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A research study to find out the changing role of the International Monetary Fund (IMF)

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ABSTRACT

The International Monetary Fund or the IMF, plays an important role with its global response to economic crises. It was created in 1944 to maintain the standard of fixed exchange rates which were established at the end of World War II. Since the abandonment of the gold standard in 1971, the IMF has adopted a new core mission, providing loans to economically troubled countries. The IMF is primarily governed by an executive board that consists of representatives of the IMF member countries, with a heavier weighting to countries that provide more money to the Fund. The executive board sets the broad policy and approves loans. The IMF has the potential to play a strategic and crucial role in stabilizing and supervising the global economy, it has its limitations due to the dynamic changes which are happening around the world's financial markets. Since countries have shifted to the flexible exchange rate system, financial independence and autonomy has increased. This development is bound to make the role of the IMF ineffective. For this research, I have collected real information by conducting a survey. I interviewed approximately 85 respondents living in Mumbai in order to fulfil the objectives of this research.

Keywords— *International Monetary Fund, Exchange Stability, Economic Crisis, Sustainable Economic Growth, International Trade, Balance of Payments, Quota Subscriptions, Asian Financial Crisis, Financial Assistance, International Monetary Cooperation ,Special Drawing Rights (SDR), Structural Adjustment Programs (SAPs), Stand-By Arrangement (SBA), Extended Fund Facility (EFF), Poverty Reduction and Growth Facility (PRGF)*

1. OBJECTIVES

The main aims for the analysis of this paper are to study

1. The Role of the IMF across the globe
2. The Role of the IMF in India
3. The Changes in Global Functioning
4. To evaluate the increasing need for the IMF to adopt new policies as per the changing global scenario

2. INTRODUCTION

In July 1944, the Bretton Woods Conference, also known as the United Nations Monetary and Financial Conference, was held in Bretton Woods, New Hampshire, United States. The conference's goal was to create a system of institutions that would foster international trade and investment while also preventing some of the monetary instability that had troubled the world following World War I. In the conference, the Articles of Agreement for a planned International Monetary Fund, which would oversee the new international monetary system, were drafted by delegates representing 44 countries.

3. OBJECTIVES AND FUNCTIONS

The IMF aims to:

- To promote global monetary cooperation
- To facilitate the balanced growth and expansion of global trade
- To promote exchange stability
- To assist member countries in the establishment of a standard multilateral system of payments
- To make resources available combined with appropriate safeguards to member countries experiencing payment difficulties

- To ensure stability of foreign exchange rates
- To reduce disequilibrium in the international balance of payments of member countries
- To promote capital investment in underdeveloped countries
- To provide short term monetary help to members during emergency situations
- To achieve balanced economic growth and a high level of employment in member countries

4. OPERATIONS

Member countries pay quota subscriptions to the IMF, which are used to fund the institution. The quota amount is dependent on the size of the member country's economy. The quota, in effect, dictates each country's weight within the IMF—and thus its voting rights—as well as the amount of IMF financing it can receive. Special drawing rights make up 25% of each country's quota. The SDR is a unit of account that member countries can use to settle international accounts with one another. A member's quota will determine its subscription, its voting weight, access to IMF funding, and allocation of Special Drawing Rights. The SDR, which is denoted by the US Dollar, can also be exchanged for other IMF members' freely traded currencies. Currently the USA has the largest share of quota, equaling 16.77% of the total votes available; it is thus the only country able to veto member decisions on its own (member decisions require an 85% majority). In contrast, India (with a population three times as large as the USA) has 2.34% of the votes; this distinction has prompted many to argue that the quota system should be reformed.

5. SCOPE

It has been established that the IMF provides support through surveillance, which it conducts on an annual basis for individual regions, countries and the global economy. However, if a country finds itself in an economic crisis, whether due to an unexpected shock to the economy or weak macroeconomic policy, it may request financial aid from the IMF. In exchange for IMF assistance during a crisis, a country is typically asked to pursue IMF supervised economic reforms, known as Structural Adjustment Programs (SAPs). The IMF has three widely used methods of providing finance to its members.

A Stand-By Arrangement (SBA) is the most utilized method of borrowing by the IMF. In this type of borrowing, a member state obtains the Fund's assurance that, over a period of 12-18 months, requests for foreign exchange withdrawals (i.e., to cover short-term BOP difficulties) up to a certain amount will be permitted if the country chooses to withdraw.

Next, the Extended Fund Facility (EFF) is a medium-term loan facility that allows countries to borrow a set amount of money over a period of four to ten years. The EFF seeks to address macroeconomic structural flaws that are driving chronic balance of payment inequalities. Financial and tax reform, as well as the privatization of public sector enterprises, are used to resolve these structural issues.

The Poverty Reduction and Growth Facility (PRGF) is the IMF's third major method of borrowing where loans are provided at extremely low interest rates. Its goal is to alleviate poverty in the poorest member countries while also building the groundwork for economic growth.

