FOR AGENDA

EBS/83/187

CONFIDENTIAL

August 26, 1983

To: Members of the Executive Board

From: The Secretary

Subject: Review of the Guidelines for Borrowing by the Fund

The attached paper reviewing the guidelines for borrowing by the Fund will be brought to the agenda for discussion on a date to be announced.

This paper is also relevant to the discussion on the policy on access to the Fund resources scheduled for Wednesday, August 31, 1983.

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

Review of the Guidelines for Borrowing by the Fund

Prepared by the Treasurer's Department

(In consultation with the Legal Department)

Approved by W. O. Habermeier

August 26, 1983

Introduction

On January 13, 1982, the Executive Board adopted Decision No. 7040-(82/7) on Guidelines for Borrowing by the Fund, the full text of which is reproduced as Appendix 1. Paragraph 4 of the decision reads as follows:

> "In the case of major developments, the Executive Board shall promptly review, and may adjust, the guidelines. In any event, the guidelines shall be reviewed when the Board of Governors has completed the Eighth General Review of Quotas, and may be adjusted as a result of that review of the guidelines."

The Eighth General Review of Quotas was completed by the Board of Governors earlier this year. Thus, a review of the guidelines is required and this memorandum has been prepared as a basis for that review. It is organized as follows. Section I sets out the background to the adoption of the present guidelines. Section II discusses the provisions of the guidelines that seem to merit reexamination at this time. The final section provides a brief summary of the main conclusions. A draft of an amended decision is set out in Appendix 2 for the consideration of the Executive Board.

I. The Background to the Guidelines for Borrowing

There were three considerations that led to the establishment of a set of guidelines for Fund borrowing. The most general was to ensure a prudent and systematic management of the way in which the Fund is financed, and in particular the relationship between internal, or ordinary, resources derived from quotas and external resources derived from borrowing. The two more specific considerations were the following:

(i) From the earliest of the staff's contacts with commercial bankers and other participants in the private capital markets, emphasis has been placed on the need for the Fund, in connection with any approach to the private markets, to have an established policy on limiting borrowing to some proportion of its total quotas. As a result, the question of guidelines for the amounts of outstanding borrowing by the Fund was raised by the staff in EBS/80/247 (11/12/80), "Borrowing by the Fund--Main Issues," which was discussed by the Executive Board at EBM/80/174 (11/26/80).

(ii) When the Fund concluded the borrowing agreement with the Saudi Arabian Monetary Agency (SAMA) in May 1981, the question of the future amounts of Fund borrowing was of considerable interest to the Saudi authorities. In view of this interest, the Managing Director wrote to the Governor of SAMA indicating that he would propose to the Executive Board a policy laying down guidelines on the amounts of borrowing by the Fund; this initiative "would be designed to assure creditors that the Fund's borrowing will be prudently managed by incorporating in the guidelines the principle of a limit on the Fund's total indebtedness expressed as a ratio of its total quotas."1/

Following extensive analysis of possible approaches to the guidelines by the staff, and considerable discussion by the Executive Board in the latter part of 1981 and early 1982, the decision set out in Appendix 1 was adopted by the Executive Board.2/ It may be useful to repeat three general points that were emphasized in the discussions because they remain relevant to any consideration of guidelines for borrowing. First, decisions to borrow are ultimately the responsibility of the Executive Board, and this provides considerable assurance to creditors that any proposals for the Fund to borrow will be carefully scrutinized by the governments of its members and that the Fund will act prudently. Second, as an intergovernmental organization with very substantial assets, the Fund is in a position to borrow very large amounts without giving rise to concern about its ability to service its debt. Third, any policy on the amounts of Fund borrowing must allow the Fund the flexibility it needs to fulfill its role in the international monetary system. This last consideration has been underscored by those developments in the international monetary system that have led to the recent rapid expansion in commitments of the Fund's resources to promote adjustment.

1/ The full text of this letter may be found in Selected Decisions, 10th Issue, p. 199.

2/ See "Guidelines on Borrowing by the Fund," EBS/81/174 (8/19/81) and Cor. 1 (8/21/81), which were discussed at EBM/81/119 and EBM/81/120 (9/4/81); "Guidelines on Borrowing by the Fund--Further Considerations," EBS/81/227 (11/24/81) and Supp. 1 (1/12/82), which were discussed at EBM/82/4 and EBM/82/5 (1/11/82) and EBM/82/6 and EBM/82/7 (1/13/82). See also the Chairman's Concluding Remarks at EBM/82/7 (1/13/82) contained in Buff Document No. 82/4 (1/22/82).

