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INTERNATIONAL MONETARY FUND

Observations on Its Financial Condition

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Mr. Chairman and Members of the Committee:

I am pleased to be here today to discuss the International Monetary Fund's (IMF) financial operations and financial reporting. As the Congress debates the executive branch's request for about $17.5[1] billion for IMF—about $14.2 billion to recapitalize the organization and about $3.3 billion to expand a credit arrangement from which IMF can borrow—questions have arisen concerning the current level of IMF resources to carry out its operations and the extent to which information is available publicly about IMF's financial condition. To help inform the debate on these and other matters, on June 1, 1998, you asked us to evaluate the adequacy of IMF's public reporting in two areas: (1) its finances and financial condition and (2) its "surveillance" or monitoring of member countries' economies. We have not yet completed our work on these issues; however, as you requested we are prepared today to discuss (1) what resources IMF currently has available to carry out its operations and (2) whether IMF's financial condition can be determined from publicly available information. We expect to report on the other matters addressed in your June 1 request later this fall.

Background

A few important concepts need to be explained when discussing IMF finances. Two of these are members' "quotas" and "currency purchases." Quotas are the membership dues that countries pay when they join IMF.[2] Up to 25 percent of quotas normally must be paid in reserve assets, which are special drawing rights or currencies that are "freely usable" in the principal foreign exchange markets (U.S. dollars, Japanese yen, Deutsche mark, French francs, or pound sterling), and the balance may be paid either in a country's domestic currency or with non-interest-bearing promissory notes.[3] The portion paid in freely usable currency or special drawing rights is referred to as the member's "reserve assets" or "initial

[1]The actual request is for about 13 billion special drawing rights (SDR), which at the time of the request was equivalent to about $18 billion. The SDR is a unit of account that IMF uses to denominate all its transactions. Its value comprises a weighted average of the values of five currencies: Deutsche mark, French franc, Japanese yen, pound sterling, and U.S. dollar. Because the value of the SDR relative to the U.S. dollar changes daily, the dollar value of amounts converted from SDRs also changes daily. For this statement, we used the SDR conversion rate of $1.3382.

[2]Members pay quotas when they initially join IMF and at other times when their quotas are increased.

[3]These promissory notes are made payable to IMF, are denominated in the member's domestic currency, and are held by the member's designated central bank or other designated depository. IMF views these notes as fully equivalent to its currency holdings because IMF can cash these notes on demand within 24 hours to receive members' domestic currency. According to IMF, 137 of its 182 members have opted to substitute promissory notes for part of their currency paid to IMF; these notes comprise about 55 percent of IMF's total currency holdings.

reserve tranche position" and can be drawn on by the member as needed without prior IMF approval. If withdrawn, these amounts are replaced with the country's own currency. Members are not obligated to replenish their reserve tranche positions.

When a country needs additional funds other than from its reserve tranche position, IMF does not loan the funds to the country, per se. Rather, the country "purchases" the currency it needs from IMF with an equivalent amount of its own currency and then later "repurchases" its own currency using SDRs or other currency on terms established by IMF. Because IMF's financial assistance is in the form of currency purchases and repurchases by member countries, the financial assistance does not reduce the combined total of IMF's currency holdings in terms of SDR equivalents. Instead, the composition of IMF's currency holdings changes. For example, the composition of IMF's holdings of member currencies can change when members purchase and repurchase currency. The relationship of IMF's holding of a member's own currency to its quota is an important one, because it can illustrate whether the member is a creditor, debtor, or in a neutral position with IMF. In general, currencies of members who are creditors are considered usable by IMF to finance transactions, while currencies of countries in a neutral borrowing or a debtor position are considered unusable by IMF.

A brief discussion about the accounting standards that IMF uses is also useful. According to the IMF External Audit Committee's (EAC) audit opinion, IMF's financial statements are prepared in accordance with generally accepted accounting principles. However, according to IMF, IMF is not bound by specific legal provisions or accounting principles adopted in the individual member countries. EAC and IMF officials told us that the accounting principles referred to in the EAC's auditor's report are neither U.S. generally accepted accounting principles nor international accounting standards, but are described in a note to the financial statements and do not differ materially from these two.

You also asked us to provide information on the current amount of outstanding IMF credit, including the share of that credit that was borrowed by developing countries. This information is provided in an attachment to my statement.

I would like to emphasize that GAO does not take a position on what action the Congress should take on the executive branch's request. That is a policy decision beyond the scope of our review.

I should also mention that, as you may know, we have no direct audit authority over IMF, as is the case with other international organizations. Nonetheless, working through the Treasury Department and the IMF's U.S. Executive Director's office, IMF has cooperated with our inquiry and provided us information not normally made publicly available.

Summary

IMF has a total of about $195 billion in currency holdings in its general resources account[4] that has been provided through quota subscriptions by its 182 members. However, as of July 20, 1998, IMF estimates that only about $130 billion of these funds represent resources that could be used; that is, are from members that are sufficiently strong economically to permit their currencies to be used for IMF operations. Of this amount, about $70 billion has already been used to finance credit to IMF members and about $17 billion has been committed for their use. Therefore, according to IMF's estimate, only about $43 billion of its $195 billion in currency holdings remain for operations, including lending. Further, IMF and U.S. Treasury Department officials have indicated in public statements that only about $10 billion to $15 billion of the available $43 billion could be used for additional credit to IMF members without leaving IMF seriously short of funds due to IMF's need to maintain certain reserves. These IMF estimates do not take into account the $11.4 billion IMF financing arrangement for Russia that was approved by IMF's Executive Board on July 20. About $2.9 billion of this $11.4 billion will come from IMF's remaining general currency holdings, and IMF will borrow the other $8.5 billion from 11 member governments that participate in the General Arrangements to Borrow (GAB).[5]

IMF's available funds are reported in its annual report; however, the report is released 6 months after IMF's fiscal year ends and, according to IMF and U.S. Treasury officials, is of limited use for decisionmaking purposes. Instead, decisionmaking requires the use of IMF's quarterly operational budgets, which are nonpublic.

