year.

## **Three main worldviews about IMF**

### **Liberalism**

Applying the liberalism world view on operations of IMF it can be seen that the liberalism view is applicable on the policies of IMF of advising countries in economic crisis. IMF regulates the trade policies of the countries; it encourages foreign trade between countries so that the companies can

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mutually get benefits of the trade by globalizing the production of goods. The policies of IMF do not change with the changing situations and nations as the liberalism view also considers all states equal. Like happened with Thailand in 1997, IMF applied the same policies in this situation which were earlier used in Latin American crisis and worsen the situation of Thailand.

### Economic Nationalism

This view best fits the operations and structure of IMF. The major actors in this view are the states and the members of IMF are countries. The motive of policies and strategies of IMF is to bring stability in the economy of the member countries only. The relations of IMF with the countries are dominated by IMF. The nationalism view is based on the Hegemonic stability theory which supports the stability in economy of states. Objective of IMF is the same, to bring stability in the economic conditions of a country.

### **Structuralism**

This view considers the major actor in policies is class i. e. the rich and developed countries are the countries which are benefitted by IMF operations. Policies of IMF are designed such that while helping a poor country in crisis it is actually making profit for the controlling countries. The executive committee of IMF has members only from these developed and rich countries as discussed in this view. The trade relation always benefits the countries like USA.



## **South Korea Economic Crisis & IMF**

The Asian economic crisis of 1997 occurred due to the declining value of Japanese Yen, hard competition with China, overabundance in electronics market, and heavy borrowing by Korean banks. So the crisis was not only the effect of external economic changes but also Korea was responsible for it. IMF issued a 57 billion USD loan to the country with certain terms and conditions. According to extreme liberal view IMF's actions created moral hazard and embedded liberal view states that the IMF's interference was required to control the situation. According to the nationalist view IMF helped the US economy not the Korea. Structural view says that the economic IMF conditions were made to benefit the G5 countries. According to Feldstein structural reform of Korean policies was unnecessary. Sachs criticized that the banks would solve the purpose in a better way than the IMF. The final outcomes were the flourishing Korea, expansion of Korean companies like LG.

## **Overview of International Monetary Fund based on Stiglitz's Article**

Joseph Stiglitz had written several articles on the world economy and the role of financial institution in it. In his article "What I learned at the World Economic Crisis – The Insider" he considers that the International Monetary Fund has helped many countries in the financial crisis and in times when the countries were facing the problem of balance of payments. The policies and financing structure of the International Monetary Fund is very adamant and do not change based on the changing problems in the world economy.

International Monetary Fund implied some policies to help Latin America I

the financial crisis of 1980s and was successful in the purpose. But it applied the same policies and structure on the economic crisis of Thailand in 1997. These implications of policies actually worsen the situation. There is no flexibility in the terms and conditions of the International Monetary Fund funding. So the article proposes that the fiscal policies of International Monetary Fund should be tractable in order to solve a wider range of problems. (Stiglitz., 2000)