As finally adopted, the decision represents a compromise between fairly divergent views. Some Directors disagreed in principle with the adoption of guidelines; others felt that there was little merit in linking borrowing to the total of quotas; and there was a wide range of views on what would be an appropriate limit. Moreover, there was extensive discussion of some of the technical aspects that were eventually incorporated in the decision, including in particular whether the combined total of borrowing plus unused credit lines or only actual borrowing should be covered by the guidelines, and on how the credit lines under the General Arrangements to Borrow (GAB) should be treated.

It should be stressed that the decision was not regarded as setting out a consensus on how much the Fund should borrow, or as establishing a limit on borrowing that in some way objectively reflected the maximum the Fund could prudently borrow in case of need. For some Executive Directors a major consideration was to underline the primary role of quotas in the financing of the Fund, and to strike a reasonable balance between the Fund's reliance on subscribed capital (i.e., quotas) and on borrowing. Other Executive Directors seemed to view the ceiling on borrowing more as a means of controlling the potential expansion of Fund credit. It was also generally recognized that the limit established by the guidelines should provide the Fund with room for maneuver in the light of reasonable expectations of the prospective need to borrow in the foreseeable future.

Another aspect of the Executive Board's discussion of the guidelines was the question of a so-called asset ratio or liquidity ratio, which would relate amounts of borrowing to the Fund's usable assets, taking into account the other potential demands that might be made on these assets. In the two staff memoranda a number of possible ratios were discussed; it was, however, concluded that the significance of the level of any particular ratio, and of changes in that ratio, were largely a matter of judgment in the light of all relevant circumstances. The Executive Board did not regard it as advisable to incorporate in the guidelines a minimum asset or liquidity ratio, but concluded that the liquidity of the Fund would be reviewed by the Executive Board at least every six months, and that a number of ratios--both actual and projected--would be presented as part of those reviews and updated quarterly in connection with the operational budgets.

II. The Provisions of the Present Guidelines and Possible Changes

Unless there are clear reasons for a substantive change, or if a change would enhance significantly the clarity and simplicity of the guidelines, the confidence of creditors in the prudence of the Fund's policies on borrowing is likely to be strengthened if the Fund maintains unchanged the principal features of the guidelines, and this general consideration should be borne in mind in any review.

There are two main elements of the guidelines that seem to merit reexamination in the present review, namely, the limit of 50-60 percent of total Fund quotas and the treatment of the GAB, and these issues are examined in detail below. An amendment will also be required to the present review clause. This clause contains the reference to the Eighth Review of Quotas that gives rise to this present review. It is proposed that this provision be amended to include a reference to the Ninth Review of Quotas, and that it also provide for a review if there were to be a change in the GAB or associated arrangements. The other provisions of the decision are (i) the Preamble, which stresses the role of quotas while noting the importance of borrowing; (ii) the requirement for "continuous monitoring" of borrowing (paragraph 1), which has been met by the periodic reviews of the Fund's liquidity position and financing needs; and (iii) the statement in paragraph 5 that the limits on borrowing are not to be understood as targets. These provisions are not discussed further in this memorandum, although it is for consideration whether the Preamble should mention the importance of the GAB, and the draft decision in Appendix 2 contains a suggested reference.

At this time, three interrelated questions seem to require examination, of which the last may be regarded as the most important. First, whether it would be useful to clarify and simplify the guidelines by setting the borrowing ceiling as a single percentage rather than as a range, as at present. Second, whether there should be a change in the treatment of the GAB credit lines. Third, whether the overall limitation on borrowing should be changed in the light of (i) the potential need for the Fund to borrow in the period up to the next quota increase, and (ii) the increases in quotas under the Eighth Review and the relatively larger increase in the GAB and its broadened applicability. In addition, the resolution of a number of other issues currently under consideration may also have a bearing on the guidelines: these include the policy on enlarged access after the quota increase, and the relationship of borrowed to ordinary resources in the future funding of enlarged access, as well members' future access under the compensatory and cereal financing facilities and the buffer stock facility.

