

DOCUMENT OF INTERNATIONAL MONETARY FUND
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**IMMEDIATE
ATTENTION**

EBS/83/94
Supplement 3

CONFIDENTIAL

July 26, 1983

To: Members of the Executive Board

From: The Secretary

Subject: Experience with the 1975 Oil Facility Subsidy Account

It is not proposed to bring the attached memorandum on the Fund's experience with the 1975 oil facility subsidy account to the agenda of the Executive Board for discussion unless an Executive Director so requests by the close of business on Tuesday, August 2, 1983. In the absence of such a request, the draft decision that appears on page 7 will be deemed approved by the Executive Board and it will be so recorded in the minutes of the next meeting thereafter.

Att: (1)

INTERNATIONAL MONETARY FUND

Experience with the 1975 Oil Facility Subsidy Account

Prepared by the Treasurer's Department

(In consultation with the Legal Department)

Approved by W.O. Habermeler

July 25, 1983

As requested by Executive Directors at EBM/83/82, (June 8, 1983), this memorandum provides a brief review of the Fund's experience with the 1975 Oil Facility Subsidy Account. Section I deals with the financial resources of the Account and discusses the extent to which financial assistance was provided through the Account to eligible beneficiaries. The final section deals with the disposition of remaining resources in the account and with its termination in accordance with the understanding reached at EBM/83/82.

I. Financial Resources of the 1975
Oil Facility Subsidy Account

1. Establishment of account

The Oil Facility Subsidy Account was established in August 1975 "to assist those members that are most seriously affected by the current situation to meet the cost of using resources made available through the Fund's Oil Facility for 1975." ^{1/}

The intention of the Subsidy Account was "to reduce the effective rate of annual charge payable on drawings...[under the 1975 Oil Facility]...by about 5 percent per annum depending upon the amounts contributed." ^{2/} When the establishment of the Subsidy Account was first discussed, the list of most seriously affected (MSA) countries in February 1975, as classified by the U.N. Emergency Operation, contained 33 Fund members (later increased to 39 members) and these countries were regarded as potentially eligible for maximum access to the 1975 Oil Facility for SDR 1.35 billion. On these considerations, the total cost of the subsidy over the life of the Facility would amount to approximately SDR 350 million. It was also assumed that some contributions would be paid in advance and these advance payments

^{1/} Executive Board Decision No. 4773-(75/131), adopted August 1, 1975.

^{2/} "A Subsidy Account for the Most Seriously Affected Countries Drawing under the 1975 Oil Facility," (SM/75/40, 2/10/75), p.1.

would be temporarily invested--e.g., if all contributions were paid in advance and invested at a rate of return of 6 percent, as then assumed by the staff, contributions could be reduced by about 14 percent from the SDR 350 million assumed to be needed. It was recognized, however, that because of many uncertainties about the timing of the contributions, the importance of the investment income should not be overstated, especially in the earlier years of the Account.

2. Financial resources

a. Contributions

As noted above, it was assumed that the needs of the Subsidy Account could be expected to be of the order of SDR 350 million to pay a subsidy of about 5 percent per annum on drawings of SDR 1.35 billion. By mid-1976, i.e., before the first subsidy was paid, it was clear, on the basis of responses received from potential donors, that contributions were unlikely to exceed SDR 160 million.

Of the 36 members and Switzerland that were requested by the Managing Director to make contributions, 25 countries responded positively (Appendix Table 1). Some of these members indicated that they would contribute only smaller amounts than had been suggested by the staff in view of domestic budget difficulties and, in some cases, because contributions to the Subsidy Account were to be financed out of a member's overseas aid budget which had already been agreed in total; some members determined the size of their contributions in the light of other members' contributions. A number of members, however, indicated the amount of their contributions to the Subsidy Account only after the needs of the Account could be fully ascertained--i.e., after the last drawings had occurred under the 1975 Oil Facility in May 1976--and after it had become clear that the Account would not need as much as SDR 350 million to pay subsidies on the outstanding purchases under the Oil Facility.