[4]IMF's general resources account handles by far the largest share of the transactions between IMF and its membership. The quotas paid by members are contained in this account.

[5]GAB is a borrowing arrangement between IMF and the 11 industrialized countries or their central banks that allows IMF to borrow currencies from these countries under specific conditions and lend the funds either to other GAB countries or to non-GAB IMF member countries.

Amounts and Potential Sources of IMF Funding

IMF has several sources available from which it can potentially obtain funds for use in its operations. The most important of these, according to IMF, are the currency holdings provided through quota subscriptions that underpin most of IMF's operating funds. Other sources include IMF's GAB and other bilateral borrowing arrangements with IMF members. In addition, IMF could potentially borrow from private sources or sell some of its gold holdings. Some of these resources are clearly more accessible than others.

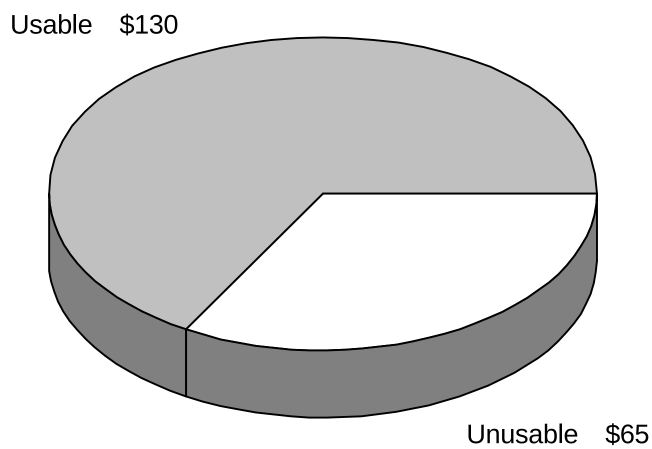
Availability of IMF's Currency Holdings

IMF's determination of available currency holdings, its primary source of readily available funding for carrying out its operations, is based on its judgment concerning the level of usable currency and the level of reserves needed for contingencies. IMF officials have stated that reserves are necessary for two reasons: (1) to maintain sufficient working balances in various currencies to execute foreign exchange transactions and (2) to have available for use in the event that some currencies become unusable and can no longer be used to finance IMF transactions due to a deterioration in members' balance of payments and external reserve positions.

There are several steps involved in calculating the amount of resources IMF has readily available for operations. First, IMF calculates the amount of currency holdings from quotas, which was estimated to be about $195 billion as of July 20, 1998. However, only the currencies of members with sufficiently strong balance of payments and gross external reserve positions are used or usable by IMF for financing its transactions and are included in its operational budget, which is a nonpublic document. Of the $195 billion of currency holdings, IMF estimates that, before taking into consideration IMF extended credit, about $130 billion, or 67 percent, is usable. The remaining $65 billion is unusable. These currencies cannot be used to finance IMF transactions because IMF has determined that the members providing these currencies may be experiencing balance of payment problems or may have drawn on their reserve assets. (See fig. 1.)

Figure 1: IMF's Breakdown of Estimated Usable and Unusable Currencies, July 20, 1998

$195 billion

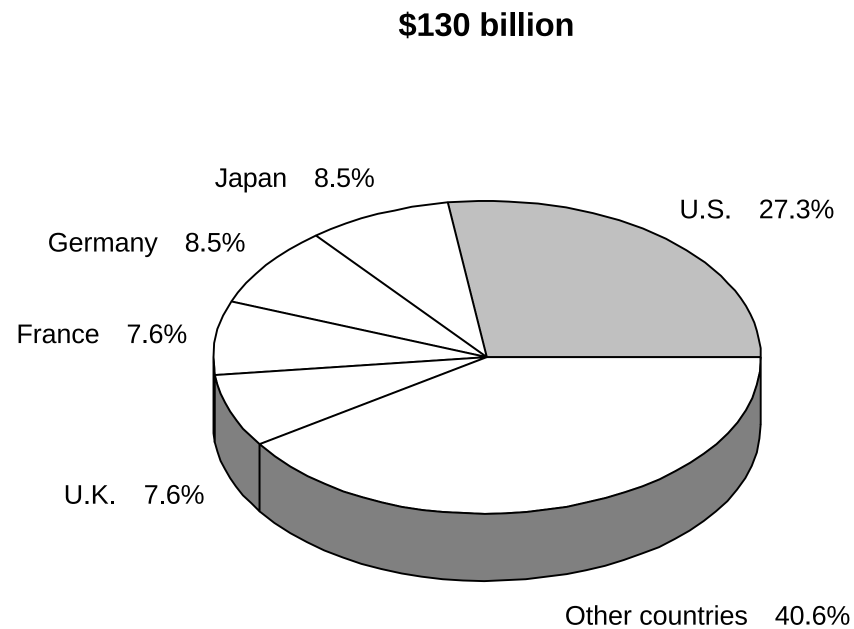


Note: The rate of $1.3382 was used to convert SDR's into U.S. dollars.

Generally, IMF presently considers 30 of its 182 members to have sufficiently strong balance of payments and external reserve positions so that their currencies can be considered usable.[6] As indicated in figure 2, the U.S. share of usable resources is about 27.3 percent.

[6]The level of usable currencies will fluctuate as certain currencies strengthen over time and become part of the operational budget, or countries that were part of the operational budget experience difficulties and, thus, are no longer included as part of the operational budget. In that instance, the entire stock of that country's currency would become unusable.

Figure 2: IMF Member's Estimated Usable Contributions, July 20, 1998



Note: The rate of $1.3382 was used to convert SDR's into U.S. dollars.