1. Replacement of the range of 50-60 percent of quotas by a single limit[1/]

The basic quantitative guideline under the present decision requires that the Fund will not allow the total of outstanding borrowing plus unused credit lines to exceed the range of 50-60 per cent of the

1/ Paragraph 2 of the decision on guidelines reads as follows:

"Subject to paragraph 4 below, the Fund will not allow the total of outstanding borrowing plus unused credit lines to exceed the range of 50-60 per cent of the total of Fund quotas. If the total of outstanding borrowing plus unused credit lines reaches the level of 50 per cent of quotas, the Executive Board shall assess the various technical factors that determine, at that time, the availability of balances of unused lines of credit. While this assessment is being made, the total of outstanding borrowing plus unused credit lines may rise, if necessary, beyond 50 per cent, but shall not exceed 60 per cent of total quotas."

total of Fund quotas. The guidelines also allow for the possible adjustment of this range in response to major developments or as a result of a scheduled review.[1]

Setting the ceiling in the form of a range was motivated by several considerations. It was agreed that the guidelines would employ the total of actual borrowing plus unused credit lines. A number of uncertainties, however, arise with the concept of unused lines of credit. These uncertainties provided one reason why the limit was expressed as a range rather than as a single percentage. In addition, the use of a range facilitated a compromise between the views of those Directors that felt a ceiling of 50 percent of quotas was adequate and those who thought that it should be higher.

The inclusion of unused lines of credit was also regarded by some Executive Directors as the more cautious and prudent approach.[2] One important reason for the inclusion of the full amount of unused credit lines (except for the special treatment of the unused GAB lines of credit) was that the Fund would, as a result, always have the ability to draw on existing credit lines without the risk of exceeding the limit in the guidelines.

The relatively brief experience of the Fund since the decision was adopted has not provided any new reason to suggest that unused lines of credit should be excluded and the limit be set in terms of actual borrowing, which was the approach favored by some Executive Directors. However, the use of a range as a limit certainly detracts from the clarity and simplicity of the guidelines, and it would be preferable, subject to the possibility of an increase in the ceiling, which is discussed below, to set the limit as a single percentage at the upper end of the range.

The present guidelines envisage the possibility that actual borrowing could rise to 60 percent of Fund quotas, although in practice it would not be likely to do so, and the role of the 50 percent level is to trigger an assessment by the Executive Board of the technical factors that affect the availability of unused credit lines. While that assessment is taking place, actual borrowing plus unused credit lines can rise above 50 percent of quotas but must not exceed

---

1/ See paragraph 4 of the guidelines.

2/ It was recognized that the inclusion of unused credit lines would be very likely to overstate the level that actual borrowing could reach. There are three reasons for this potential overstatement: (i) some credit lines may have become unusable because of a weakening in the lender's balance of payments and reserve position; (ii) during the period over which lines of credit can be drawn down, some part of actual borrowing is likely to fall due for repayment; and (iii) there may be a need to arrange in advance new lines of credit to finance the repayment of shorter-term borrowing.

60 percent. If the range of percentages in the guidelines were replaced by a single percentage, this would not preclude the triggering of a similar assessment at a lower percentage. However, with the continuous monitoring of the Fund's liquidity and financing needs, and given the requirement for the Executive Board to approve any new borrowing arrangements, the requirement for such an assessment in the guidelines seems to be superfluous. If this assessment was regarded as essential at a certain percentage below the ceiling, this could be a matter of understandings between the Managing Director and the Executive Board, but--in the interest of simplicity--the requirement for the assessment of the relevant technical factors need no longer be reflected in the guidelines, which are in the public domain.

2. Treatment of GAB credit lines[1/]

The guidelines provide that the total of borrowing plus unused credit lines is to include either outstanding GAB borrowing or half the total of the GAB credit lines, whichever is the larger. This method of dealing with the GAB recognized that the present GAB can be activated only to finance purchases by GAB participants, and that the credit lines of all participants cannot be activated at the same time. Obviously, the credit line of the participant for which the GAB is activated is not available, and the balance of payments and reserve positions of some other participants may make it difficult to activate their credit lines for substantial amounts.