b. Investment income

As shown in Appendix Table 2, total contributions received over the life of the Account amounted to SDR 160.3 million. Some members, e.g., Austria, Canada, Italy, Luxembourg, the Netherlands and Switzerland paid their contributions in a single installment early after the establishment of the Account. Most other countries made their contributions in two or four installments and seven members made their contributions in seven equal annual installments, the last being received in 1982/83. The undisbursed balances held in the Subsidy Account were invested in short-term U.S. Government obligations (Appendix Table 3). The investments were normally for one year maturity and held to maturity; for very short periods, usually immediately preceding disbursements, the balances needed for paying the subsidy were invested in overnight repurchase agreements with the Federal Reserve Bank of New York. Taking the life of the Account as a

whole, i.e., from August 1, 1975 to June 30, 1983, interest earned on investments amounted to SDR 23.9 million representing an average effective yield on investments of 8.7 percent per annum.

c. Valuation gains (losses)

The accounts of the Subsidy Account are expressed in terms of the SDR. The contributions to the Subsidy Account were received in currency and converted to equivalent amounts of SDRs on the basis of exchange rates against the SDR at the time of receipt. However, the investments were held in U.S. dollar-denominated assets and as a consequence valuation gains and losses occurred when these investments were expressed in terms of the SDR. Taking the whole period of operation of the Subsidy Account, changes in the SDR/US\$ exchange rate resulted in net valuation gains of SDR 2.3 million.

3. Beneficiaries and use of 1975 Oil Facility

As noted earlier, the original beneficiaries eligible to receive subsidies from the Account were limited to 39 Fund members that were included in the United Nations' list of countries most seriously affected by the increased price of oil (Appendix Table 4). Of these 39 members, 18 used the resources made available through the 1975 Oil Facility for an amount totalling SDR 551.04 million. This amount of use of the 1975 Oil Facility was about 41 percent of the expected maximum estimated by the staff at the time the Account was being established. (In this regard, it is noteworthy that contributions to the Subsidy Account of approximately SDR 160 million amounted to approximately 46 percent of the original anticipated amount of SDR 350 million.)

In May 1977, some Executive Directors proposed to expand the list of beneficiaries of the Subsidy Account to include those members that were eligible to receive concessional financial assistance from the Trust Fund as developing countries with low per capita incomes. Seven such countries ^{1/} had not been included in the Subsidy Account arrangements either because they were not members of the Fund when the Account was established or were not listed by the U.N. as most seriously affected countries. The donors to the Subsidy Account endorsed the inclusion of the seven members in the list of beneficiaries. It was also agreed that benefits to them from the Subsidy Account would be made "only after provision is made for all present beneficiaries to receive a subsidy of 5 per cent per annum of all balances subject to changes under the 1975 Oil Facility." ^{2/} With these additions, it was understood that no further extension of the list of beneficiaries would

^{1/} Grenada, Malawi, Morocco, Papua New Guinea, the Philippines, Zambia, and Zaire.

^{2/} Amendment to the "Subsidy Account Decision: Additions to the List of Beneficiaries" (EBS/78/640, November 28, 1978).

be proposed. These seven members had purchases outstanding under the 1975 Oil Facility amounting to SDR 251.3 million, raising total purchases for eligible beneficiaries under the 1975 Oil Facility to 59.4 percent of the expected maximum total of purchases when the Account was established. Subsidies were first paid to the seven members that were added to the list of beneficiaries in May 1980, with respect to the first two financial years of the Account, following the annual review of the Subsidy Account for the financial year 1980.

4. Charges under 1975 Oil Facility and rate of subsidy

Use of the 1975 Oil Facility carried charges at the rates of 7.625 percent per annum for the first three years, 7.75 percent for the fourth year, and 7.875 percent per annum for the final three years. If members made repurchases in accordance with the agreed schedule of repurchase--i.e., in 16 quarterly installments starting 3 1/4 years after the date of the drawing--then the average recurrent cost of using the 1975 Facility throughout its life was 7.71 percent per annum.

As noted earlier, in establishing the Subsidy Account, it was suggested that its objective might be to "reduce the effective rate of annual charge payable on drawings by about 5 percent," but it was not precluded that a higher rate could be paid. In this regard, it was necessary for a choice to be made periodically on the rate of subsidy. The suggestion of a rate of 5 percent was made in the expectation that all unconditional contributions would in fact be made, that investment income would be of a reasonable size, and repurchases made by the beneficiaries would be as scheduled. Furthermore, a basic aim of the Account was that the rate of subsidy should be such as "to equalize the percentages payable to all recipients during the period of payments under the Decision" and in the early years of the Account this prompted a conservative approach in determining the rate of subsidy.

