The International Monetary Fund

Headquarters building of the International Monetary Fund, Washington, D.C.

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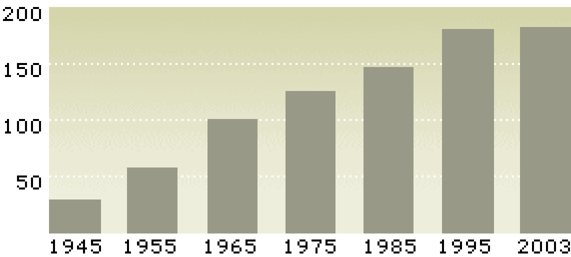
The Executive Board of the International Monetary Fund, Washington, D.C.

What is the IMF?

The International Monetary Fund (IMF) was created in 1944 at the Bretton Woods Conference and is one of the three international organizations. The purpose of the IMF is to promote international monetary cooperation, exchange stability, and orderly exchange arrangements; to foster economic growth and high levels of employment; and to provide temporary financial assistance to countries to help balance of payments adjustment [1]. The idea came from the intention to prevent the kinds of chain reaction in the economic system that caused world currencies to collapse like in the Great Depression of the 1930s.



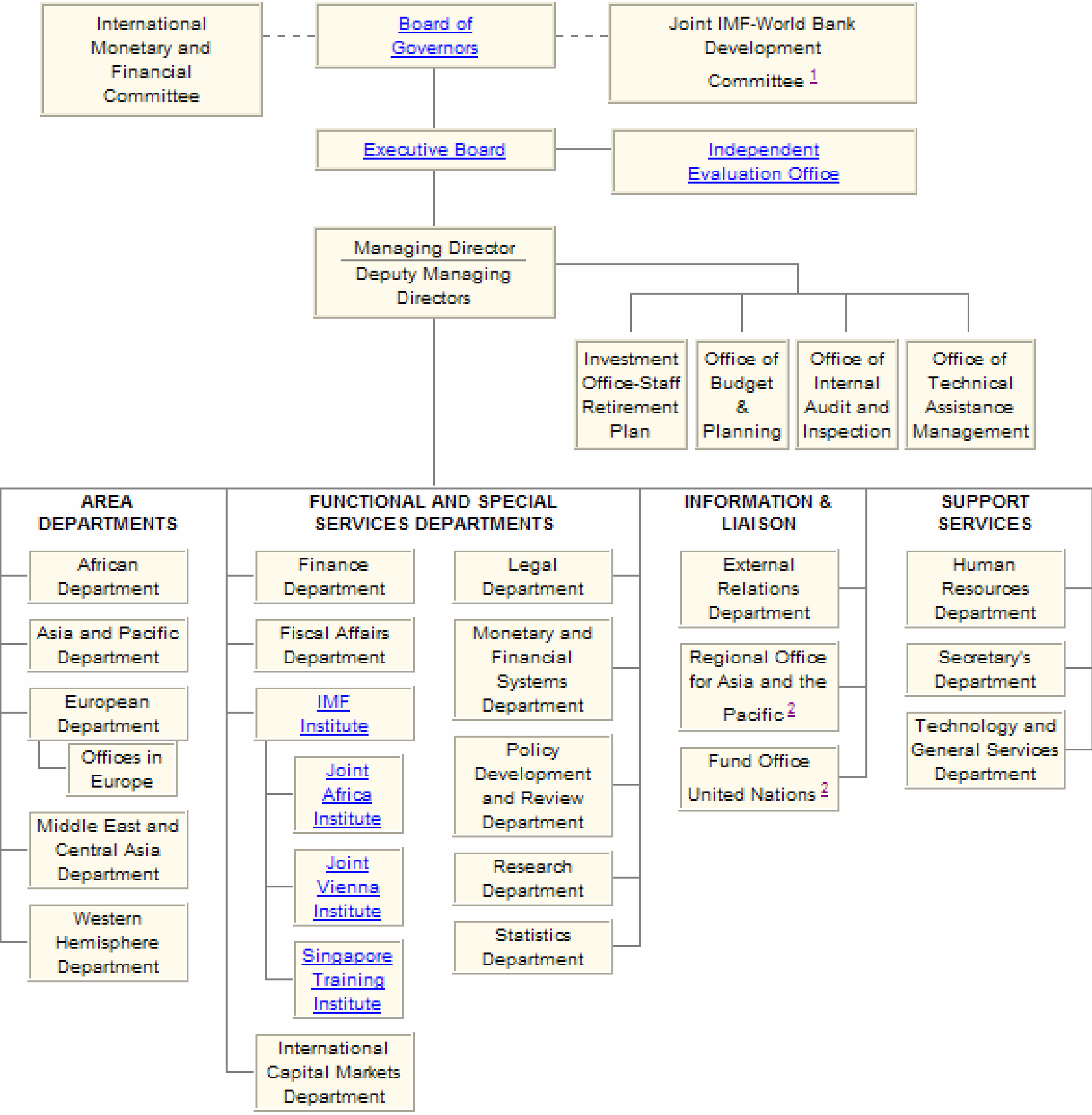
Growth in IMF Membership, 1945 - 2003
(number of countries)