The character of the GAB is to be changed significantly in a number of ways. First, it was agreed to provide for a substantial enlargement of the arrangements to a total of SDR 17 billion.[2/] Second, under certain conditions involving a threat to the stability of the international monetary system, the Fund will have the possibility of activating the GAB to assist the Fund in financing

---

1/ Paragraph 3 of the guidelines reads as follows:

> "Recognizing that the credit lines of all participants in the General Arrangements to Borrow (GAB) cannot be used at the same time and that the GAB can be activated only to finance purchases by a GAB participant, the total of outstanding borrowing plus unused credit lines under paragraph 2 above shall include, in respect of the GAB, either outstanding borrowing by the Fund under the GAB or one half of the total of credit lines under the GAB, whichever is the greater."

2/ The addition of Switzerland to the list of participants also strengthens the arrangements because a substantial credit line is available from a participant that cannot, as a nonmember, make purchases from the Fund for which the GAB could be activated.

purchases in the credit tranches by members other than participants.[1] Third, the Fund will be able to conclude borrowing agreements that are associated with the GAB, and one such agreement (with Saudi Arabia--for SDR 1.5 billion) has been concluded.[2]

These changes in the size and applicability of the GAB suggest that its treatment under the guidelines should be reconsidered. First, the description of the nature of the GAB incorporated in the text of paragraph 3 needs to be revised and supplemented by a reference to "associated borrowing arrangements." Second, the question will need to be decided as to how much of the total of the GAB and associated arrangements should be regarded as usable for the purpose of the guidelines.

In this connection, there are two somewhat conflicting considerations. On the one hand, particularly in view of the broadened applicability of the GAB, the amount that is included in the total of unused credit lines should be such that there would always be scope within the overall borrowing ceiling for the GAB to be activated for a substantial proportion of the total arrangements. On the other hand, it would be disadvantageous to incorporate a proportion of the GAB that was unrealistically high, as this could unnecessarily inhibit the Fund's ability to borrow from other sources, particularly as the Fund has no guarantee that the GAB can be activated.

There can, of course, be no basis for predicting precisely how much of the GAB would be available in the event it was activated. Much will depend on the circumstances at the time the Managing Director would make his proposals, and in particular on the balance of payments and reserve positions of the lenders. If, for example, the activation was to finance purchases by one of the participants, that participant's

---

1/ Paragraph 21(b) defines the circumstances as follows:

> "The Managing Director may initiate the procedure for making calls under Paragraph 7 in connection with requests referred to in Paragraph 21(a) if, after consultation, he considers that the Fund faces an inadequacy of resources to meet actual and expected requests for financing that reflect the existence of an exceptional situation associated with balance of payments problems of members of a character or aggregate size that could threaten the stability of the international monetary system. In making proposals for calls pursuant to Paragraph 21(a) and (b), the Managing Director shall pay due regard to potential calls pursuant to other provisions of this Decision."

2/ From here on the use of the term "the GAB" is intended to encompass the associated arrangement with Saudi Arabia although it should be noted that the Fund's ability to activate the arrangement is not identical to its ability to activate the GAB.

credit line would not be available. The largest credit line is that of the United States, which is 23 percent of the total of the credit lines of the GAB and the associated arrangement with Saudi Arabia. Thus, to regard 75 percent of the credit lines as being normally usable would allow for the largest credit line not being available: it would also cover the nonavailability of the credit lines of various combinations of other lenders.1/

There is, however, also the possibility that the Fund could activate the arrangements to finance nonparticipants, and it cannot be precluded that the credit lines of all lenders might be drawn on. It could be important at such a time to promote confidence in the system that all the lenders participate in the activation. Nevertheless, it would remain unlikely that the full amounts of each credit line could be drawn on in full, particularly as the Managing Director's proposals must be guided by the balance of payments and reserve positions of the lenders. To take account of this, even in circumstances in which all lenders participated, it might not be unreasonable to expect, as in the past, that about one half of the credit lines of lenders accounting for about one half of the total might not be usable. This would also point to a usability of about three quarters of the total.

An examination has also been made, based on the usability of currencies under the operational budgets, of the availability of GAB credit lines over the last six and a half years, following the increase in Japan's credit line in November 1976. On average over that period about 60 percent of available credit lines were usable.2/ At present, using the same criterion, an amount of SDR 15.8 billion, or about 85 percent, would be usable from the GAB plus the arrangement with Saudi Arabia.