In "Subsidy Account" (SM/75/197, July 23, 1975), it was noted that "if contributions were augmented or earlier repurchases were made in any year, the Fund would make an annual review to determine whether additional amounts might be distributed to all recipients of payments..." (p.4). It was also made clear in that paper that any reductions in the rate of subsidy would apply prospectively and not retroactively. For example, in the second annual review of the Subsidy Account (EBS/77/164, May 18, 1977) the staff noted that "Although it now seems conceivable that a higher rate...[of subsidy]...might be paid eventually, uncertainties and conditions continue to be attached to some contributions... The staff feel that the aim to promote "equality of benefit" over time can best be achieved by increasing the rate of subsidy retroactively as and when the available funds would permit payment of a higher subsidy, with certainty, to all recipients equally."

From 1978 onwards, it became apparent that the resources in the Account would be more than sufficient to pay a subsidy of 5 percent per annum, on a retroactive basis, to the original 18 beneficiaries. The resources of the Account were increasing faster than estimated as indicated by the flow of donations which was somewhat ahead of schedule. Also, in 1979 two members, Ivory Coast and India, made early repurchases with respect to all their outstanding drawings under the Oil Facility, and would not be eligible for subsidies in future years. Furthermore, the level of investment income, due to the sharp increase in short-term interest rates (see Appendix Table 3), was also rising faster than the 6 percent that had been assumed at the outset of the Account.

In 1980, in view of the actual and prospective increase in resources in the Account, subsidies were paid for the first time to the seven new beneficiaries, at a rate of 5 percent, on a retroactive basis to FY 1976 and 1977. Since 1980 subsidies have been paid at the rate of 5 percent to all eligible members throughout the life of the Oil Facility. As of June 30, 1983 the Account held assets which amounted to SDR 11.4 million, which on disbursement would raise the total of subsidies paid by the Account to SDR 186.5 million.

5. Overall experience of the Subsidy Account

The Subsidy Account was the first trust arrangement established by the Fund for the benefit of a particular group of Fund member countries. In that sense, the Subsidy Account was a forerunner of the Trust Fund and the Supplementary Financing Facility Subsidy Account. The main objectives of the Subsidy Account can be said to have been broadly met: viz. to reduce substantially the net cost to those most seriously affected members which used the Fund's Oil Facility for 1975. The Account has provided, on an equal basis for all beneficiaries throughout the period of the Oil Facility, a subsidy of 5 percentage points, compared with the average recurrent cost of using the 1975 Oil Facility over the life of the Facility of 7.71 percent per annum.

The Subsidy Account was financed by donations, amounting to SDR 160 million, from 24 member countries and Switzerland. The financing of the Account was a significant cooperative response to help meet the needs of the poorest members at a time of generally difficult international financial circumstances.

From the point of view of the beneficiaries, the payment of a subsidy with respect to the charges on their drawings under the Oil Facility provided a welcome alleviation of strains on their balance of payments position. Subsidies, amounting so far to SDR 175 million, have been paid to 25 eligible members. This total amounted to the equivalent of 21 percent of the total drawings by the beneficiaries under the 1975 Oil Facility and to 64.3 percent of their total charges with respect to their drawings under that Facility, thereby increasing the grant element in drawings under the Facility to 28.8 percent.

After distribution of the assets remaining in the Subsidy Account, these figures would increase to approximately 23.2 percent of their Oil Facility drawings, 68.6 percent of the Oil Facility charges, and contain a grant element of 30 percent. On a somewhat wider basis of comparison, the payments by the Subsidy Account amounted, on average, to the equivalent of approximately 10 percent (10.8 percent) of the total charges paid by eligible beneficiaries on their outstanding indebtedness to the Fund (Appendix Table 5).