In the beginning there were 29 member countries who contributed a certain share of the money when they signed its Articles of Agreement in December 1945. Those years marked an era during which economic activities in the major industrial countries weakened. Today, IMF has 184 member nations and a staff of about 2680, of whom two-thirds are economists in 139 countries, with headquarters in Washington, D.C. It is administered by a 24-member Executive Board representing the IMF's 184 members and currently chaired by *Rodrigo de Rato* who is Spanish. Also, there is another team of management formed by three Deputy Managing Directors where each director is drawn from a different region of the world.

The Board of Governors, on which all member countries are represented, is the highest authority governing the IMF. It usually meets once a year, at the Annual Meetings of the IMF and the World Bank. Each member country appoints a Governor (usually the country's minister of finance or the governor of its central bank) and an Alternate Governor. The Board of Governors decides on major policy issues but has delegated day-to-day decision-making to the Executive Board. Key policy issues relating to the international monetary system are considered twice-yearly in a committee of Governors called the International Monetary and Financial Committee, or IMFC (until September 1999 known as the Interim Committee)[1]. A joint committee of the Boards of Governors of the IMF and World Bank called the Development Committee advises and reports to the Governors on development policy and other matters of concern to developing countries.

Over time, the purposes of IMF have remained unchanged but its operations such as surveillance, financial assistance, and technical assistance have developed to meet the changing needs of its members in an evolving world economy. Especially in the early 1990s, there were enormous economic challenges due to the globalization. IMF responded to those needs by introducing reforms aimed at strengthening the architecture of the international monetary and financial system and by enhancing its own contribution to the prevention of financial crisis. According to the report of August 31, 2005, the Fund has total quotas of $312 billion and outstanding loans of $71 billion to 82 countries. The IMF's five largest

shareholders are the United States, Japan, Germany, France, and the United Kingdom and also there are China, Russia, and Saudi Arabia who have their own seats on the Board. The other 16 Executive Directors are elected for two-year terms by groups of countries, known as constituencies.