6. IMPORTANCE

We can see that throughout history the IMF has aided countries in averting financial disasters that would otherwise greatly damage their economies. The International Monetary Fund has instilled in member countries a sense that their economic issues affect the entire international community, not just them. They have done this by giving their members a platform to discuss monetary, fiscal, financial, trade, and exchange issues in general, as well as international payments problems. Through its many missions, the Fund has become a specialised institution that conducts research on various economic challenges and provides professional advice to member countries on how to effectively deal with them. The IMF has also provided support to developing countries in a variety of ways. It has attempted to address the issue of international liquidity by introducing Special Drawing Rights (SDRs), an artificial currency that was created as a foreign exchange reserve, primarily to aid poor countries.

6.1 Criticisms

Many developing countries benefit from the IMF's assistance in overcoming monetary issues and maintaining a stable international financial system. Despite this coherently defined aim, carrying out its job can be extremely difficult and have far-reaching consequences for the receiving countries. The International Monetary Fund has faced a slew of criticisms, the majority of which have focused on its conditions for loans, creation of moral hazard & lack of responsibility. Few of these criticisms include:

6.2 Loan Conditionality

The IMF lends money to countries on the condition that they follow certain economic policies. These policies usually include:

- Forcing governments to reduce borrowing, which leads to higher taxation and lower government spending.
- Implementation of higher interest rates to allow the currency to stabilise.
- Allowing unsuccessful firms to declare bankruptcy or become insolvent.
- Enforcing structural adjustments such as deregulations, reduction in corruption and privatisation.

6.3 Exchange Rate Reforms

The IMF's main goal was to establish a system of stable currency rates. After the Bretton Woods system collapsed in August 1971 as a result of the US's unwillingness to convert dollars into gold, the member countries adopted a variety of exchange rates including regulated float, pegged and joint float exchange rates. Thus, It is obvious that the IMF has failed to establish a stable and consistent international exchange market.

6.4 Moral Hazard

Member countries, like Greece, have been suspected of adopting unrealistic budgets in the hope that the international community, led by the IMF, would eventually rescue them. Countries are eager to borrow more as they have the knowledge that they will be bailed out.

6.5 Free Market Criticisms

Many argue that the IMF has been overreaching through its intervention. Advocates for free markets think that allowing capital markets to operate without intervention is preferable. They believe that intervening to control exchange rates compounds the problem and that allowing currencies to trade at market value is ideal.

7. REVIEW OF LITERATURE

In 1997, the Asian meltdown was caused in large part by South Korea, Thailand, the Philippines, Malaysia and Indonesia's heavy reliance on short-term foreign loans. When it became apparent that private enterprises in those nations would not be able to meet their payment obligations, international currency markets panicked. Currency traders sought to convert their Asian money into dollars, and the Asian currencies plummeted. That made it harder for the Asian countries to pay their loans, and it made imports suddenly very expensive. The IMF treated the Asian financial crisis like other situations where countries could not meet their balance of payment obligations. The Fund made loan arrangements to enable countries to meet foreign debt payments (largely to private banks in these cases) on the condition that the recipient countries adopt structural adjustment policies. But the Asian crisis differed from the normal situation of countries that faced difficulties paying off foreign loans.

Malaysia stood out as a country that refused IMF assistance and advice. Instead of further opening its economy, Malaysia imposed capital controls, in an effort to eliminate speculative trading in its currency. While the IMF mocked this approach when adopted, the Fund later admitted that it succeeded. Malaysia generally suffered less severe economic problems than the other countries embroiled in the Asian financial crisis.

7.1 Consequences of The Asian Financial Crisis in Countries Like Thailand and Indonesia

The Asian financial crisis led to massive amounts of human suffering. In South Korea, a country whose income approaches European levels, unemployment skyrocketed from approximately 3 percent to 10 percent. In Indonesia, the worst hit country, poverty rates rose from an official level of 11 percent before the crisis to 40 to 60 percent in varying estimates. GDP declined by 15 percent in one year. At one point, the food shortage in Indonesia became so severe that then-President B.J. Hobbies implored citizens to fast twice a week. IMF policies exacerbated the economic meltdown in countries hit by the Asian financial crisis. Mandated reductions in government spending worsened the Asian nation's recessions and depressions while forcing the elimination of price controls and subsidies for the poor imposed enormous costs on the lowest income strata.

7.2 The Relationship Between IMF And India

India is a Founding member of the IMF. India has not taken any financial assistance from the IMF since 1993. Repayments of all the loans taken from International Monetary Fund have beencompleted on 31 May, 2000. 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%. India decided to invest its reserves, initially up to US$ 10 billion through the Notes Purchase Agreement (NPA), and subsequently up to US$ 14 billion through New Arrangement to Borrow(NAB) As of 7 April, 2011, India has invested SDR 750 million (approx. 5,340.36crores) through nine note purchase agreements with the IMF. The relationship between the IMF and India has grown strong over the years. In fact, the country has turned into a creditor to the IMF. India is among one of the developing economies that effectively employed the various Fund programs to fortify its fiscal structure. Through productive engagement with the IMF, India formulated a consistent approach to expand domestic and global assistance for economic reforms. Whenever India underwent balance of payments crises, it sought the help of the IMF and in turn the internationally recognized reserve willingly helped India to overcome its difficulties.