Currencies provided from quotas are recorded in IMF's balance sheet as an asset. The distinction between usable and unusable currency is not reported on IMF's balance sheet, but is discussed in its annual report.

As shown in table 1, IMF reduces its total usable currencies of $130 billion by about $70 billion, the amount of its members' currency purchases outstanding, to determine its available usable resources.

Table 1: IMF Available and Uncommitted Resources

U.S. dollars in billions

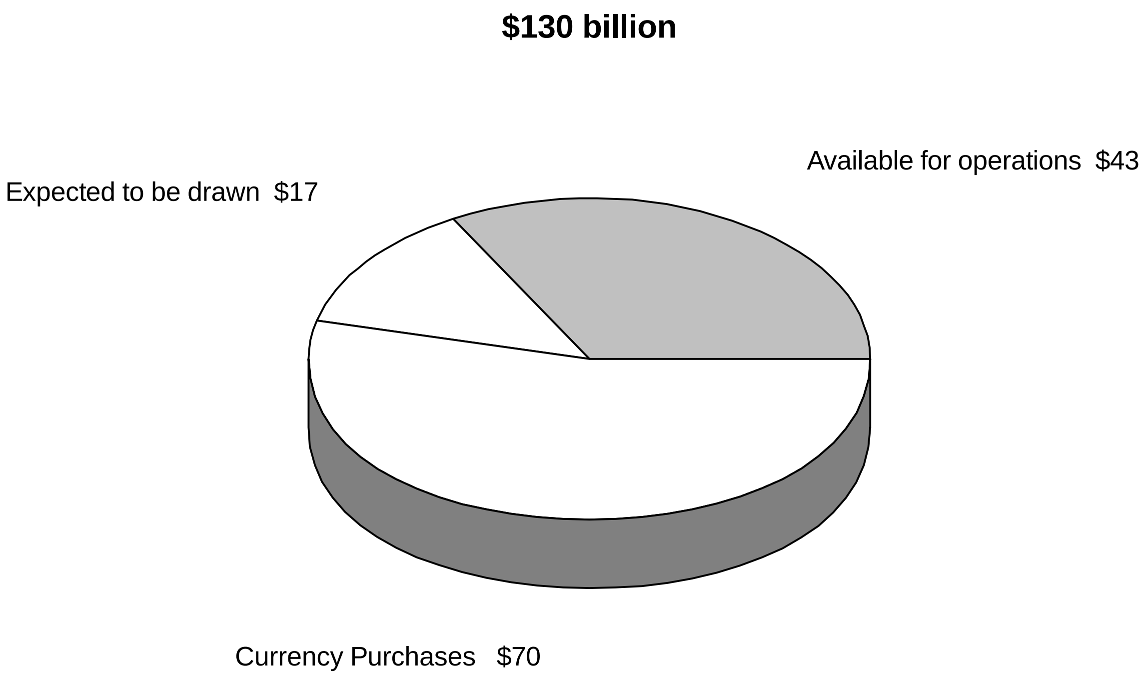
IMF's calculation of available and uncommitted resources	Projected through July 20, 1998
Total usable resources (before IMF extends credit)	$130
less: currency purchases	(70)
Available and usable resources	$60
less: commitments	(17)
Available and uncommitted resources	$43

Note: SDR conversion rate = $1.3382.

Source: IMF.

IMF further reduces its available and usable resources of $60 billion by the amount of the commitments it has made to countries in need of assistance in their balance of payment positions. Estimated undrawn commitments total about $17 billion. After these deductions, IMF's usable currency holdings amounted to about $43 billion as of July 20, 1998. (See fig. 3.) However, IMF adjusts this amount to establish a level of reserves it may need for contingencies.

Figure 3: IMF's Breakdown of Estimated Usable Currencies, July 20, 1998.



Note: The rate of $1.3382 was used to convert SDR's into U.S. dollars.

There has been some discussion about the appropriate level of IMF reserves, the outcome of which may lead to different estimates of the amount available for IMF operations. Table 2 will assist in understanding the two approaches. The results of both approaches have been cited by IMF and Treasury officials in public discussions and have thus led to some confusion about how much currency holdings are really available.[7]

[7]This confusion about IMF available resources was clearly in evidence at a July 13, 1998, press briefing by IMF's First Deputy Managing Director and Treasurer, where the Treasurer, in response to a question regarding the Fund's liquidity, stated: "We have net usable resources of SDR 23.5 billion, say, $31 billion." Question: "What does that mean—we have heard the $10 to $15 billion figure tossed around that currently, the IMF has in lendable resources." Treasurer: "I'm giving you what it would be in lendable resources." Question: "So what would the $10 to $15 billion be?" Treasurer: "That calculation has been made by the U.S. on a slightly different basis." First Deputy Managing Director: "Let me get this straight. We have $44 billion?" Treasurer: "No. At the moment, we have $31 billion." Question: "Where does this $10 to $15 billion figure come from?" Treasurer: "The U.S. Treasury did a calculation that if we came down to 30-percent liquidity ratio, that would leave us with only $10 to $15 billion . . . ."

Table 2: Approaches to Estimating IMF Reserves and Available Resources

U.S. dollars in billions

	Approach 1	Approach 2
Available and uncommitted resources	$43	$43
less: Adjustment factor	(12)	N/A[a]
Available, uncommitted, and adjusted resources	$31	N/A[a]
less: Reserves for creditor countries that may need to draw on reserve assets	[b]	(30-35)
Resources available for operations	$31[c]	$8-$13

Note: SDR conversion rate = $1.3382.

[a]Not applicable to this methodology for estimating the reserve.

[b]According to a high-level IMF official, IMF reserves 30 percent of the reserve tranche positions of members with usable currencies in the event that one or more of these members may—as they have the right to do without prior IMF approval—draw on these positions. This reserve is currently valued at $21 billion. However, this reserve is not included in IMF's operational budget or liquidity reviews, and thus we do not list it in the table.