These considerations do not point clearly to the use of any particular proportion. They do, however, suggest that a proportion of one half might generally be on the low side, while three quarters, although available in certain circumstances, might be rather high. Given the enhanced applicability of the GAB, and the need to create confidence that a substantial proportion of the total could normally be activated within the guidelines to cope with strains in the system, it is proposed that the present decision be amended as regards the treatment of the GAB credit lines. Specifically, it is proposed that the total of unused credit lines would include two thirds of the total of GAB and associated arrangements. This would be SDR 12.3 billion of the new total of SDR 18.5 billion.

1/ For example, the combined credit lines of Germany and Japan, the next largest lenders, total 24.4 percent of the total. The credit lines of France, Italy, and the United Kingdom also total 24.4 percent.

2/ Over 27 quarterly periods availability exceeded three fourths of the total in 14 of these periods, and in 3 periods fell below one fourth of the total.

3. Revision of the limit

This section discusses what the overall limit on borrowing plus unused credit lines should be, taking into account the possible needs of the Fund to borrow over the next several years, and the increase in quotas and the considerably enhanced potential importance of the GAB. As mentioned above, the potential need for the Fund to borrow in the light of agreed policies on access and the method of financing, and the balance between the Fund's reliance on quotas and on borrowing, were important considerations underlying the adoption of the present guidelines.

a. Future borrowing needs

As a minimum, the guidelines should accommodate reasonable projections of future borrowing based on policies agreed by the Executive Board on both members' access to Fund resources and the method by which this access is to be financed. Given the difficulties of projecting the amounts the Fund may need to make available to members over the period until the next quota increase, the guidelines should also provide reasonable scope for the Fund to deal with unexpected developments.

In EBS/83/170 (8/12/83), "The Fund's Liquidity Position and Financing Needs," it is estimated that by about the end of 1983 borrowing plus unused credit lines, including the present allowance of SDR 3.2 billion for the GAB, will be about SDR 26.1 billion.[1] This amount of borrowing plus unused credit lines assumes that new lines of credit totaling SDR 6 billion will be in place at that time. If the new quotas and the enlargement of the GAB come into effect at that time, and the proposal is accepted to include two thirds of the GAB and associated arrangements in the total of unused credit lines, the total of borrowing plus unused credit lines will rise by SDR 9.1 billion (i.e., the difference between SDR 3.2 billion and SDR 12.3 billion). At SDR 35.2 billion, the total of borrowing plus unused credit lines would be 39 percent of total quotas of SDR 90 billion.

Additional borrowing needs in the period from January 1984 through April 1986 have been projected in recent staff memoranda on enlarged access. With access limits set in the range of 102/307 and 125/375 percent of members' quotas, and assuming that the overall use of ordinary and borrowed resources would be in about equal proportions, the additional borrowing need to about April 1986 would range from SDR 8.3 billion to SDR 13.1 billion.[2] Over the same period, repayments of

1/ See Appendix Table 1 in EBS/83/170 (8/12/83) "The Fund's Liquidity Position and Financing Needs."

2/ See EBS/83/79, Review of Enlarged Access Policy, and EBS/83/133 (6/28/83), "Review of the Policy on Access to the Fund's Resources," in particular, Table 2. The general order of possible demand for Fund resources under stand-by and extended arrangements for the period January 1984-April 1986 is confirmed in the recent review of the Fund's liquidity position and financing needs (EBS/83/170).

borrowing will total about SDR 3.4 billion. The level to which the total of borrowing plus unused credit lines would rise would depend on whether the additional SDR 8-13 billion of borrowing was financed by the GAB exclusively, or by other borrowing arrangements exclusively, or by some combination of both sources.

If the GAB were used to cover the additional need to borrow, and no other credit lines were established, the total of borrowing plus unused credit lines of SDR 35.2 billion would simply decline by repayments of borrowing (SDR 3.4 billion) over the period to April 1986. At SDR 31.8 billion, or 35 percent of quotas, the total would include the allowance of SDR 12.3 billion for the GAB. This would cover a substantial proportion of new borrowing in the range of SDR 8.3 billion to SDR 13.1 billion. At the same time, if it were necessary and feasible to borrow the full amount of SDR 18.5 billion under the GAB in response to strains in the monetary system, the total would rise to SDR 38.0 billion, or 42 percent of total quotas.