8. INDIAN ECONOMIC CRISIS OF 1991

8.1 Causes and consequences

The crisis was caused by currency overvaluation; the current account deficit, and investor confidence played a significant role in the sharp exchange rate depreciation. The economic crisis was primarily due to the large and growing fiscal imbalances over the 1980s. During the mid-eighties, India started having balance of payments problems. Precipitated by the Gulf War, India's oil import bill swelled, exports slumped, credit dried up, and investors took their money out. Large fiscal deficits, over time, had a spillover effect on the trade deficit culminating in an external payments crisis. By the end of 1990, India was in serious economic trouble. The gross fiscal deficit of the government (center and states) rose from 9.0 percent of GDP in 1980-81 to 10.4 percent in 1985-86 and to 12.7 percent in 1990-91. For the center alone, the gross fiscal deficit rose from 6.1 percent of GDP in 1980-81 to 8.3 percent in 1985-86 and to 8.4 percent in 1990-91. Since these deficits had to be met by borrowings, the internal debt of the government accumulated rapidly, rising from 35 percent of GDP at the end of 1980-81 to 53 percent of GDP at the end of 1990-91. In mid-1991, India's exchange rate was subjected to a severe adjustment. This event began with a slide in the value of the Indian rupee leading up to mid-1991.The authorities at the Reserve Bank of India took partial action, defending the currency by expanding international reserves and slowing the decline in value. However, in mid-1991, with foreign reserves nearly depleted, the Indian government permitted a sharp depreciation that took place in two steps within three days (1 July and 3 July 1991) against major currencies.

8.2 Recovery

India was only weeks away from defaulting on its external balance of payment obligations.

The foreign exchange reserves had dried up to the point that India could barely finance three weeks worth of essential imports. The Government of India's immediate response was to secure an emergency loan of $2.2 billion from the International Monetary Fund by pledging 67 tonnes of India's gold reserves as collateral. The Reserve Bank of India had to airlift 47 tonnes of gold to the Bank of England and 20 tonnes of gold to the Union Bank of Switzerland to raise $600 million. National sentiments were outraged and there was a public outcry when they learned that the government had pledged the country's entire gold reserves against the loan.

9. RESEARCH METHODOLOGY
Exploratory research is undertaken to explore an area where little is known or to investigate the possibilities of undertaking a particular research study. Quantitative research deals with data which can be expressed numerically and is used for the collection of data from a small sample. Therefore, the type of research Methodology used for this study is - Exploratory & Quantitative Research.

10. HYPOTHESIS
The hypothesis proposed here is as mentioned below:
Ho- The IMF has played a role in bringing economic stability worldwide.
H1- The IMF has not played any role in bringing economic stability worldwide.

11. DATA TYPES AND SOURCES '
Types of Data can be classified into two types: Primary & Secondary.

11.1 Meaning of Primary data and its importance
Primary data refers to the first hand data gathered by the researchers themselves. Sources of primary data include surveys, observations, experiments, questionnaires, interviews, focus groups etc. An advantage of using primary data is that it directly answers the question that needs to be addressed and provides up to date information while allowing the researcher to have control over how the data is collected to ensure accuracy. However, collecting primary data is a time-consuming process.

11.2 Meaning of Secondary data and its importance
Secondary data is the data that has already been collected through primary sources and made readily available for researchers to use for their own research. It is data that can be collected from several sources such as censuses, government publications, internal records of an organisation, reports, books, journals, articles, websites etc. Secondary data is quickly and easily accessible to researchers. Some sources of secondary data also provide large sample sizes that more accurately represent the population. But, secondary data isn't always specific to the purpose of an individual's research and might be out-dated.

For this research, both primary and secondary data have been used.

11.3 Sampling Methodology
There are two types of sampling methods:
· Probability sampling involves random selection, allowing you to make statistical inferences about the whole group.
· Non-probability sampling involves non-random selection based on convenience or any other other criteria, allowing you to easily collect initial data.
For this research, probability sampling has been utilized.

11.4 Population
This is the set of maximum people (male & female) of different fields to which the findings are to be generalized.