[c]This does not consider the reserve described in note b.

Source: IMF.

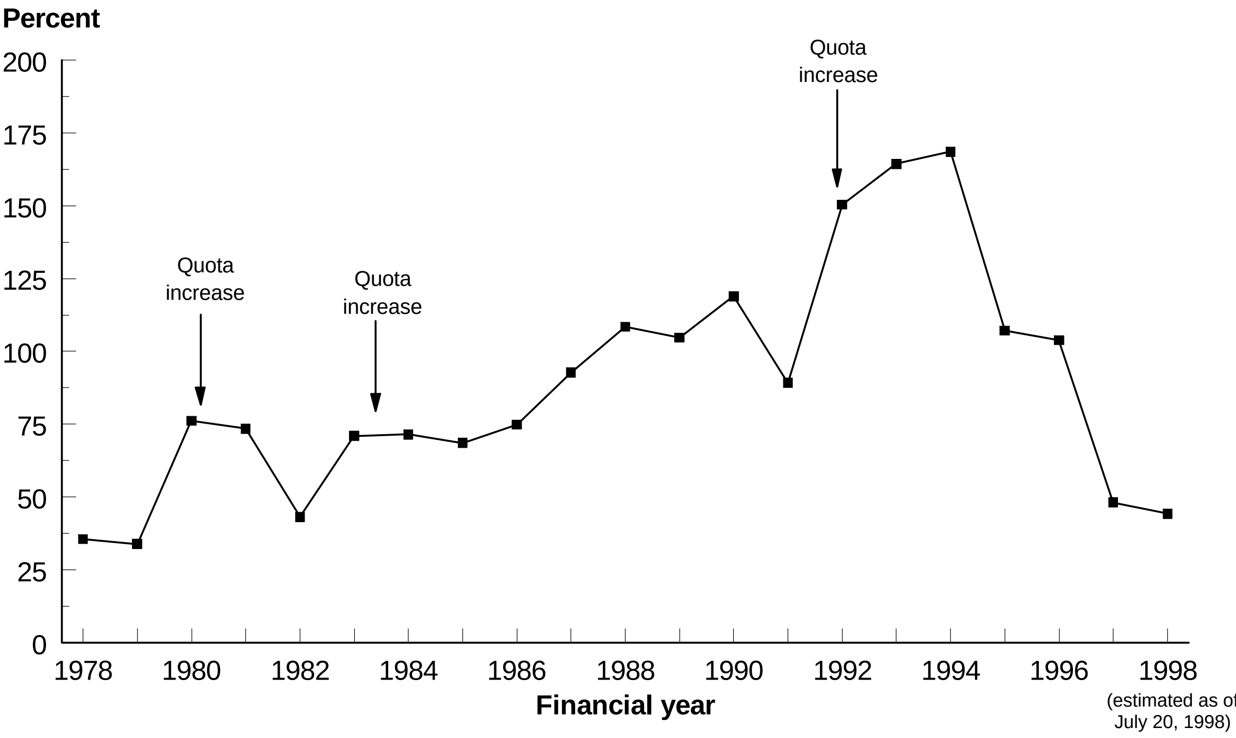
Approach 1 in table 2 is used by IMF to calculate its available resources. Using this method, IMF adjusts its available and uncommitted resources by $12 billion for the establishment of a reserve, as required by the Executive Board. According to IMF documents, this reserve has two components. One component is an adjustment for minimum working balances, which IMF officials stated are needed due to the number and types of currencies it manages to execute its foreign exchange transactions. The second component is a reserve of 10 percent of the quotas of members included in the operational budget for transfers, in case one or more of these countries may encounter balance of payments problems and can no longer provide its currencies as a source of funding for IMF transactions. After this adjustment, IMF would have $31 billion available for operations.

The second approach to estimating IMF's reserve requirements, shown in table 2, is based on the concept of a minimum IMF liquidity ratio.[8] This approach has been used by the U.S. Treasury and endorsed by the IMF's First Deputy Managing Director. As shown in figure 4, as of July 20, 1998, IMF's liquidity ratio was about 44 percent, which is lower than at any time

[8]IMF's "liquidity ratio" is defined as its available, uncommitted, and adjusted resources, which total $31 billion, divided by the total of the member's undrawn reserve assets (about $70 billion) plus outstanding borrowings ($0).

during the last 15 years. This approach considers IMF's historical low liquidity ratio of about 30 percent to be the minimum threshold that could be achieved before it becomes imprudent to lend. In order not to drop below this 30-percent threshold, IMF would have to retain about $30 billion to $35 billion of its $43 billion in usable and uncommitted resources, which would leave only about $8 billion to $13 billion of resources that IMF could use. The $30 billion to $35 billion adjustment represents the possibility that one or more countries providing usable currencies would draw on its reserve tranche position. The amount of IMF resources that should be retained is ultimately a judgment call of IMF's Executive Board. This decision would pinpoint the level below which the Executive Board would consider it imprudent to continue lending.