On the other hand, the borrowing need might have been met exclusively from new borrowing arrangements. This could be the case, for example, if circumstances had not arisen in which the GAB could be activated, or if as a matter of policy the GAB was being kept in reserve to cope with possible strains in the monetary system. In that event, the end-1983 total of SDR 35.2 billion would increase to the range of SDR 40.1 billion to SDR 44.9 billion, or 45-50 percent of total quotas.1/ The percentage at the upper end of the range would cover the use of the GAB and associated arrangements for two thirds of the total (SDR 12.3 billion); if it were necessary and feasible at that point to use the whole of the GAB in response to serious strains in the monetary system, the total applicable for the guidelines would rise to SDR 51.1 billion, or about 57 percent of total quotas.2/

Given the need for the Fund to have adequate room for maneuver, particularly in respect of its ability to borrow under the GAB in crisis situations, a limit of 60 percent of total quotas, or possibly

---

1/ The totals are derived as follows: SDR 35.2 billion less repayments of SDR 3.4 billion plus additional borrowing of SDR 8.3 billion to SDR 13.1 billion.

2/ It would, of course, be closer to 60 percent if the total of Fund quotas were to be less than SDR 90 billion in the event that a few members accounting for a small percentage of the total quota increase would not have consented to their increases. If the shortfall were significantly below SDR 90 billion, it would be reasonable to assume that those members that had failed to consent would not be those that are likely to be making heavy demands on the Fund's resources. Thus, a smaller total of quotas is more likely to mean a reduction in the Fund's usable resources than in demands on those resources. This possibility represents another uncertainty that would support a modest increase in the limit.

somewhat higher--say, two thirds of total quotas, would seem to be required in the light of the potential need for the Fund to borrow through April 1986.

Two other considerations suggest that it would be prudent to set the limit at 60 percent, or possibly higher. The projections mentioned above only cover the period to April 1986. Although the flow of repurchases will be very large after that date, there can be no guarantee that the peak of borrowing will have passed. Some time will remain before the completion of the next quota review, which should have taken place by March 31, 1988, and experience suggests that a further period would elapse before new quotas would be put into effect. At this stage it is impossible to say what the Fund's needs might be over the period until new quotas would come into effect. Moreover, new borrowing arrangements seem likely to involve a higher proportion of shorter maturities than in the past. This may mean that the Fund will need to establish new credit lines before the repayment of these borrowings falls due. More generally, with the Fund engaged in a greater degree of maturity transformation, there may be a greater need to have credit lines available as a source of liquidity on a contingency basis.

b. Quota increase and enlargement of the GAB

The decisions on quotas and the GAB, and the acceleration of the normal timetable, reflected the perceived strains in the international monetary system and the need to create confidence that the Fund would command sufficient resources to promote the adjustment needed to cope with those strains. It remains to be seen whether the overall increase in the Fund's access to resources will be sufficient to meet the potential needs over the next several years. What is clear, however, is that the Fund's need for new resources is to be met by a relatively small increase in quotas and a relatively much larger increase in potential access to borrowed resources. Quotas will be increased by about 50 percent, but at the same time the Fund's potential ability to borrow under the GAB has been nearly trebled; the arrangements are available for activation in a wider range of circumstances than in the past; and an important borrowing agreement has been concluded in association with the GAB. In present circumstances, and given the continued need to foster confidence, the greater emphasis on borrowing relative to quotas would certainly seem to justify setting the ceiling at the upper end of the present range of 50-60 percent, or possibly even higher. 1/

c. Revision of the borrowing ceiling

In the light of the above discussion, it would seem that the overall ceiling on Fund borrowing should be set at 60 percent of the total

1/ At present the GAB is 10.5 percent of total quotas. At SDR 18.5 billion, including the arrangement with Saudi Arabia, it will be 20.5 percent of quotas. Thus, its importance relative to quotas has nearly doubled.

of quotas, that is to say, at the upper end of the range of 50-60 percent under the present guidelines. A small increase--say, to two thirds of total quotas--might also be justified in the light of the uncertainties as to the future need for the Fund to borrow in the period prior to the next quota increase and the possibility that the Fund might be engaging in a greater degree of maturity transformation than in the past. Such an increase could be justified and explained by the enlargement of the GAB relative to quotas and its enhanced potential as a source of finance at times when the international monetary system is threatened.

III. Summary of Main Conclusions

This memorandum has reviewed briefly the background to the existing guidelines (Section I) and discussed possible changes (Section II). At the outset of the discussion in Section II, it was noted that unless there are clear reasons for substantive change, or unless a change would enhance significantly the clarity and simplicity of the guidelines, the confidence of creditors is likely to be strengthened if the Fund maintains unchanged the principal features of the guidelines. It is in the light of this general consideration that the following proposals are put forward.