II. Disposal of Assets Remaining in the Subsidy Account

Following the Executive Board discussion (EBM/83/82, June 8, 1983) of "Final Review of the Oil Facility Subsidy Account" (EBS/83/94, May 13, 1983) it was decided to pay a subsidy of 5 percent to eligible beneficiaries for the period May 1, 1982 to May 11, 1983. All balances remaining under the 1975 Oil Facility were repurchased in early May 1983 and only a small amount of charges, covering the period May 1-11, 1983 remain to be paid in early August 1983. The financial statement of the Account as of June 30, 1983 is presented in the Appendix.

In EBS/83/94, the staff proposed that the resources remaining in the Account after payment of the subsidies for the period May 1, 1982 to May 11, 1983, be distributed in the form of a retroactive payment, which would be equivalent to about 0.32 per cent per annum, to all original and additional beneficiaries in proportion to their average balances that were eligible for subsidy during the lifetime of the Subsidy Account. The staff felt that this proposal was in keeping with earlier discussions on the Subsidy Account, summarized above, that the rate of subsidy would be increased from 5 percent if that could be done consistently with a basic objective of the Account to equalize the benefit of the Account for all recipients in all years. As pointed out above, any increase in the rate from 5 percent would be paid retroactively to the beneficiaries.

At EBM/83/82, some Executive Directors raised the alternative course of action of dividing the assets remaining in the Account at its termination among the donors. Paragraph 6 of the terms of the Decision on the Subsidy Account reads as follows:

"6. (a) If the Executive Directors find that the Subsidy Account is no longer necessary or that its purpose cannot be carried out, the Account will be terminated.

(b) If any assets remain in the Subsidy Account on the date of its termination, the amount will be divided among the donors that have made deposits in it in proportion to their contributions."

In that discussion it was pointed out that if any assets remained in the Account at the date of termination "all donors that had made

deposits in it would share in the remaining assets in proportion to their contributions." However, it would not be possible to make a return of contributions to only some of the donors; all donors must receive their respective share if any return of contributions were to be made. After discussion, the Executive Board agreed that a retroactive distribution should be made to all eligible beneficiaries and the Account should then be terminated.

In the light of the understanding reached at EBM/83/82, the following decision is proposed for adoption by the Executive Board:

1. Subsidy payments shall be made to the beneficiaries listed in Table 1 of EBS/83/94, Supplement 3, on the Fund's holdings of each member's currency subject to charges that were outstanding under the 1975 Oil Facility and eligible for subsidy for the period May 1, 1975 to May 11, 1983 at a rate (approximately 0.32 percent) that will fully utilize the remaining resources of the account.

2. These payments shall be made in U.S. dollars as soon as practicable after all charges due at the end of July 1983 in connection with the Oil Facility have been paid.

3. No charge shall be levied for the services rendered by the Fund in the administration, operation, and termination of the account.

4. After disbursement of subsidy payments under paragraph 2 above, the Subsidy Account shall be considered terminated.

Table 1. Estimated Amount of Final Subsidy Payment
(Amounts in SDRs)

Member	
Bangladesh	676,185
Cameroon	197,601
Central African Rep.	44,546
Egypt	529,983
Grenada	7,995
Haiti	69,674
India	1,758,994
Ivory Coast	92,519
Kenya	467,161
Malawi	62,821
Mali	66,248
Mauritania	89,092
Morocco	300,400
Pakistan	1,854,939
Papua New Guinea	179,326
Philippines	2,540,261
Senegal	165,620
Sierra Leone	83,381
Sri Lanka	569,960
Sudan	306,111
Tanzania	343,803
Western Samoa	6,853
Yemen, Peo. Dem. Rep.	201,689
Zaire	543,689
Zambia	263,849
Total	11,422,039

Table 1. Subsidy Account: List of Proposed Contributors and Amounts, and Actual Contributions
(in millions of SDRs)

<u>Member</u>	<u>Amounts</u> <u>First Proposed</u> <u>1/</u>	<u>Actual</u> <u>Contributions</u> <u>4/</u>
Algeria	2.00	--
Australia	5.70	5.70
Austria	2.30	2.30
Belgium	5.80 <u>2/</u>	5.60
Brazil	3.70	1.85
Canada	9.50	9.50
Denmark	2.20	2.20
Finland	1.60	1.60
France	12.90	12.68
Germany	13.70	13.72
Greece	1.20	0.60
Iceland	0.20	--
Indonesia	3.00	--
Iran	27.70	6.00
Iraq	9.80	--
Ireland	1.00	--
Italy	8.60	8.60
Japan	10.30	10.30
Kuwait	17.20	--
Libyan Arab Republic	5.80	--
Luxembourg	--	0.11
Netherlands	6.00	6.00
New Zealand	1.70	1.70
Nigeria	12.40	--
Norway	2.10	2.10
Oman	1.50	--
Qatar	4.00	--
Portugal	1.00	--
Saudi Arabia	72.90	40.00
South Africa	0.00 <u>3/</u>	1.35

1/ See SM/75/40.

