

International Monetary Fund (IMF) bailout

Why in news?

Recently Sri Lanka secured a \$3 billion bailout from the International Monetary Fund (IMF) amid the worst economic crisis.

What is IMF?

- **Establishment** - The IMF was established in 1944 in the aftermath of the Great Depression of the 1930s.
- **Aim** - To bring about international economic coordination to prevent competing currency devaluation by countries trying to promote their own exports.
- **Membership** - IMF has 190 countries as its members.
- **Headquarters** - Washington, D.C., United States.
- **Role** - IMF is the last resort lender for countries facing severe economic crises.
- The IMF fosters international financial stability by providing
 - Policy advice
 - Financial assistance
 - Capacity development
- IMF provides financial support to countries hit by crises in order to restore economic stability and growth.
- IMF does not lend for specific projects.
- **Resources of IMF** - IMF funds come from three sources
 - Member quotas
 - Multilateral borrowing agreements
 - Bilateral borrowing agreements

What is the IMF bailout?

- **Bailout** - Means extending support to an entity facing a threat of bankruptcy.
- **Lending** - The IMF lends money countries the form of Special Drawing Rights (SDRs)
 - Special Drawing Rights (SDRs) is a basket of five currencies, US dollar, Euro, Chinese Yuan, Japanese Yen and British Pound
- The bailout can be executed in the form of loans, cash, bonds, or stock purchases.
- **Reasons for bailout** - Countries seek IMF bailouts for the following reasons
 - To resolve macroeconomic risks
 - To solve currency crises
 - To meet external debt obligations
 - To buy essential imports
 - To push the exchange value of their currencies
- **Conditions** - The countries are expected to meet following conditions for the IMF

bailout

- Structural reforms such as fiscal transparency, tax reforms.
- Reforms in state-owned enterprises.
- Reforms in macroeconomic variables like monetary and credit aggregates.
- Reforms in international reserves.
- Reforms in fiscal balances and external borrowing.

What about the crisis in Sri Lanka and Pakistan?

- **Sri Lankan economy crisis** - Sri Lanka witnessed a sharp rise in domestic prices and the exchange value of their currencies plunged.
- Currency crisis are usually the result of mismanagement of the currency by its central bank.
- It is partly contributed to decline of foreign tourists during the Covid-19 pandemic.
- **Pakistan economy crisis** - It is a part of 2022-2023 political unrest in Pakistan.
- The crisis caused severe economic challenges for months due to which food, gas and oil prices have risen.
- **General factors that lead to economic crisis**
 - Inappropriate fiscal and monetary policies
 - Large current account and fiscal deficits
 - High public debt levels
 - Exchange rate fixed at an inappropriate level
 - Weak financial system
 - Political instability and weak institutions

What are the pros and cons of IMF bailout?

| Pros | Cons |
|--|---|
| <ul style="list-style-type: none">• Ensures the survival of a country amid economic turmoil• Ensures that the functioning of essential industries and economic systems• Provide technical expertise to the affected country on how to implement reforms to strengthen the economy and institutions | <ul style="list-style-type: none">• Can result in reduced government spending and higher taxes, measures• Can also create a sense of dependency on external funding• Affects the investing environment in the country |

Quick facts

India and the IMF

- India is a founder 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 been completed on May 2000.

- Finance Minister is the ex-officio Governor on the Board of Governors of the IMF.
- RBI Governor is the Alternate Governor at the IMF.
- 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 has invested SDR 750 million through nine note purchase agreements with the IMF.

Note purchase agreements is usually a temporary bilateral arrangement for an initial period of one year which may be extended by a period of up to two years and the principal of the notes is to be denominated in SDR

References

1. [The Indian Express | IMF Bailout](#)
2. [Department Of Economic Affairs | IMF and India](#)