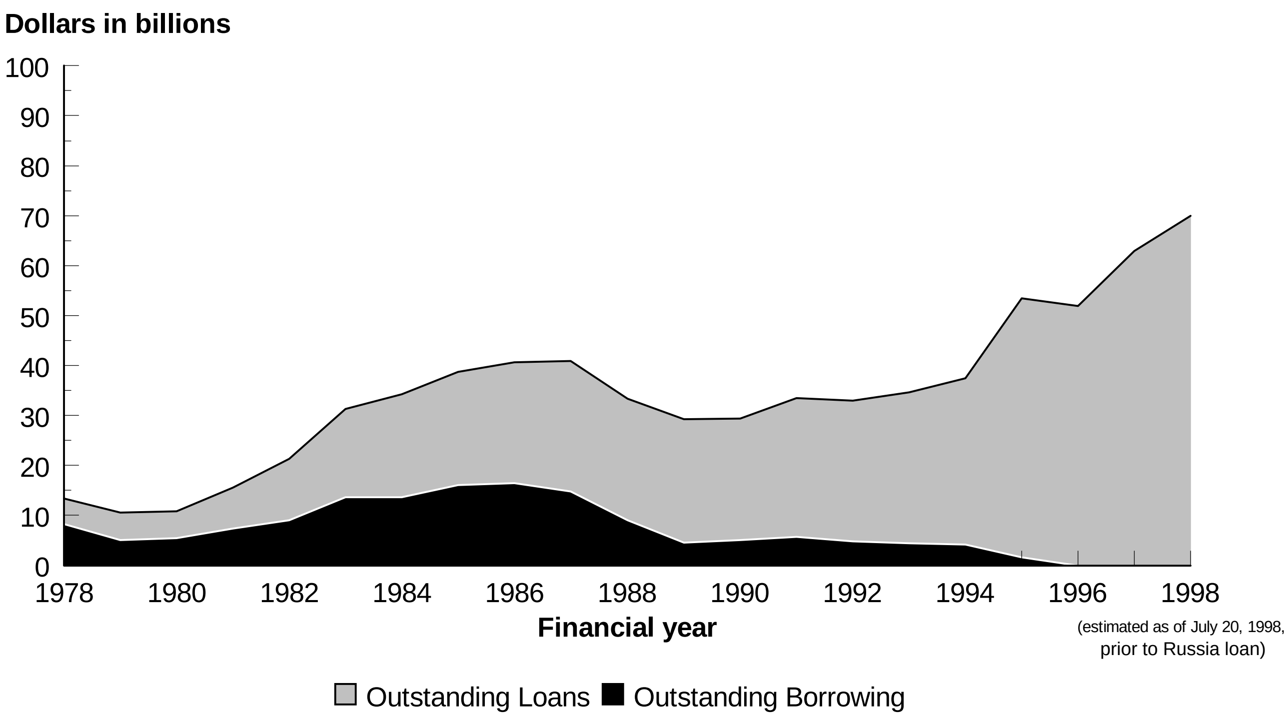
Figure 4: Trends in IMF's Liquidity Ratio, 1978-98



Other Potential Resources Available to IMF

In addition to its permanent, quota-based resources, IMF's Articles of Agreement permit it to borrow funds for use in its operations and transactions. This borrowing may be from any source, public or private.[9] Since 1962, IMF and 11 industrialized countries have maintained standing lines of credit, known as the General Arrangements to Borrow, for IMF to use in emergencies. Before the recent activation of GAB for Russia, GAB was last used by the United States in 1978 when the United States borrowed funds that IMF had borrowed from GAB participants and used them to intervene in world currency markets on behalf of the U.S. dollar. IMF has had other borrowing arrangements over the years, notably during 1979-86. The relative share of borrowed resources used in financing IMF assistance to member countries over the period 1978 through July 20, 1998, is shown in figure 5.

Figure 5: Trends in IMF's Outstanding Assistance and Share Obtained Through Borrowing, 1978-98



IMF also has 103.4 million fine ounces of gold that it could potentially use to fund its operations. IMF has never borrowed funds from private sources.

[9] IMF can borrow funds from nonmembers, but it has no authority to hold currencies of nonmembers.

According to IMF officials, IMF last seriously considered private borrowing in the early 1980s. Table 3 shows these different potential resources.

Table 3: Non-Quota Resources Potentially Available to IMF

U.S. dollars in billions

Potential resources	Potential amount available[a]
General Arrangements to Borrow	$22.7
Special arrangement with Saudi Arabia	2.0
New Arrangements to Borrow (NAB)	22.7[b]
Other Borrowing Authority	[c]
Gold	4.8[d]

[a]Converted from special drawing rights, the unit of account that IMF uses to denominate all of its transactions. The conversion rate used is SDR 1.3382 per dollar.

[b]Approved by IMF's Board of Governors but not yet entered into force.

[c]IMF's Articles of Agreement permit IMF to borrow from any other source, public or private. The Articles of Agreement do not limit the amount of such borrowing.

[d]This figure understates the value of the 103.4 million fine ounces of gold that IMF holds and values at SDR 35 per ounce (about $47 per ounce). IMF estimates that the market value of this gold is about $32 billion. The current market price of gold is about $300 per ounce, but if IMF were to sell some of its gold, it is unclear how much money could be raised because the world price likely would fluctuate as a result of the sale.

Source: IMF.

General Arrangements to Borrow

GAB is a borrowing arrangement between IMF and 11 industrialized countries or their central banks[10] that allows IMF to (1) borrow currencies from these countries under specific conditions and (2) provide funds either to other GAB countries or to non-GAB IMF member countries. A country receiving funds from IMF under GAB is charged the same interest rate as that for standard IMF loans made from regular IMF resources (the SDR interest rate) and is generally required to repay the loan within 5 years. The total of GAB resources is about $22.7 billion, with an additional $2 billion available under a separate agreement with Saudi Arabia. The U.S. share of GAB is about $5.7 billion, or 25 percent of GAB.[11]

[10]The 11 participants in GAB are Belgium, Canada, France, Deutsche Bundesbank (German central bank), Japan, Italy, the Netherlands, Switzerland (Swiss National Bank), Sveriges Riksbank (Swedish central bank), the United Kingdom, and the United States.

[11]The German central bank's share of GAB is $3.2 billion, or 14 percent; Japan's share is about $2.9 billion, or 12.5 percent; and the share of France and the United Kingdom is about $2.3 billion, or 10 percent each. Other country and central bank shares are less.