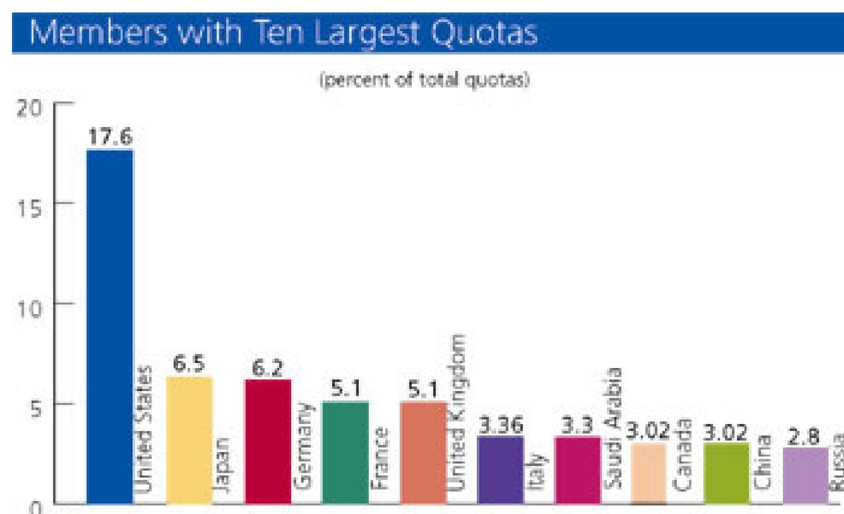


The IMF's resources come mainly from the quota (or capital) subscriptions that countries pay when they join the IMF, or following periodic reviews in which quotas are increased. Countries pay 25 percent of their quota subscriptions in Special Drawing Rights (SDRs) or major currencies, such as U.S. dollars or Japanese yen; the IMF can call on the remainder, payable in the member's own currency, to be made available for lending as needed. Quotas determine not only a country's subscription payments, but also the amount of financing that it can receive from the IMF, and its share in SDR allocations. Quotas also are the main determinant of countries' voting power in the IMF. Quotas are intended broadly to reflect members' relative size in the world economy: the larger a country's economy in terms of output, and the larger and more variable its trade, the higher its quota tends to be. The United States of America, the world's largest economy, contributes most to the IMF, 17.5 percent of total quotas; Palau, the world's smallest, contributes 0.001 percent. The most recent (eleventh)

quota review came into effect in January 1999, raising IMF quotas (for the first time since 1990) by about 45 percent to SDR 212 billion (about $300 billion)[1].

IMF also, if it sees necessary, may borrow to supplement the resources available from its quotas. The IMF has two sets of standing arrangements to borrow if needed to cope with any threat to the international monetary system [1]:

- The General Arrangements to Borrow (GAB), set up in 1962, which has 11 participants (the governments or central banks of the Group of Ten industrialized countries and Switzerland).
- The New Arrangements to Borrow (NAB), introduced in 1997, with 25 participating countries and institutions. Under the two arrangements combined, the IMF has up to SDR 34 billion (about $50 billion) available to borrow.



The IMF's purposes have also become more important because of the expansion of its membership. The number of IMF member countries has more than quadrupled from the date it was formed. This reflects in particular the attainment of political independence by many developing countries and more recently the collapse of the Soviet bloc. Also the expansion of the IMF's membership, together with the changes in the world economy, have required the IMF to adapt in a variety of ways to continue serving its purposes effectively.

IMF looks at the performance of the economy as a whole, in another words macroeconomic performance. This includes total spending and its major components like consumer spending and business investment, output, employment, inflation and as well as the country’s balance of payments. We can describe one country’s macroeconomic policies as those policies related to the government’s budget, the management of the interest rates, money, and credit, and exchange rate. On the other hand, IMF focuses also on the financial sector policies such as regulation and supervision of banks and other financial institutions. In addition the IMF pays attention to structural policies that affect macroeconomic performance. We can give labor market policies that affect employment and wage behavior as examples of structural policies.

IMF gives advices to each member on how its policies in these areas may be improved. It can be said that the IMF is a forum which involves active dialogue with each country and

discussing not only national economic policies in a global context, but also issues important to the stability of the international monetary and financial system. In September 2000, the IMF's then managing director Horst Köhler set out some major priorities for the work of the IMF [1]. According to those priorities, institution would make all the effort to promote sustained non-inflationary economic growth that benefits all people of the world; to be the center of competence for the stability of the international financial system; focus on its core macroeconomic and financial areas of responsibility, working in a complementary fashion with other institutions established to safeguard global public goods; and to be an open institution, learning from experience and dialogue, and adapting continuously to changing circumstances.

Countries that joined the IMF between 1945 and 1971 agreed to keep their exchange rates (in effect, the value of their currencies in terms of the U.S. dollar, and in the case of the United States, the value of the U.S. dollar in terms of gold) kept at rates that could be adjusted, but only to correct a "fundamental disequilibrium" in the balance of payments and with the IMF's concurrence [1]. This so-called Bretton Woods system of exchange rates remained in place until 1971 when the U.S. government suspended the convertibility of the U.S. dollar (and dollar reserves held by other governments) into gold. Since then, IMF members are free to choose any form of exchange arrangement they wish: some now allow their currency to float freely, some keep their currencies pegged to another currency or a group of currencies, some have adopted the currency of another country as their own, and some participate in currency blocs.

