CURRENCY MANIPULATIONS AND INTERNATIONAL TRADE LAW: AN OVERVIEW OF THE EXISTING IMF LEGAL REGIME

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I. INTRODUCTION

As per the principles of Law of Contract, trade or business is a process of enrichment for the participants in the agreement. In order to ensure a flourishing economy it remains imperative to adopt a good economic Laws & policies for all the participants of the trade. A good economic policy, which includes a good currency culture, ensures not only prosperity within the economy but also ensures peace and stability in the world. It is not a surprise that the preamble part of the World Trade Organization stresses upon the trade and economic endeavors which infuses stability and sustainable development. The Preamble part of the WTO rules (i.e. Marrakesh Agreement Establishing the World Trade Organization) provides for recognizing relations in the field of trade and economic endeavor should be conducted with a view to raising standards of living, ensuring full employment and a large and steadily growing volume of real income and effective demand, and expanding the production of and trade in goods and services, while allowing for the optimal use of the world's resources in accordance with the objective of sustainable development, seeking both to protect and preserve the environment and to enhance the means for doing so in a manner consistent with their respective needs and concerns at different levels of economic development.[1]

II. INTERNATIONAL TRADE LAW AND CURRENCY MANIPULATIONS

The experience has shown that no economic policy can achieve a prosperous international trade system without controlling the currency manipulations as money is the media of all the trade and business. It has been estimated that the currency manipulators affect the flow of currency about $1.5 trillion per year. Historically, there have been numerous cases of currency devaluation by Countries and even currency wars[2] in order to gain unfair trade advantages. The most notable point over here, though there have many complaints regarding the currency manipulations in the international trade arena though not even one country has been declared as a manipulator by the International Monitory Fund. Hence, in order to infuse an ideal international trade legal

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[1] Preamble, Marrakesh Agreement Establishing the World Trade Organization

[2] Most notable case of currency devaluation during the great depression 1930s when the major economies had abandoned the gold standard and for the purpose of getting economic advantages they resorted to competitive devaluation.

regime there is a crying need to investigate the issue of currency devaluation along with its potential and real impact on the international trade.

III. WHAT IS A CURRENCY MANIPULATION?

The case of currency manipulations occur when a government adopts a policy to devalue its currency to gain an unfair trade advantage over others in international trade market. The value of currency under the floating exchange rate reflects a confluence of various demand and supply factors in a currency market (in other words, like any other commodity the value of the currency is decided by the demand and supply factors in the currency market). The major factors which affect the value of the currency (in floating exchange rate regime) in the international market are current account balance, inflation rate, interest rate etc. Because of the interaction between the various demand and supply factors the currency of any country attains the 'equilibrium value' which is the actual value of the currency. When a government through various instrumentations disturbs this equilibrium value in its favour (to gain an unfair advantage in trade) this situation is known as 'currency manipulation'.

The equilibrium value of the currency may be disturbed by the acts of government or private players. To depreciate its currency the government may sell out its own currency and buy the foreign currency. On the other hand for the purpose of appreciating its currency the government may sell the foreign financial assets, like bonds, bank deposits (which are generally officially kept as reserve by the government).

In the appreciation or depreciation of the currency there is the role of private players also. For example the FIIs might be lured to invest in the country where they can get higher rate of return.[3] Though with regard to the currency manipulations the role of the government is more important as it can control the conduct of the private parties too and at the same time it can influence various capital control measures such as taxes or other regulatory restriction for the purpose of the private capital inflows and outflows. It should be noted that such measures (for devaluation of currency) will not give rise to a case of currency manipulation if it has been done in order to achieve a domestic financial stability. It is the mandate of the IMF which is the reflection of the generally universally acceptable norms of currency and exchange.

IV. CURRENCY MANIPULATIONS AND ARTICLES OF AGREEMENT (IMF): LEGAL MANDATES OF ARTICLE IV OF IMF

The Article IV of the Articles of Agreement, International Monetary Fund deals with the issue of currency manipulations. It provides the general as well as four specific obligations for the parties. The general obligations of the parties as provided under Article IV recognizing that the essential purpose of the international monetary system is to provide a framework that facilitates the exchange of goods, services, and capital among countries, and that sustains sound economic growth, and that a principal objective is the continuing development of the orderly underlying conditions that are necessary for financial and economic stability, each member undertakes to collaborate with the Fund and other members to assure orderly exchange arrangements and to

[3] This was a major reason of devaluation of rupee in August, 2013 in India as the Indian market is deeply dependent upon the foreign institutional investors.

promote a stable system of exchange rates".[4]

The Article IV of the IMF can be conveniently divided into three parts Preamble, General Obligations and Specific Obligations.[5] The Preamble part (or even the Section 1 of the Article) is not obligatory in nature. It merely provides the essential guidelines which are to be observed by the member nations while doing the trade with each other.[6] The general obligation of the member is to collaborate with the fund and other members so that a goal of stable and orderly exchange rate in the world could be achieved. At the same time the International Monetary Fund provides the following four specific obligations:[7]

a) Endeavour to direct its economic and financial policies towards the objective of fostering orderly economic growth with reasonable price stability, with due regard to its circumstances;
b) Seek to promote stability by fostering orderly underlying economic and financial conditions and a monetary system that does not tend to produce erratic disruptions;
c) Avoid manipulating exchange rates or the international monetary system in order to prevent effective balance of payments adjustment or to gain an unfair competitive advantage over other members; and
d) Follow exchange rate policies compatible with the undertakings under this Section.