2/ Including Luxembourg.

3/ Not included in SM/75/40.

4/ In some cases, the amounts proposed do not correspond to the amounts provided since the latter were defined in local currency based on SDR rates prevailing prior to actual payment.

Table 1. Subsidy Account: List of Proposed Contributors and Amounts, and Actual Contributions (concl'd.)
(in millions of SDRs)

<u>Member</u>	<u>Amounts</u> <u>First Proposed</u> 1/	<u>Actual</u> <u>Contributions</u> 4/
Spain	3.40	3.40
Sweden	2.80	2.80
Switzerland	0.00 3/	3.29
Turkey	1.30	--
United Arab Emirates	12.60	--
United Kingdom	24.10	12.00
United States	57.60	--
Venezuela	6.10	6.00
Yugoslavia	<u>0.00</u> 3/	<u>0.90</u>
Total	353.70	160.29

1/ See SM/75/40.

2/ Including Luxembourg.

3/ Not included in SM/75/40.

4/ In some cases, the amounts proposed do not correspond to the amounts provided since the latter were defined in local currency based on SDR rates prevailing prior to actual payment.

Table 2. Contributions Received in Financial Years, 1976-83

(Amounts expressed in SDRs)

Donors	1976	1977	1978	1979	1980	1981	1982	1983
Australia		1,070,000	2,370,000	1,130,000	1,130,000			
Austria		2,300,000						
Belgium			2,240,000	1,120,000	840,002	840,004	559,744	256
Brazil	462,500	462,500	462,500	462,500				
Canada	9,500,000							
Denmark		640,000		320,313	309,555	307,320	308,315	314,496
Finland		373,611	426,389	400,000		400,000		
France	2,613,786	2,431,716	2,481,248	2,245,988		2,600,007	305,271	
Germany	6,841,275			6,878,568				
Greece		150,000			447,049			
Iran	1,500,000	1,500,000		1,500,000	1,500,000			
Italy			8,600,000					
Japan		2,199,095	2,163,822	1,986,000	1,705,530	1,482,804	762,749	
Luxembourg	108,150							
Netherlands	6,000,000							
New Zealand		286,473	320,288	310,831	269,498	220,406	227,429	65,860
Norway	500,000	1,600,000						
Saudi Arabia		9,989,587	9,820,034		20,209,628	(19,249)		
South Africa	670,000	680,000						
Spain	490,000	490,000		980,000	490,000		950,000	
Sweden		1,400,000	700,000	700,000				
Switzerland	3,285,250							
United Kingdom	2,339,229		4,352,766	2,183,892	1,696,701	1,068,659	363,301	
Venezuela	1,500,000		1,500,000	3,000,000				
Yugoslavia	225,000	225,000		450,000				
	<u>36,035,190</u>	<u>25,797,982</u>	<u>35,437,047</u>	<u>23,668,092</u>	<u>28,597,963</u>	<u>6,899,951</u>	<u>3,476,809</u>	<u>380,613</u>
Cumulative Total	36,035,190	61,833,172	97,270,219	120,938,311	149,536,274	156,436,225	159,913,034	160,293,647

Table 3. The Financial Position of the Subsidy Account,
 Financial Years 1976-83 and June 30, 1983
 (Amounts expressed in SDRs)