Briefly, we mention below the IMF's purposes that are indicated in the Article #1 of Articles of Agreement [1]:

- To promote international monetary cooperation through a permanent institution which provides the machinery for consultation and collaboration on international monetary problems.
- To facilitate the expansion and balanced growth of international trade, and to contribute thereby to the promotion and maintenance of high levels of employment and real income and to the development of the productive resources of all members as primary objectives of economic policy.
- To promote exchange stability, to maintain orderly exchange arrangements among members, and to avoid competitive exchange depreciation.
- To assist in the establishment of a multilateral system of payments in respect of current transactions between members and in the elimination of foreign exchange restrictions which hamper the growth of the world trade.
- To give confidence to members by making the general resources of the Fund temporarily available to them under adequate safeguards, thus providing them with opportunity to correct maladjustments in their balance of payments without resorting to measures destructive of national or international prosperity.
- In accordance with the above, to shorten the duration and lessen the degree of disequilibrium in the international balances of payments of members.

Operations

So, the Fund is supposed to be directed in all policies and decisions by the purposes set forth in this agreement. Striving to serve these purposes, the IMF has engaged in the following operations:

- Monitoring economic and financial developments and policies, in member countries and at the global level, and giving policy advice to its members based on its more than fifty years of experience.
- Lending to member countries with balance of payments problems, not just to providing temporary financing but to support adjustment and reform policies aimed at correcting the underlying problems.
- Providing the governments and central banks of its member countries with technical assistance and training in its areas of expertise.

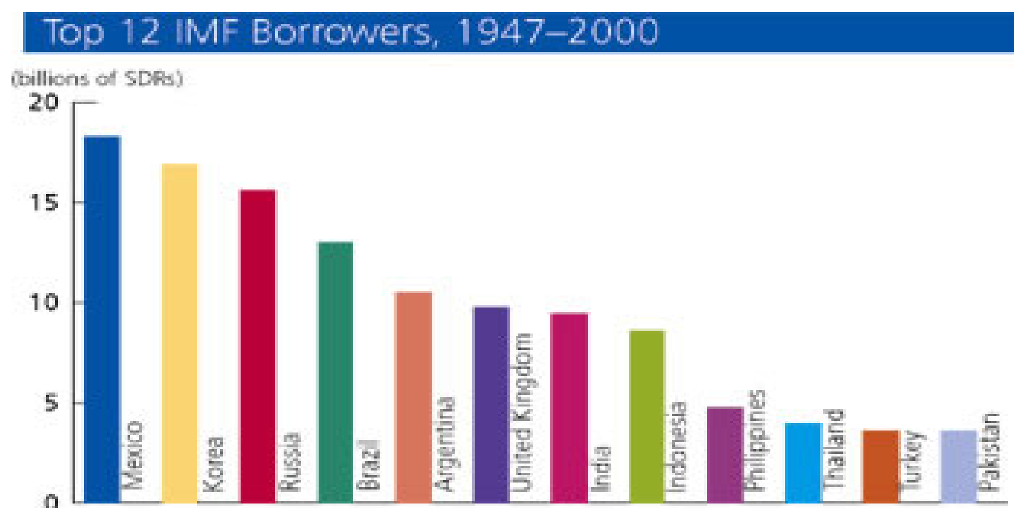
How the IMF's policies are determined and implemented

The Executive Board usually meets three times a week, in full-day sessions, and more often if needed, at the organization's headquarters in Washington, D.C. The IMF has a weighted voting system: the larger a country's quota in the IMF—determined broadly by its economic size—the more votes it has. But the Board rarely makes decisions based on formal voting; rather, most decisions are based on consensus among its members and are supported unanimously.

Positive effects of the IMF's policies

The IMF offers its financial assistance to the countries or regions which they find themselves in an economic crisis whether caused by a sudden shock to its economy or poor macroeconomic planning. In return for the IMF's help, a country is usually required to embark on an IMF-monitored economic reform program, otherwise known as Structural Adjustment Policies (SAPs).

The IMF can lend its money in three implemented facilities [1]. Loans are administered with especially low interest rates. A Stand-by Agreement offers financing of a short-term balance of payments, usually between 12 to 18 months. A medium-term arrangement which is termed as the Extended Fund Facility (EFF), typically over a three to four-year period aims to address structural problems within the macro-economy that are causing chronic balance of payment inequities. The third main facility offered by the IMF is known as the Poverty Reduction and Growth Facility (PRGF). As the name implies, it aims to reduce poverty in the



poorest of member countries, at the same time, laying the foundations for developing their economies.