Activation of GAB requires approval by IMF's Executive Board and GAB participants representing three-fifths of the total credit arrangements and two-thirds of the participants. Therefore, with its 25-percent share of GAB resources, the United States can block GAB activation if it obtains the support of other GAB participants that have credit commitments large enough to reach more than 40 percent of total resource commitments. The criteria for activating GAB are stricter if the funds are for a non-GAB participant than for a GAB participant. The criteria for use by GAB participants is a determination that an "impairment" in the international monetary system exists and IMF should supplement its resources. If GAB funds are to be lent to a non-GAB participant, the criteria are that an "exceptional situation" exists that could threaten "the stability of" the international monetary system and IMF lacks sufficient resources to extend the needed financing. There are no formal criteria for determining the existence of a threat to the international monetary system.

Under the just-concluded expanded financing program for Russia, IMF will borrow about $8.5 billion from GAB members. This decision was based on the determination that an "exceptional situation" exists in the region that could threaten the stability of the international monetary system. All 11 GAB members will participate; each member will lend funds to IMF in proportion to its share of GAB. The United States, with its 25-percent GAB share, will lend IMF about $2.1 billion. Germany, the country with the next-largest share of GAB, will lend IMF about $1.2 billion.[12]

Prior to this use of GAB, over the course of the 36 years that GAB has existed, it has been activated nine times to assist France, Italy, the United Kingdom, and the United States. According to a U.S. Treasury official, GAB was last used in 1978, when the United States drew more than $2.9 billion from its own reserve tranche, including $994 million in funds from loans under GAB and more than $1.9 billion from IMF currency holdings. According to the Treasury official, at that time, the United States needed to purchase yen and Deutsche marks in quantities greater than IMF possessed in order to use the currencies to help stabilize the U.S. dollar's exchange rate. Consequently, IMF borrowed the currencies from Japan and Germany under GAB and sold them to the United States.[13] Prior to GAB use for Russia, no IMF-member country that was not a GAB participant had used GAB, although such countries had been eligible to use GAB since 1983. GAB

[12]The associated arrangement to GAB between IMF and Saudi Arabia will not be activated for Russia.

[13]Other funds were also used then to help stabilize the dollar, including funds from gold sales and special financial instruments issued in foreign currencies.

was not used to assist Mexico in its 1994-95 financial crisis nor to help Asian countries in their current financial crises.

New Arrangements to Borrow

In January 1997, following an agreement by the Group of Ten (G-10) countries[14] to expand the size and membership of GAB, IMF's Executive Board voted to create the New Arrangements to Borrow. NAB would not replace GAB, which will remain in force; however, NAB would be the facility of first recourse in the event of a need to provide supplementary resources to IMF. The decision to create NAB grew out of concern following Mexico's financial crisis of 1994-95 that substantially more resources might be needed to respond to future sovereign financial crises. Under NAB, the number of participating countries will be increased to 25, and the total amount of credit available in NAB will be up to about $45.5 billion, which is composed of the $22.7 billion available under GAB and an additional $22.7 billion for NAB. NAB could be activated when participants representing 80 percent of the credit lines' resources determine that there is a threat to the international financial system. This could make it more difficult to use NAB than GAB, since GAB requires only a 60-percent approval for activation. As you know, NAB has not yet entered into force.

Other Borrowing Arrangements

In the past, IMF has borrowed funds from official sources other than through GAB. The largest such borrowing arrangements were in 1979 and 1981. In 1979 IMF concluded a series of borrowing agreements with a group of 14 industrial and oil exporting countries to finance IMF's supplementary financing facility, which was designed to assist members whose balance of payments deficits were large in relation to their quotas. In 1981, due to the continued high demand for IMF financing, IMF concluded individual borrowing agreements with various central banks and the Bank for International Settlements.[15] The 1979 and 1981 borrowing arrangements totaled SDR 23.1 billion (roughly $31 billion at today's dollar/SDR exchange rate). IMF's most recent bilateral borrowing arrangement was a SDR 3 billion arrangement with Japan in 1986. At one point, in 1985, IMF borrowings from member governments (under all borrowing arrangements) equalled almost 42 percent of outstanding IMF credit (loans).

[14]The G-10 consists of 11 major industrialized countries that consult on general economic and financial matters. The 11 countries are: Belgium, Canada, France, Germany, Italy, Japan, the Netherlands, Sweden, Switzerland, the United Kingdom, and the United States.

[15]BIS is an organization of central banks that is based in Basle, Switzerland. It is the principal forum for consultation, cooperation, and information exchange among central bankers.

According to a U.S. Treasury official, the option to borrow funds from private sources was last seriously considered in the early 1980s. According to an IMF official, the IMF's structure is based on cooperation with its members, and that is what it considers to be its source of financing. According to a U.S. Treasury Department official, IMF decided not to borrow from private capital markets in the early 1980s for a number of reasons. First, it was believed that the cooperative nature of the institution might be undermined were IMF to begin relying on private sources, rather than its membership, to fund its operations. Also, there was a concern about the consequences of having IMF, which seeks to stabilize international capital markets, rely on those markets for its funding. And, there was uncertainty about whether IMF could have borrowed the amount of funds it needed from private markets quickly enough to employ them as needed.

IMF's Gold Holdings

IMF also has gold holdings that some have suggested it could potentially use to fund its operations. Currently it holds about 103.4 million fine ounces of gold at designated depositories in four member countries.[16] IMF acquired most of its gold prior to 1978, when IMF's Articles of Agreement required that in most cases 25 percent of members' quota subscriptions be paid in gold and transactions between member countries and IMF normally be conducted in gold.

IMF values its gold at SDR 35 per ounce (about $47 per ounce),[17] the original cost at which the gold was acquired. Therefore, IMF's gold holdings are valued on IMF's balance sheet at SDR 3.6 billion (about $4.8 billion). However, IMF estimates and makes public as a note to its balance sheet the current market value of its gold holdings based on the market price. In April 1998 IMF estimated its gold was worth about $32 billion. Were IMF to decide to sell some of its gold, it is unclear how much money could be raised because the world price likely would be affected as a result of the sale.