	1976	1977	1978	1979	1980	1981	1982	1983	June 30, 1983
Balance at beginning of period		36,686,385	50,630,093	58,746,352	59,735,399	73,934,615	62,090,034	20,329,194	13,554,866
Contributions received	36,035,190	25,797,982	35,437,047	23,668,092	28,597,963	6,899,951	3,476,809	380,613	--
Interest earned on investments	322,083	2,324,480	2,404,139	3,259,139	5,621,859	5,316,542	2,730,476	1,722,729	234,893
Valuation gain (loss)	329,112	(360,249)	(2,218,982)	(988,127)	(921,021)	3,711,209	2,083,422	462,393	164,729
Subsidy Payments (less)		13,818,505	27,505,945	24,950,431	19,099,585	27,772,283	50,051,547	9,340,063	2,532,449
Balance invested at end of period	36,686,385	50,630,093	58,746,352	59,735,399	73,934,615	62,090,034	20,329,194	13,554,866	11,422,039
<u>Investment income:</u>									
(i) As per cent of closing balance	0.88	4.59	4.09	5.46	7.60	8.56	13.43	12.71	--
(ii) Cumulative	322,093	2,646,563	5,050,702	8,310,215	13,932,074	19,248,616	21,979,092	23,701,821	23,936,714

Table 4. List of Potential Beneficiaries

1. List of Most Seriously Affected (MSA) Countries 1/

Afghanistan	Laos
Bangladesh	Lesotho
Benin (Dahomey)	Madagascar (Malagasy Republic)
Burma	Mali
Burundi	Mauritania
Cameroon	Niger
Central African Republic	Pakistan
Chad	Rwanda
Egypt	Senegal
El Salvador	Sierra Leone
Ethiopia	Somalia
Ghana	Sri Lanka
Guinea	Sudan
Guyana	Tanzania
Haiti	Uganda
Honduras	Upper Volta
India	Western Samoa
Ivory Coast	Yemen Arab Republic
Kampuchea (Khmer Republic)	Yemen, People's Democratic Republic of
Kenya	

2. Additional Beneficiaries 2/

Grenada	Philippines
Malawi	Zaire
Morocco	Zambia <u>3/</u>
Papua New Guinea	

1/ Fund members, as in Annex A of the Subsidy Account Decision, that were on the May 1975 list of MSA's compiled by the United Nations.

2/ With the addition of these members, the list of beneficiaries included all members eligible to receive assistance from the Trust Fund that used the 1975 Oil Facility.

3/ Zambia was added to the Trust Fund in the second period and therefore was eligible for subsidy payments only with respect to average daily balances subject to charges from July 1, 1978.

Table 5. Oil Facility Subsidy Account:
Subsidy Payments in Relation to Total Charges,
Financial Years 1976-83
(In millions of SDRs)

	Subsidy Payments 1976-1983	Charges on all Fund Borrowing 1976-1983	Charges on 1975 Oil Facility Only	(1) as % (2)
	(1)	(2)	(3)	(4)
Original beneficiaries:				
Bangladesh	10.37	117.56	15.78	8.82
Cameroon	3.02	9.46	4.60	31.92
Central African Republic	0.68	5.64	1.04	12.06
Egypt	8.11	71.51	12.35	11.34
Haiti	1.06	7.01	1.61	15.12
India	26.95	234.22	41.08	11.51
Ivory Coast	1.42	48.16	2.16	2.95
Kenya	7.15	66.09	10.89	10.82
Mali	1.02	5.66	1.56	18.02
Mauritania	1.36	11.05	2.08	12.31
Pakistan	28.42	262.67	43.27	10.82
Senegal	2.54	31.40	3.86	8.09
Sierra Leone	1.28	15.04	1.95	8.51
Sri Lanka	8.74	94.98	13.30	9.20
Sudan	4.74	116.53	7.23	4.07
Tanzania	5.28	41.56	8.04	12.70
Western Samoa	0.11	1.16	0.16	9.48
Yemen, PDR	3.08	11.74	4.70	26.24
Subtotal	115.33	1,051.21	175.67	10.97
Additional beneficiaries:				
Grenada	0.13	0.86	0.19	15.12
Malawi	0.95	15.80	1.45	6.01
Morocco	4.61	122.29	7.02	3.77
Papua New Guinea	2.75	10.96	4.12	25.09
Philippines	38.92	270.67	59.27	14.38
Zaire	8.34	104.97	12.74	7.95
Zambia	4.04	145.11	11.60	2.78
Subtotal	59.74	670.66	96.39	8.91
Total	175.07	1,721.87	272.06	10.17