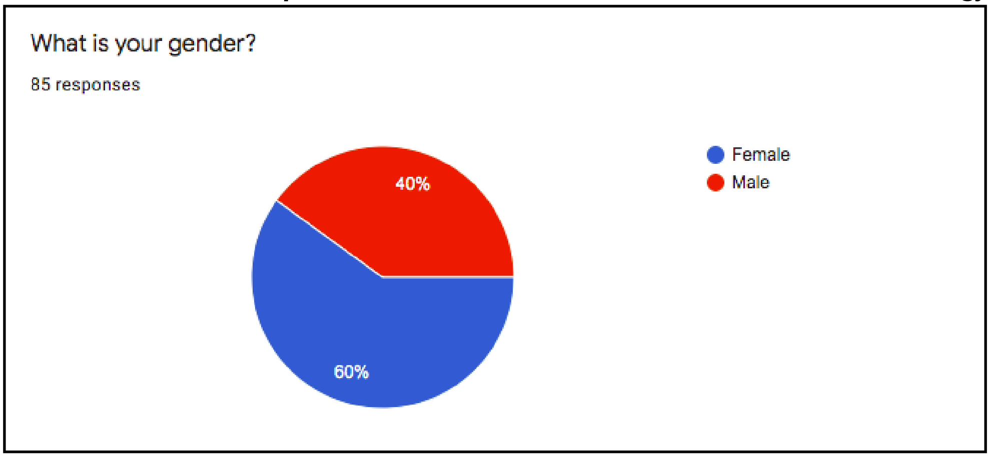
11.5 Sample Size
A sample size of 85 respondents is selected for this study to make the study meaningful and relevant.

11.6 Sampling Area
The area of the research was the city of Mumbai located in the state of Maharashtra in India. This city was selected because it is the business capital of India so its residents are likely to be trading in foreign currencies and would be aware of the IMF.

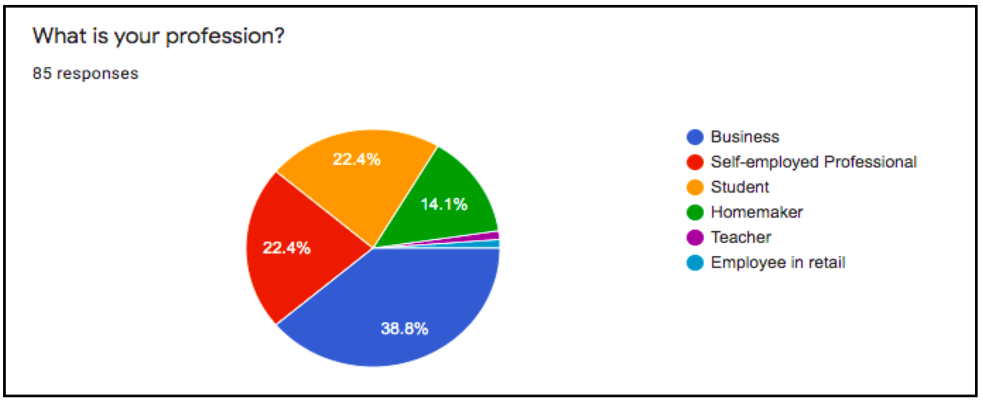
11.7 Sampling Procedure
The sample type & procedure opted for this study is prepared by circulating a questionnaire via Whatsapp within the city of Mumbai. The data collected is mainly based on gender and profession.

11.8 Limitations of the Study
- The study is only conducted in the city of Mumbai in India.
- The lack of knowledge of respondents about International Monetary Fund can be a major limitation. Restrictions due the Covid-19 pandemic prevented the utilisation of in-person interviews as sources of data.
- The analysis is based upon primary as well as secondary data. A possibility of unauthorized data cannot be avoidable.

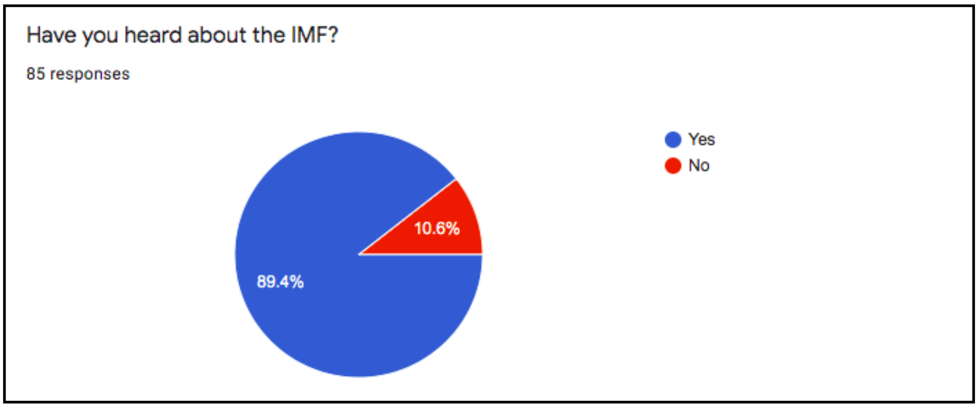
12. DATA ANALYSIS AND PRESENTATION
WE TOOK THE SURVEY: QUESTIONNAIRE METHOD AND RESULTS WERE AS FOLLOWS: WE GOT 85 RESPONSES TO THE COMPULSORY QUESTIONS ASKED BELOW:



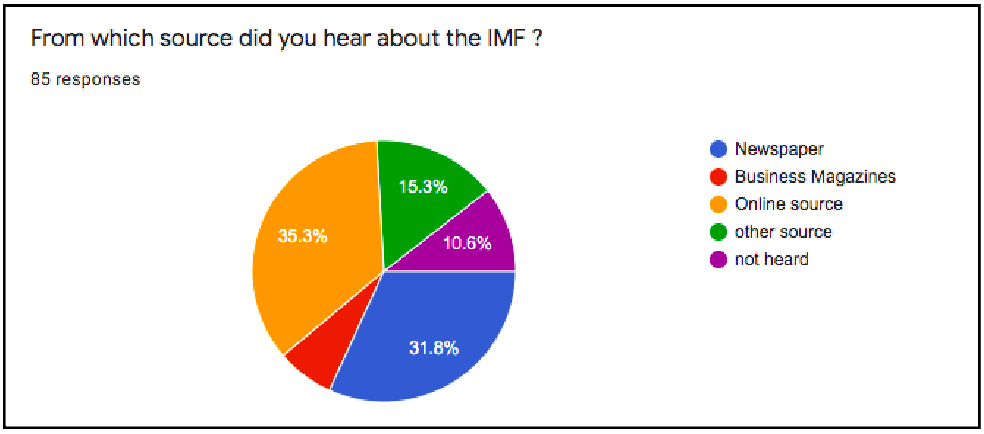
From the above it is clear that males have outnumbered females in answering questionnaire.



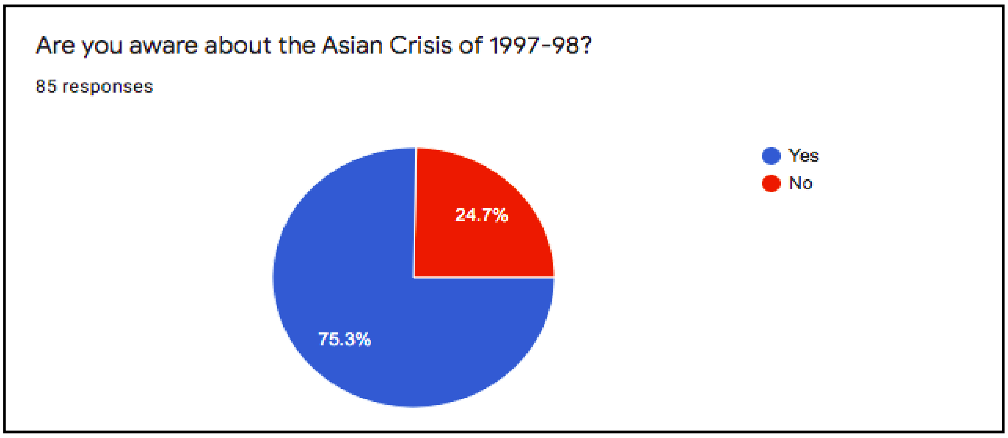
People from various profession have filled the questionnaire.



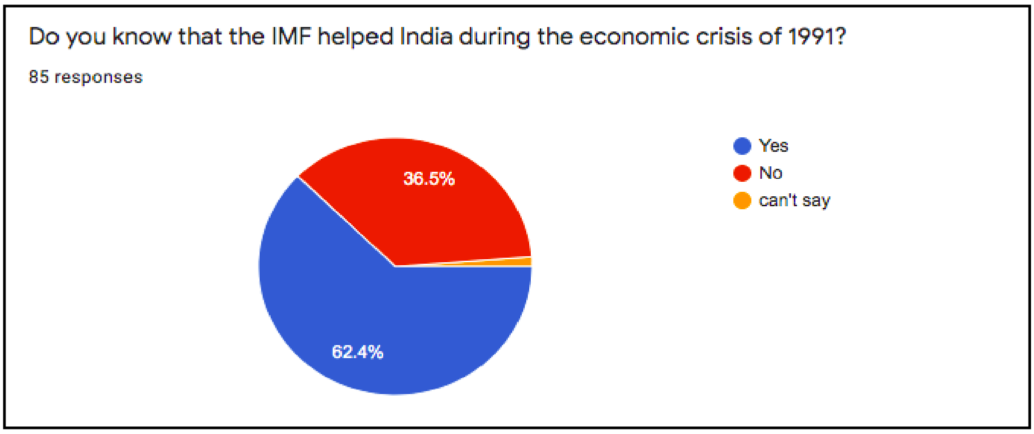
From the above diagram we can infer that a large percentage of the survey population were aware about the IMF which helps strengthen the evidence for this research.