The IMF offers technical assistance to transitional economies, for instance, the former Soviet Republics, during the time of changeover from centrally planned economies to market-run economies. The IMF offers emergency funds to collapsed economies. Another example, in the time of the 1997 financial crisis in Asia, the funds were injected into South Korea's foreign reserves in order to boost the local currency, help the country avoid a damaging devaluation. Emergency funds can also be loaned to the countries that have faced economic crisis as a result of a natural disaster.

Negative effects of the IMF’s policies

The structural adjustment is an undemocratic and inhumane means of loaning funds to countries facing economic failure. These countries are often facing the social problems, because they have to put financial concerns ahead of the social ones. Thus, by being required to open up their economies to foreign investment, to privatize public enterprises, and to cut government spending, these countries suffer an inability to properly fund their education and health programs. Moreover, foreign investing corporations often exploit the situation by taking advantage of local cheap labor while showing no regard for the environment. So, in another word, maybe the IMF is only deepening the gap between the wealthy and the poor countries of the world.

Another example is the economic crisis which occured in Argentina. The government of Argentina was required by the IMF to reduce the government spending, higher the cost of the public service, allow the foreign corporations to transfer the capital freely and a political condition was added which was authorizing the immunity of American soldiers. At last, the government was obliged to accept this political condition of the IMF. In this case, we can obviously see that the IMF has become a tool, with which the USA imposes the political and military pressure to other countries.

Direct effects of policies

The policies of the IMF can help the low income countries and reduce the property.

“At present, more than a billion people are living on less than $1 a day. More than three-quarters of a billion people are malnourished—about a fifth of them children. One-hundred and sixteen of every 1000 children born in low-income countries die before reaching the age of five, the majority from malnutrition or disease that is readily preventable in high-income countries.” So the extreme poverty prevalent in low-income countries is really a critical problem facing the global community. According to the IMF website, “In September 1999, the objectives of the IMF's concessional lending were broadened to include an explicit focus on poverty reduction in the context of a growth oriented strategy. The IMF will support, along with the World Bank, strategies elaborated by the borrowing country in a Poverty Reduction Strategy Paper (PRSP).”

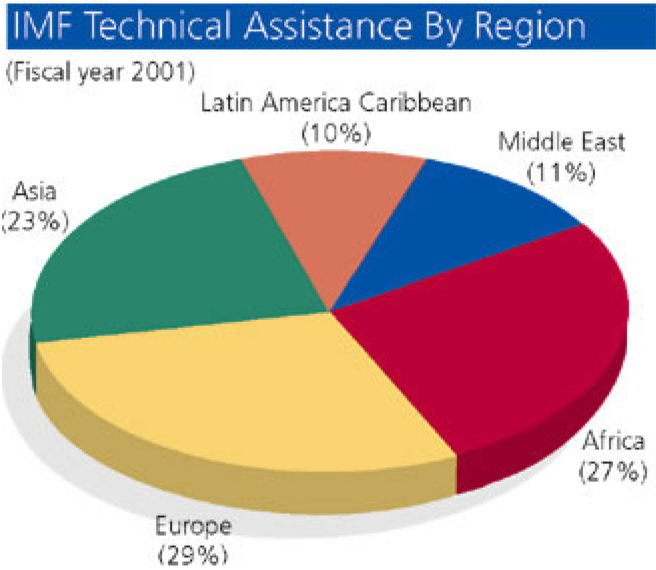
To solve the poverty problem, the first method must be implemented by the low-income countries themselves. They should pursue sound policies and good governance. The second method is larger and more effective international support, including official development assistance and trade liberalization to open markets to developing country exports [1].

Responding to widespread concern expressed by developed countries, and in concert with the World Bank, the IMF began its Heavily Indebted Poor Countries (HIPCs) facility in 1996. The HIPC initiative was intended to manage and even resolve the debt problems of the most heavily indebted poor countries (41countries, mostly in Africa) with a total debt of about $200 billion. In these countries debt service obligations consumed large parts of countries export earnings. The IMF tries to seek a permanent solution to these countries' debt problems by combining substantial debt reduction with policy reforms to raise long-term growth and reduce poverty.

The IMF provides financial assistance to low-income countries; it lends them money to support adjustment and reform policies designed to correct balance of payments problems and promote sustainable growth.