The phrase "In particular, each member shall:" in Article IV links the general obligations of the members with the particular obligations. The phrase also indicates that the list of four specific obligations is not exhaustive and the general obligations are broader than the specific obligations.

Legal Remedies for Currency Manipulations

Currency manipulation has a very wide impact upon the international trade. The IMF regime provides the checks and balances over the exchange rate of any currency for the purpose of regulating the instances of currency manipulations. Section 2 of the IMF mandates the member nation to notify any changes in its exchange arrangements. Section 2 provides that each member shall notify the Fund, within thirty days after the date of the second amendment of this Agreement, of the exchange arrangements it intends to apply in fulfillment of its obligations under Section 1 of this Article, and shall notify the Fund promptly of any changes in its exchange arrangements. Further, Article IV, Section 1(iii) mandates that each member shall avoid

manipulating exchange rates or the international monetary system in order to prevent effective balance of payments adjustment or to gain an unfair competitive advantage over other members.

Hence, the Fund mandates the members to not to resort to any manipulative exchange rate. But at the same time it does not provide any guideline about the acts which

[4]Section 1 of Article IV, Articles of Agreements, IMF.

[5]*See Also*, IMF, Article IV of the Fund's Articles of Agreement: An Overview of the Legal Framework, at 7, Legal Department, In consultation with the Policy Development and Review Department (2006)

[6]The relevant part of the Preamble provides, ´Recognizing that the essential purpose of the international monetary system is to provide a framework that facilitates the exchange of goods, services, and capital among countries, and that sustains sound economic growth, and that a principal objective is the continuing development of the orderly underlying conditions that are necessary for financial and economic stability….."

[7]Section 1 of Article IV, Articles of Agreements, IMF.

constitute the manipulative policies. Further it does not provide any remedy in case any member nation adopts any manipulative exchange rate policy. Although for the purpose of ensuring compliance the Fund has the provisions of surveillance which are commenced on routine basis.

Fund Surveillance

The Fund surveillance is also known as Article IV consultation. Under Article IV of the IMF, Section 3 (a), the Fund is duty bound to ensure compliance from the member nation and the member nations are also bound to abide by the rules provided by the IMF under Articles IV of the Articles of Agreement. For the purpose of ensuring compliance under Section 3, of Article IV, the IMF has the right to institute a process of surveillance. In the process of surveillance the IMF supervises and even advises the member nations over its exchange rate policies [under Section 3 (b) of IMF]. The Section 3 (b) of Article IV, Articles of Agreement, International Monetary Fund provides in order to fulfill its functions under (a) above, the Fund shall exercise firm surveillance over the exchange rate policies of members, and shall adopt specific principles for the guidance of all members with respect to those policies. Each member shall provide the Fund with the information necessary for such surveillance, and, when requested by the Fund, shall consult with it on the member's exchange rate policies. The principles adopted by the Fund shall be consistent with cooperative arrangements by which members maintain the value of their currencies in relation to the value of the currency or currencies of other members, as well as with other exchange arrangements of a member's choice consistent with the purposes of the Fund and Section 1 of this Article. These principles shall respect the domestic social and political policies of members, and in applying these principles the Fund shall pay due regard to the circumstances of members.

The surveillance is undertaken by the IMF may be bilateral or multilateral (or integrated surveillance). Under the bilateral surveillance the staffs of IMF visit the concerned member nation and collect information about the macroeconomic policy of the country such as fiscal policy, exchange rate, soundness of economy etc. A report is prepared by the IMF mission and its summary is referred to the executive board for its discussions. If the member nation is agreed with the report the findings and observation in such report is adopted and its summary is published. While preparing the report the socio-economic-political situations are also taken into account.

V. CONCLUSION

After having discussed the IMF provisions, a natural corollary can be drawn that the existing IMF regime is not sufficient to deal with the currency manipulations cases. The present IMF regime does not provide the remedies or dispute settlement mechanism for the currency manipulations cases. It is not a surprise that there have been so many instances of selfish exchange rate policies and currency manipulations cases but till date IMF has not declared any country as the currency manipulator. The reason behind it that the IMF provisions seem vague in nature with regard to the currency manipulations and it is moreover reduced merely to a soft law. Even though IMF provides some mandatory provisions regarding compliance but it has no dispute settlement mechanism. Some respite in the form of dispute settlement mechanism is provided by WTO but it remains to investigate whether WTO has any role to play at all in the cases of currency manipulations and the policy makers are badly divided on this issue in the world over.