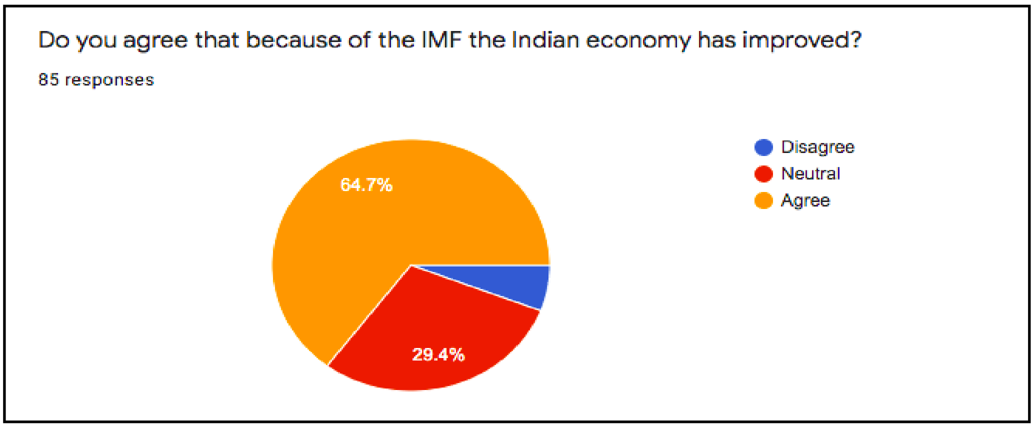
The pie chart above indicates that Newspapers and Online sources are largely used data sources where the IMF is frequently discussed.



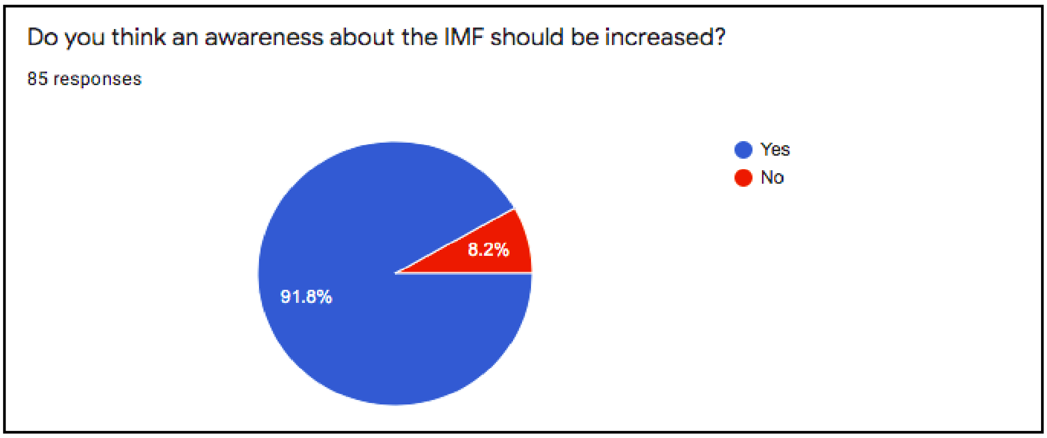
Almost 3/4th of the surveyed population was aware of the Asian Crisis of 1997-98 which ensured that respondents did have adequate knowledge of this field while filling the form.



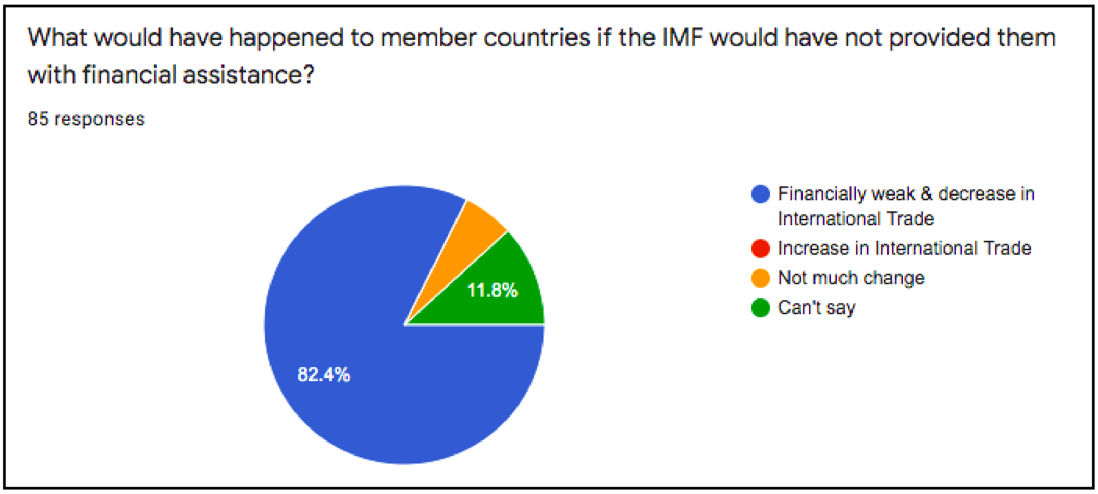
An adequately large number of the population was informed of the IMF's contribution to helping India combat its economic crisis of 1991.