If the low-income countries do not want or do not need financial assistance from the IMF, the Policy Support Instrument can offer its advice, monitoring, and endorsement of their economic policies. It supervises the member countries, sometimes it sends additional staff to visit the member countries when needed. Each member country undertakes to collaborate with the IMF in its efforts to ensure orderly exchange arrangements and to promote a stable system of exchange rates. It can help signal dangers ahead and enable members to act in a timely way to avoid trouble. It is a vehicle intended to help them design effective economic programs and provide reassuring signals to donors, the multilateral development banks, and markets.

The IMF provides the technical assistance. Adequate policy-making capacity is critical for sustainable development and growth. The IMF provides assistance and training, generally free of charge, to help member countries strengthen the capacity of their institutions and officials to manage economic and financial policies. In recent years, the Fund has reinforced its efforts in low-income countries by establishing regional technical assistance centers in the Pacific, the Caribbean, East and West Africa, and in the Middle East. [1] It offers a wide range of technical assistance, as well as training for government and central bank officials, in its areas of expertise.



The IMF provides technical assistance and training mainly in four areas [1]:

- Strengthening monetary and financial sectors through advice on banking system regulation, supervision, and restructuring, foreign exchange management and operations, clearing and settlement systems for payments, and the structure and development of central banks;
- Supporting strong fiscal policies and management through advice on tax and customs policies and administration, budget formulation, expenditure management, design of social safety nets, and the management of internal and external debt;
- Compiling, managing, and disseminating statistical data and improving data quality;
- Drafting and reviewing economic and financial legislation.

The policy of IMF also helps its member country in crisis, by getting their economies back on track. When a country imports more than it exports, it has a "trade deficit," which can hurt both that country and others that it trades with. The IMF helps member countries cope with foreign exchange shortages caused by balance of payments problems. Bad luck, inappropriate policies, or a combination of the two may create balance of payments difficulties in a country.

The actual causes of economic crisis is usually varied and complex (e.g. weak domestic financial systems, large and persistent fiscal deficits). To solve this problem, the IMF can provide some types of loans, loans made through the Poverty Reduction and Growth Facility (PRGF), which provides funds to low-income countries to address protracted balance of payments problems; loans provided through Stand-By Arrangements (SBA), which is the largest amount of funds. It charges market-based interest rates on loans to assist with short-term balance of payments problems. The IMF provides other types of loans as well, including Emergency Assistance to countries that have experienced a natural disaster or are emerging from armed conflict.

Fast Facts on IMF Lending	
(as of August 31, 2005)	
Loanable funds	$140 billion
Of which: For concessional loans	$4 billion
Loans outstanding	$71 billion to 82 countries
Of which: Loans on concessional terms	$10 billion to 57 countries

Fast Facts on IMF Lending

Indirect effects of policies

Indirectly, the IMF policy strengthens the International Monetary and Financial System.

Globalization, by increasing the volume and speed of international capital flows, has also increased the risk of financial crises. The financial crises in emerging markets in the mid- and late 1990s were a reminder of the risks associated with globalization. (The most severe one is

the economic crisis in Asia). More and more financial crises occur and because of globalization, a crisis in one country or region can rapidly spill over into other economies. So investors may retreat quickly and massively if they sense shortcomings in domestic economic policies. The crises exposed not only policy weaknesses in the crisis countries themselves, but also flaws in the international financial system. IMF commits itself to advance the fight against poverty in low-income countries and enable countries to achieve higher living standards; indirectly, it strengthens the International Monetary and Financial System.

To reduce the risk of future financial crises and to promote the speedy resolution of those that do occur, the IMF has been working with its member governments, and with other international organizations, regulatory bodies, and the private sector, to strengthen the international monetary and financial system.