(i) To improve the clarity and simplicity of the guidelines, it is proposed that the expression of a limit as a range (at present 50-60 percent of total quotas) be dropped, and the ceiling be expressed as a single percentage of total quotas. It is also proposed, in the light of the continuous monitoring of the Fund's liquidity and financing needs, to drop from the decision the requirement for a special assessment of the availability of unused credit lines at a percentage lower than the limit. Nevertheless, if it were felt necessary, it could be understood that if the ratio were to reach 50 percent of quotas an assessment would be made by the Executive Board as under the existing decision.

(ii) The substantial enlargement of the GAB, together with its broadened applicability, suggests that its treatment under the guidelines requires reexamination. Under the present guidelines, one half of the total of the GAB (or actual borrowing if this is larger) is included in the total of borrowing plus unused credit lines. In view of the enlargement of the GAB and its broadened applicability, the Fund should always be in a position to cope with strains in the international monetary system by activating the arrangements for a substantial proportion of the total. This can only be assured if the guidelines provide sufficient scope for such activation. At the same time, the allowance made for GAB activation should not be unrealistically high. Although these considerations do not point clearly to a specific proportion, they do suggest that one half of the total might be on the low side. It is proposed, therefore, that two thirds of the total of the GAB plus associated borrowing arrangements be included in the total of borrowing plus unused credit lines.

(iii) The increase in quotas of about 50 percent was accompanied by a relatively much larger increase in the GAB. Although the enlarged scope for borrowing is available only on a contingency basis, and the Preamble to the guidelines should continue to stress the primacy of quotas, the decision on the GAB represents a somewhat greater emphasis on potential borrowing relative to quotas than existed when the present guidelines were adopted. Moreover, if the GAB were kept in reserve or the conditions for its activation did not arise, or if it were preferred for the Fund to borrow from non-GAB sources, the total of borrowing plus unused credit lines (including two thirds of the GAB) could exceed 50 percent of total quotas of SDR 90 billion by about April 1986, and could move close to 60 percent of quotas if it were necessary and feasible for GAB borrowing to rise to a high proportion of the total. Moreover, there can be no guarantee that the position that might be reached in April 1986 would represent the peak level of borrowing in the period prior to the next quota increase. For these reasons, it is proposed that as a minimum the ceiling be set at 60 percent of total quotas, that is to say, the upper limit of the present range of 50-60 percent. Moreover, it is for consideration whether a modest increase in the ceiling might be justified in the light of the uncertainties in the period prior to the next quota increase. Together with the change proposed in the treatment of the GAB, a modest increase in the limit--say, to two thirds of total quotas--may help to strengthen confidence that the Fund will be able to command the necessary resources to promote adjustment and to cope with both the present strains in the system and those that might arise in the period before the Ninth Review of Quotas is completed.

A draft decision, which incorporates the above proposals, together with the other minor drafting changes mentioned earlier in this memorandum, is set out in Appendix 2. The guidelines proposed should not become effective until both the quota increase and the revision and enlargement of the GAB are in effect. It is, therefore, proposed that the Executive Board decide in principle on the text of the guidelines, and that a lapse-of-time decision putting the new guidelines into effect be circulated when the quota increases and the new GAB become effective. The discussion in this memorandum, and the suggested procedure for bringing the new guidelines into effect, are based on the assumptions that the quota increase will go into effect in accordance with the timetable required by the Resolution and that the enlarged and revised GAB will go into effect at about the same time. If these assumptions prove incorrect, the matter may need to be brought back to the Executive Board.

Guidelines for Borrowing by the Fund

Quota subscriptions are and should remain the basic source of the Fund's financing. However, borrowing by the Fund provides an important temporary supplement to its resources. In present circumstances, it facilitates the provision of balance of payments assistance to its members under the Fund's policies of supplementary financing and enlarged access.

The confidence of present and potential creditors in the Fund will depend not only on the prudence and soundness of its financial policies but also on the effective performance of its various responsibilities, including, in particular, its success in promoting adjustment.

Against this background the Executive Board approves the following guidelines on borrowing by the Fund.

1. Fund borrowing shall remain subject to a process of continuous monitoring by the Executive Board in the light of the above considerations. For this purpose, the Executive Board will regularly review the Fund's liquidity and financial position, taking into account all relevant factors of a quantitative and qualitative nature.