The regular use of gold in IMF transactions ended in 1978, when IMF's Articles of Agreement were amended to reflect the end of the fixed currency exchange rate system that had governed the international financial system up to that time. Under its amended articles, IMF may sell gold outright on the basis of market prices and may accept gold in the

[16]The member countries are France, India, the United States, and the United Kingdom. These gold holdings represented about 9.6 percent of world gold holdings in March 1998.

[17]Except for a small amount (21,396 ounces) that a member government gave to IMF in December 1992 in partial settlement of an overdue loan obligation. IMF values this amount at SDR 5.1 million (about $6.8 million currently).

discharge of a member's obligations to IMF at an agreed price on the basis of market prices at the time of acceptance. IMF's General Counsel told us that IMF does not have authority to engage in any other gold transactions—including loans, leases, or use of gold as collateral—because these uses are not expressly allowed under IMF articles.

Although IMF may sell gold to raise funds, it does not regard gold holdings to be a liquid asset and, therefore, does not consider gold to be a liquid resource for lending purposes. According to IMF documents and IMF officials, the principal reason for not considering gold to be a liquid asset is that IMF's Articles of Agreement require that any sale of gold be approved by IMF's Board of Governors by an 85-percent majority of total voting power. Thus, any group of countries that holds more than 15 percent of IMF's voting power could prevent a gold sale. For instance, the United States, which has nearly an 18-percent share of IMF's voting power, could unilaterally block a gold sale.[18]

In 1995, IMF's Executive Board adopted a policy on gold. The policy contained these principles:

- As an undervalued asset held by IMF, gold provides a fundamental strength to IMF's balance sheet. Any mobilization of IMF's gold should avoid weakening IMF's overall financial position.
- IMF should continue to hold a relatively large amount of gold among its assets, not only for prudential reasons, but also to meet unforeseen contingencies.
- IMF has a systemic responsibility to avoid causing disruptions to the functioning of the gold market.
- The profits from any sales of gold should be retained and only the income deriving from the investment of those profits used for any operations that might be agreed.

[18]Under U.S. law, the executive branch may not approve IMF dispositions of gold over 25 million ounces benefitting individual IMF member countries or particular segments of IMF membership unless the Congress by law authorizes the disposition (22 U.S.C. 286c). According to a U.S. Treasury official, because 25 million ounces of IMF gold were sold between 1976 and 1980 for the benefit of a particular segment of IMF membership, any further sale of gold for the benefit of a particular segment of IMF membership requires statutory approval.

Extent of Public Disclosure of IMF's Financial Condition

As I have already indicated, it is not possible in a timely manner to determine from publicly available sources what resources IMF has available for operations. Information on the availability of and actual use of IMF's resources is regularly provided to its members, including the U.S. Treasury, in quarterly operational budgets and periodic liquidity reviews prepared by IMF staff. These documents provide considerable detail about IMF's financial condition. For example, the operational budget specifies the amounts of usable currencies to be used in purchases, repurchases, and other IMF financial transactions expected to take place during that period. The liquidity reviews provide information on developments affecting IMF's liquidity, 2-year projections of the use of IMF's resources, and trends in IMF liquidity estimates. However, these documents are not publicly available. According to IMF, these documents contain information that could be market sensitive because they include judgment calls about which members' currencies are strong or weak.

IMF's publicly available quarterly and annual financial statements do not disclose the amount of usable currencies, although this is reported in IMF's annual report. The amount of usable currencies and the commitments IMF is likely to make can be determined using additional nonpublic documents. The publicly available financial statements do not show the adjustment factors that IMF uses to estimate its liquidity.

IMF and U.S. Treasury officials told us that few people outside of IMF use or rely on IMF's public financial statements for information about IMF's financial condition or liquidity, and IMF and Treasury officials indicated that most potential users of financial statements do not consider them to be very useful for decisionmaking purposes. Moreover, according to private sector investment analysts we spoke with, the financial markets are more interested in information IMF has about individual country programs and information in its International Financial Statistics.

Audits of IMF's Financial Statements

IMF's financial statements are audited annually and, according to IMF officials, have received "clean," or unqualified audit opinions from the EAC. We have not reviewed the audit work supporting the opinions or assessed the independence of the EAC. The EAC consists of three people who are nominated by IMF members and are approved by the Executive Board to serve 1-year terms. At least one person has to be nominated by one of the six largest quota holders of IMF (United States, Germany, Japan, the United Kingdom, France, and Saudi Arabia). Of the three members, a chairman is selected at the end of the 1 year term to serve an additional year. The EAC reports to IMF's Managing Director and to the Executive Board.

To enable the EAC to express an opinion on whether IMF's financial statements present fairly the Fund's financial position and results of operations, the EAC relies on an audit by a certified public accounting (CPA) firm—which is selected by the Managing Director. The CPA firm issues an advisory letter to the EAC that contains the CPA firm's opinion on the financial statements. The EAC discusses the audit with the CPA firm and reviews its work papers, and then the EAC issues an audit opinion on IMF's financial statements. If the EAC has any audit issues or recommendations for improvements, it issues its views and suggestions to the Managing Director and the Executive Board. Again, we have not tested the work of the EAC and cannot comment on the reasonableness of its audit opinion. The IMF has commissioned a study of its internal audit and evaluation function and how it obtains its external audit, and expects to have a report on these matters in September 1998.

Mr. Chairman, this concludes my prepared statement. I will be happy to answer any questions you or other Members may have.