Speculations about the IMF

"Debt is an efficient tool. It ensures access to other peoples' raw materials and infrastructure on the cheapest possible terms. Dozens of countries must compete for shrinking export markets and can export only a limited range of products because of Northern protectionism and their lack of cash to invest in diversification. Market saturation ensues, reducing exporters' income to a bare minimum while the North enjoys huge savings. The IMF cannot seem to understand that investing in a healthy, well-fed, literate population is the most intelligent economic choice a country can make.[2]"

Over time, the IMF has come to play a much more active role than simply as a short-term donor to countries with a budget imbalance. Critics say the IMF operates mostly in the interest of global investors, and at the expense of workers in developing countries. Typically, the IMF requires countries that apply for loans to cut social spending, privatize state-owned industries, reduce workers' rights and emphasize production for export - all with the goal of enabling the country to pay off its debts. But their programs have been heavily criticized for many years for resulting in poverty. In addition, for developing or third world countries, there has been an increased dependency on the richer nations. This is despite the IMF and World Bank's claim that they will reduce poverty.

East Asian economies which experienced the pressure from the U.S. Treasury Department and the IMF to open up their markets completely to international investment, including short-run, speculative capital flows, were admired by the U.S. and the Fund and considered as neoliberal success stories [3]. But as soon as the hot money got out of those East Asian countries, Fund managers told that the East Asian governments had been less virtuous than they were presumed.

"The IMF likes to go about its business without outsiders asking too many questions. In theory, the fund supports democratic institutions in the nations it assists. In practice, it undermines the democratic process by imposing policies. Officially, of course, the IMF doesn't "impose" anything. It "negotiates" the conditions for receiving aid. But all the power in the negotiations is on one side—the IMF's—and the fund rarely allows sufficient time for broad consensus-building or even widespread consultations with either parliaments or civil society. Sometimes the IMF dispenses with the pretense of openness altogether and negotiates secret covenants. [4]"

A Case Study: Turkey

Turkey's stock market plunged in the crisis of the year 2000 and some interest rates increased to more than 1,200 percent in that financial crisis such that analysts feared that the crisis could spread to Russia and other struggling economies [3]. Turkish officials began emergency talks with the International Monetary Fund in Ankara, the capital, urgently asking for a $5 billion loan to help counter a rush to sell Turkish Lira that threatened to undermine the country's unsafe economy. Officials feared that, if not contained, the financial crisis could send Turkey's economy into a downward spiral of unemployment and company closures. Investors, both foreign and Turkish, were moving their money out of markets as they were losing confidence in the country's future and were worrying about the effect a devaluation of the Lira could have on their holdings. Turkey's stock market lost nearly 40 percent of its value in the following two weeks after crisis.

However, in the last few years, both the IMF and the government of Turkey have tried to explain the recovery of economy after the 2000 crisis as a result of "successful crisis management". The unmentioned reality behind the growth and deflation is that there has been an appreciation of the new Turkish lira (YTL) and sharp reductions in wages which is the result of a dramatic increase of the surplus value extracted from the working class [5]. The new IMF program will have serious social effects in a country where a quarter of the population lives below the poverty line, more than a million people go hungry and the vast majority find themselves in a state of misery and despair.

The first 10 months of the year of the crisis marked one of the most stable economic periods in recent Turkish history. In that period, Turkey had won praise from the IMF and international financial analysts for its financial policies, decreasing government spending and making other economic policy changes suggested by the IMF. In other words, Turkey was a perfect model of neoliberal economic virtue according to the IMF, and therefore one would think the last place a crisis should break out. So, due to that fact, following questions have been asked: Why declaration of some bad loans triggered a crisis in this situation, whereas it usually shouldn't have been the case? Who decided to lower the interest of financing productive Turkish investments, which would be brought to a standstill by astronomical interest rates, to the interests of international wealth management?

The crisis in Turkey led to thinking once again that deploying IMF policies like reducing government spending, privatizing public services, opening completely to international investment, and accumulating what used to be more than sufficient foreign exchange reserves to adequately protect your currency ($18 billion in the case of Turkey), is no protection at all from economic failure in the new world of unchecked neoliberalism.

What the future holds for the IMF and how it should seek to evolve

Coming up with viable suggestions for evolution paths for an organization as complex as IMF is extremely difficult at best. The inevitable prerequisite is being in a top position in terms of knowledge about economics and sociology and having access to accurate and impartial global statistics. We, as authors of this report, emphasize the fact that we are not in this privileged position and the following analyses and suggestions merely project our current knowledge of the world order and socio-economic aspects of the IMF's policies. The

suggestions made here can be seen mostly as rolling back the ideas of "Free Market Economy". They seemed enough reasonable and sustainable to the authors of this report, but may not seem as such to many readers.