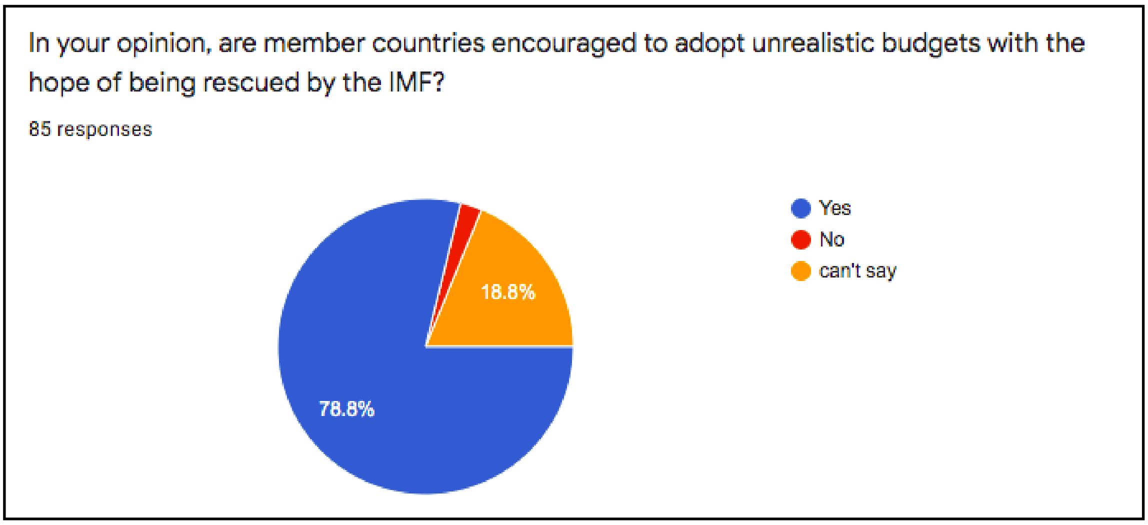
More than 50% of the population believed that because of IMF, Indian economy has improved.



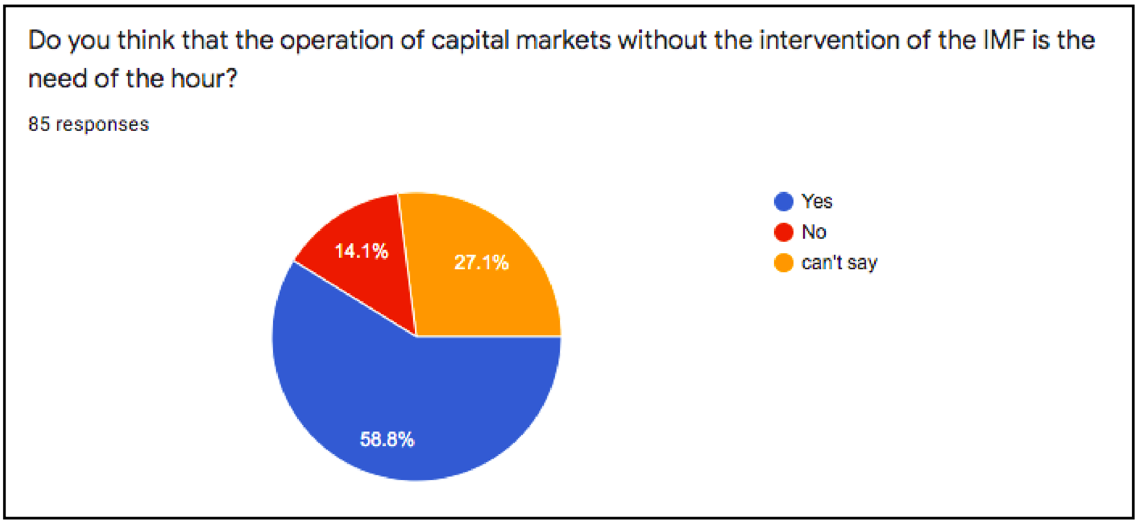
Almost the entirety of the surveyed population acknowledges the need to increase the awareness of the IMF in society.