2. Subject to paragraph 4 below, the Fund will not allow the total of outstanding borrowing plus unused credit lines to exceed the range of 50-60 per cent of the total of Fund quotas. If the total of outstanding borrowing plus unused credit lines reaches the level of 50 per cent of quotas, the Executive Board shall assess the various technical factors that determine, at that time, the availability of balances of unused lines of credit. While this assessment is being made, the total of outstanding borrowing plus unused credit lines may rise, if necessary, beyond 50 per cent, but shall not exceed 60 per cent of total quotas.

3. Recognizing that the credit lines of all participants in the General Arrangements to Borrow (GAB) cannot be used at the same time and that the GAB can be activated only to finance purchases by a GAB participant, the total of outstanding borrowing plus unused credit lines under paragraph 2 above shall include, in respect of the GAB, either outstanding borrowing by the Fund under the GAB or one half of the total of credit lines under the GAB, whichever is the greater.

4. In the case of major developments, the Executive Board shall promptly review, and may adjust, the guidelines. In any event, the guidelines shall be reviewed when the Board of Governors has completed the Eighth General Review of Quotas, and may be adjusted as a result of that review of the guidelines.

5. The percentage limits specified in paragraph 2 above, or any other limits that may be adopted as a result of a review pursuant to paragraph 4 above, are not to be understood, at any time, as targets for borrowing by the Fund.

Decision No. 7040-(82/7)
January 13, 1982

Guidelines for Borrowing by the Fund
Proposed Amendment to Decision

Quota subscriptions are and should remain the basic source of the Fund's financing. However, borrowing by the Fund provides an important temporary supplement to its resources. In present circumstances, it facilitates the provision of balance of payments assistance to ~~its~~ members under the Fund's policies of supplementary financing and enlarged access. The General Arrangements to Borrow (GAB) and associated borrowing arrangements are of increased importance as a potential source of borrowing in the event that the Fund needs supplementary resources to forestall or cope with an impairment of the international monetary system.

The confidence of present and potential creditors in the Fund will depend not only on the prudence and soundness of its financial policies but also on the effective performance of its various responsibilities, including, in particular, its success in promoting adjustment.

Against this background the Executive Board approves the following guidelines on borrowing by the Fund.

1. Fund borrowing shall remain subject to a process of continuous monitoring by the Executive Board in the light of the above considerations. For this purpose, the Executive Board will regularly review the Fund's liquidity and financial position, taking into account all relevant factors of a quantitative and qualitative nature.

2. Subject to paragraph 4 below, the Fund will not allow the total of outstanding borrowing plus unused credit lines to exceed ~~the range of 50-60 per cent~~ [60 percent] [two thirds] of the total of Fund quotas. ~~If~~

~~the total of outstanding borrowing plus unused credit lines reaches the level of 50 per cent of quotas, the Executive Board shall assess the various technical factors that determine, at that time, the availability of balances of unused lines of credit. While this assessment is being made, the total of outstanding borrowing plus unused credit lines may rise, if necessary, beyond 50 per cent, but shall not exceed 60 per cent of total quotas.~~

3. ~~Recognizing that the credit lines of all participants in the General Arrangements to Borrow (GAB) cannot be used at the same time and that the GAB can be activated only to finance purchases by a GAB participant,~~ The total of outstanding borrowing plus unused credit lines under paragraph 2 above shall include, in respect of the GAB and borrowing arrangements associated with the GAB, either outstanding borrowing by the Fund under ~~the GAB~~ these arrangements, or ~~one half~~ two thirds of the total of credit lines under ~~the GAB~~ these arrangements, whichever is the greater.

4. In the case of major developments, the Executive Board shall promptly review, and may adjust, the guidelines. In any event, the guidelines shall be reviewed when the Board of Governors has completed the ~~Eighth~~ Ninth General Review of Quotas, or when there is a change in the GAB or associated arrangements, and may be adjusted as a result of ~~that~~ such reviews ~~of the guidelines~~.

5. The ~~percentage~~ limits specified in paragraph 2 above, or any other limits that may be adopted as a result of a review pursuant to

paragraph 4 above, ~~are~~ is not to be understood, at any time, as a targets for borrowing by the Fund.

Decision No. 7040-(82/7),
January 13, 1982
as amended by
(date), 1983