We first highlight some of the criticisms of the organization:

For many years, the Fund has set severe loan conditions that in many cases have led to the deepening the crises. The Fund, even more than its partner, the World Bank, is known for its high-handed approach to poor countries. The manner with which it handled the Asian and Latin American crises has led to the criticism that its cure was worse than the illness. There is widespread belief that the IMF went too far in the previous crises on imposing policies such as control on government spending and higher taxes, higher interest rates, and liberalized markets and fewer state controls. For example, as stated by the Deputy Prime Minister of Thailand during their financial crisis in late 90s, the deflationary effect of implementation of the IMF's policies was stronger than the IMF predicted. There have also been claims of double standards, in the Asian crisis, as Korean and Indonesian authorities were prevented by the IMF from bailing out their troubled financial institutions and corporations whilst international investors benefited from the IMF's packages and were making the most of the opportunity to buy Asian assets cheaply. Even, there has been some disagreements between the IMF and its sister organization, the World Bank, over the handling of the Asian crisis as well, as the World Bank was very critical of the idea of raising interest rates sharply to prevent further fall of the currencies. That policy is widely believed to be wrong in retrospect.

Having heard these criticisms and considering the responses of the IMF, posted on its website, we found that the common accusation that IMF is favoring big international investors and the top economies when designing and implementing its policies is not well-supported in terms of available impartial facts and statistics. So, in this front, we have not identified clear negative trends in order to be able to come up with solutions. Nevertheless, the following general recommendations are offered for consideration to the IMF's Board of Governors:

- A more humane approach and less aggressive policies in lending to troubled countries which ensure a sustainable development and prosperity for that country.
- The aim of Reduction of Poverty has not had any tangible success and new approaches must be designed and put in place in order to achieve that.
- Targeting development in the IT sector worldwide to narrow down the digital gap currently apparent between the developing countries and the developed ones.

We have some specific recommendations to the IMF which may seem outrageous and unprecedented in the today's modern and market-driven economies, however, there are some interesting rationale behind their propositions:

Although there are some lending facilities at the IMF's disposal to help the economies in crisis, we propose another measure which can be contemplated and that is imposing a cap for exchange rate fluctuations in the order of, for example, 2% weekly. The mechanism by which such a policy could be implemented is not intended to be explored here, but an approach of intervention could be used like the one currently central banks use to affect the exchange rate or a similar approach which market makers use in major exchanges, like NYSE, which is taking up the opposite position in the transactions in case there is an unbalanced flow of buy and sell orders. The rationale behind this is that, if there is a real difference between the current exchange rate and the fundamental equilibrium level, then, this adjustment can take

place over time smoothly. This measure can alleviate the problem of violent and often speculative liquidations of assets and investment transfers. Such measure is not unprecedented in the exact sense of the word, as there exists similar mechanism for the banking industry in the modern economies which ensures the deposits of the customers in case of the default of the financial institution. Example of such state-sponsored bodies is the FDIC in the USA. So, having such a body, acting in the international level, can calm the markets and is not necessarily against the idea of free market economy.

IMF can issue guidelines for setting the interest rates by the central banks, thereby avoiding such differences in the real interest rates between countries. Building Carry Trades [Long positions in high-yield currencies funded by short positions in low-yield currencies] in some countries is potentially hazardous and speculation may lead to disaster and unwinding of the speculative positions can threaten a whole economy.

IMF can eliminate highly-leveraged positions from currency markets which are first to be unwound at first signs of trouble. This unwinding can give enough momentum to the downward spiral which can bring down an economy in very short periods.

IMF can take a more active role in persuading countries to adopt reasonable exchange rate regimes. Although, after the collapse of Bretton Woods system, countries have been free to adopt any exchange rate regime they wish, but, this has led to some major trade problems. Some countries, by holding the value of their currencies artificially low against the major currencies, have boosted their exports and their competitiveness rather unfairly.

These are the results of our analyses of current shortcomings of the IMF and its policies. The authors of this report have sought to come up with some concrete and reasonable suggestions which could improve the health of the global financial system. But, we reiterate the fact that these suggestions are open to question and may even spark some other imbalances and deficiencies in other sectors of the economy. We do acknowledge the hardship that the organization faces in its day-to-day business in drafting new viable policies.

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