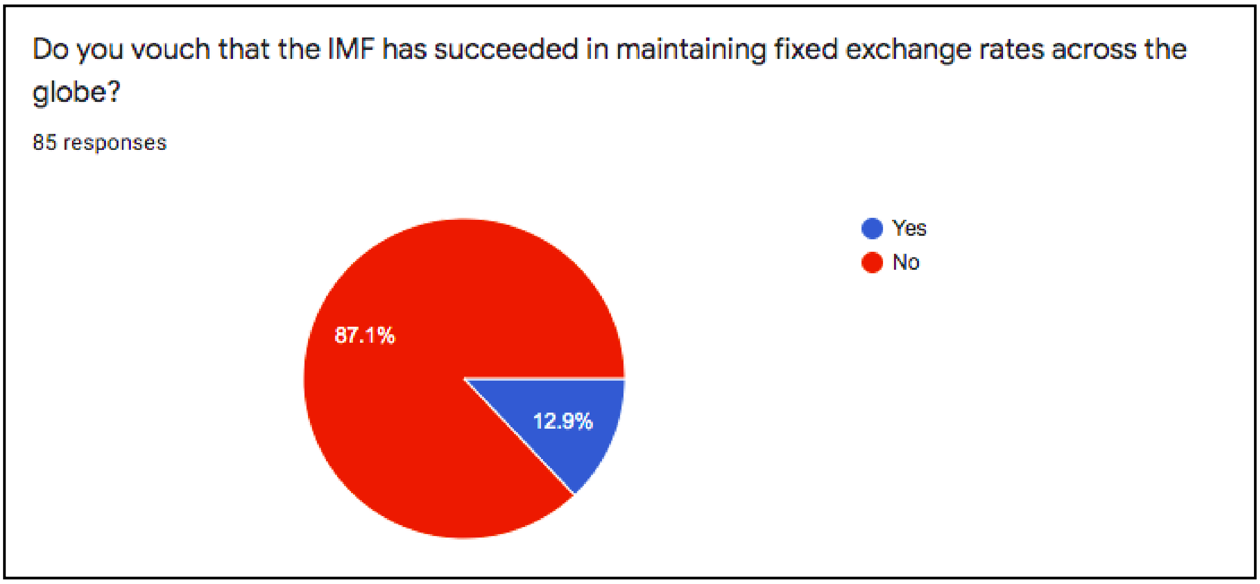
As per the data presented above, the absence of aid from the IMF leads to financial weakness and decrease in International trade within member countries.



According to the data acquired from the questionnaire, a high number of respondents believe that member countries are encouraged to adopt unrealistic budgets with the hope that the IMF will bail them out during a crisis.



An analysis of the data presented above suggests that it is necessary for capital markets to function without the intervention of the IMF.



This figure indicates that that a large number of people do think that the IMF has not succeeded in stabilising global exchange rates.

13. FINDING, CONCLUSION AND SUGGESTIONS

From the primary and secondary information provided, it can be concluded that the future of both Bretton Woods institutions remains uncertain. Both the IMF and World Bank escaped the efforts of the Republican U.S. Congress in the mid-1990s to sharply curtail and even eliminate both organizations. These agencies have been less successful in answering the charges from the left, as the IMF retains its demand for "structural adjustments" and the World Bank still favors funding for large, project-driven funding. While both the IMF and the World Bank have instituted some reforms, they have been unable to appease the concerns of outraged environmentalists, labor unionists, and nationalists and advocates of indigenous peoples in the developing world. Still, as this essay has suggested, these two organizations are really the misguided target for the legitimate concerns people of all ideological stripes have had about the rapid pace of globalization in the past half century.

While it is true that they have often been too driven by U.S. foreign policy concerns, in the end the influence of both institutions has been widely overstated. And despite their mistakes during the past half century, they have rarely been given credit for many of the little things they do well. Both institutions perform economic surveillance over most of the world's economy, a valuable task that no other international or private organization could perform with such skill. Both agencies also serve as a store of expert knowledge and wisdom for countries throughout the world that lack trained specialists. While neither the IMF nor the World Bank has met the lofty goals of their founders or wielded the nefarious influence charged by their critics, they have and should continue to play a small but important role in promoting prosperity and economic stability worldwide. Therefore my Null Hypothesis (H0) has been proved and my Alternative Hypothesis (H1) is proved wrong.

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APPENDIX

Questionnaire

1. What is your gender? *
   - Female
   - Male

2. What is your profession? *
   - Business
   - Self-employed Professional
   - Student
   - Homemaker
   - Other

3. Have you heard about the IMF? *
   - Yes
   - No

4. From which source did you hear about the IMF? *
   - Newspaper
   - Business Magazines
   - Online source
   - other source
   - not heard
5. Are you aware about the Asian Crisis of 1997-98? *
   - Yes
   - No

6. Do you know that the IMF helped India during the economic crisis of 1991? *
   - Yes
   - No
   - can't say

7. Do you agree that because of the IMF the Indian economy has improved? *
   - Disagree
   - Neutral
   - Agree

8. Do you think awareness about the IMF should be increased? *
   - Yes
   - No

9. What would have happened to member countries if the IMF would have not provided them with financial assistance? *
   - Financially weak & decrease in International Trade
   - Increase in International Trade
   - Not much change
   - Can't say

10. In your opinion, are member countries encouraged to adopt unrealistic budgets with the hope of being rescued by the IMF? *
    - Yes
    - No
    - can't say

11. Do you think that the operation of capital markets without the intervention of the IMF is the need of the hour? *
    - Yes
    - No
    - can't say

12. Do you vouch that the IMF has succeeded in maintaining fixed exchange rates across the globe? *
    - Yes
    - No