The International Monetary Fund's Current Lending

You asked us to provide information on IMF's current lending. Figure I shows members' currency purchases outstanding from IMF's general resources account (GRA) as of May 31, 1998.[1] As the figure shows, IMF had about $70 billion in outstanding loans at that time. About $48.4 billion, or 70 percent, of these loans went to developing countries, and the other $20.3 billion, or 30 percent, had been borrowed by countries in transition.[2] No industrial countries had outstanding borrowings from IMF at that time.[3] Figure I does not include about $8.4 billion of outstanding loans from non-GRA IMF lending facilities.[4]

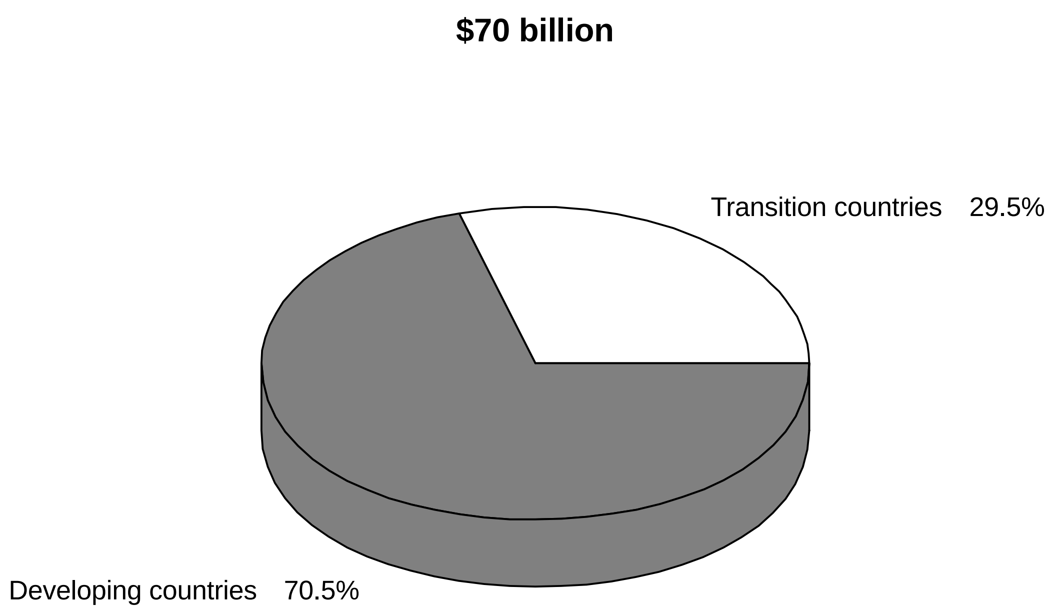
[1]IMF financing is not transacted in the form of loans. When a country borrows from IMF, it "purchases" the currency it needs from IMF with an equivalent amount of its own currency and then "repurchases" its own currency later using special drawing rights (SDR) or other currency on terms established by IMF. The SDR is a unit of account that IMF uses to denominate all its transactions. Its value comprises a weighted average of the values of five currencies: deutsche mark, French franc, Japanese yen, pound sterling, and U.S. dollar.

[2]IMF considers 130 member countries to be developing countries and 28 member countries to be countries in transition (that is, countries that either comprised the former Soviet Union or Soviet-dominated Eastern or Central Europe).

[3]IMF considers 24 members to be industrialized countries: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Japan, Luxembourg, the Netherlands, New Zealand, Norway, Portugal, San Marino, Spain, Sweden, Switzerland, the United Kingdom, and the United States.

[4]Much of this lending was on concessional (below market interest rate) terms to the poorest IMF member countries.

Figure 1.1: IMF's Estimated Currency Purchases, May 31, 1998



Note: Figures include purchases from the general resources account only. The May 31, 1998, rate of $1.33536 was used to convert SDR's into U.S. dollars.

Normal Limits to Borrowing From IMF

The amount of funds that a member country may borrow from IMF is typically limited to a certain percentage of that member's quota.[5] This is true both for individual financing programs and for the total amount of funds that a member can borrow from IMF. Current rules governing use of IMF's general resources account permit an IMF member to borrow an amount equal to 100 percent of its quota per year, with a cumulative limit of 300 percent, unless exceptional circumstances permit. These limits exclude drawings under "special facilities," such as the concessional (below market interest rate) Enhanced Structural Adjustment Facility. These limits were last changed in 1994, when the yearly limit on borrowing was increased from 68 percent of quota to 100 percent.

In the past 3 years, IMF has provided financing to a number of large developing countries that have experienced financial crises. IMF's financial assistance to Mexico in 1995 and its 1997-98 financing programs for

[5]Quotas are the membership dues that countries pay when they join IMF. In addition to determining access to IMF resources, a member's quota determines its voting power in IMF and is the basis for determining its share in the allocation of SDRs to IMF members.

Thailand, Indonesia, and Korea all were well in excess of the normal limit on cumulative borrowing. Mexico's 1995 assistance program from IMF amounted to 688 percent of its quota. Thailand's July 1997 financing arrangement with IMF was about $3.9 billion, or about 500 percent of its quota. Indonesia's November 1997 IMF financing arrangement for about $10.1 billion, which was augmented by an additional $1.3 billion on July 15, 1998, now totals about 557 percent of its quota. Korea's December 1997 program of about $21 billion was equivalent to about 1,940 percent of its quota.

Charges on IMF Currency Purchases

A member borrowing funds from IMF pays various charges to cover IMF's operational expenses, including compensation paid to the member whose currency it is borrowing. Presently, a borrower typically pays in service charges and commitment fees about one-half of 1 percent of the amount borrowed and in interest charges about 4.6 percent. This 4.6 percent is the SDR interest rate[6] (about 4.3 percent, as of July 20, 1998) plus an amount that is designed to allow IMF to meet its annual administrative expenses, cover any overdue finance charges that members have not yet paid, and compensate members whose currencies have been purchased by other IMF members.

[6]The SDR interest rate is determined by reference to a combined market interest rate, which is a weighted average of yields or rates of short-term instruments in the capital markets of the five members whose currencies comprise the SDR.

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