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April 14, 1983

To: Members of the Executive Board

From: The Secretary

Subject: Meeting of the UNCTAD Committee on Invisibles and Financing Related to Trade

Attached for the information of the Executive Directors is a report by the Fund observers on the meeting of the UNCTAD Committee on Invisibles and Financing Related to Trade, held in Geneva from March 1 to 11, 1983.

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INTERNATIONAL MONETARY FUND

UNCTAD--Committee on Invisibles and Financing Related to Trade
Second Part of the Tenth Session

Report by the Fund Observers 1/

April 13, 1983

1. Introduction and summary

The second part of the tenth session of the Committee on Invisibles and Financing Related to Trade (CIFT) took place in Geneva from March 1-11, 1983 under the chairmanship of Mr. M. Aleman of Ecuador. Messrs. Jack Barnouin and Richard Eglin of the Geneva Office attended as Fund observers.

The agenda contained six basic issues, namely, the requirements of an effective system of international financial cooperation, the flow of financial resources to developing countries, the access of developing countries to capital markets, international monetary issues, a review of current trends in Official Development Assistance (ODA), and an evaluation of the operational features of an Export Credit Guarantee Facility (ECGF). 2/ The discussion of these issues took place in the context of financial and monetary issues to be considered at the Sixth Conference of UNCTAD in Belgrade in June 1983. 3/ The first four issues were discussed collectively. Distinct positions were adopted by the Group of 77 and the Group B countries, with the former indicating that significant reforms were desirable in the international financial system, and the latter stating that the system was fundamentally sound. On the fifth issue, there was broad consensus that the volume of ODA was inadequate to meet the critical needs of developing countries and that priority should be given to the adoption of measures designed to accelerate the attainment of the target of 0.7 per cent of GNP for ODA. On the sixth issue, the Committee adopted a decision to request the Trade and Development Board at its twenty-sixth session to further consider an international ECGF.

2. International financial and monetary issues 4/

The UNCTAD representative noted that, while the international financial system had afforded a measure of insulation from external disturbances to developing countries during the 1970s, unprecedented pressures were now being placed on their external payments by the world economic crisis. Among those pressures, he emphasized the depressed levels of imports in developed economies, the increase in prices of manufactured imports, adverse movements in the prices of primary commodities

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1/ Documents referred to in this report will be on file in the Secretary's Department.
2/ UNCTAD document TD/B/C.3/175/Add.1.
3/ "UNCTAD VI, International Financial and Monetary Issues," TD/275.
4/ UNCTAD document TD/275.

and energy, the rise in international interest rates, and the growth of protectionism. Many developing countries were finding it increasingly difficult to finance their import requirements and their debt service obligations out of available supplies of foreign exchange, while at the same time the private banking system was becoming reluctant to increase its exposure to developing countries. He noted that a number of significant changes, such as closer cooperation among individual commercial banks and the IMF, had already occurred in response to the current crisis. However, he stated, sufficient changes had not yet taken place to restore the momentum of the development process and to avert a worsening of the financial difficulties of developing countries.

He introduced the policy proposals of the UNCTAD secretariat for addressing current international financial and monetary problems and noted that these included an emergency financing program for the next two years in favor of developing countries involving a sum of about US$70 billion. Because of the need for immediate action, this additional financing would have to come from international mechanisms which were already in place, and among the measures that UNCTAD was proposing were an SDR allocation of at least SDR 30 billion in the current basic period, the re-establishment of the Trust Fund financed by the sale of a significant proportion of the IMF's gold stock, the liberalization of the Compensatory Financing Facility so as to provide 100 per cent coverage of an export shortfall in the shortfall year, an acceleration of the IBRD's regular lending program, and short-term generalized debt renegotiation to relieve developing countries of a substantial proportion of their debt servicing obligations over the next two years. He added that the proposed increases in financial flows from the IMF and the IBRD should be accompanied by reconsideration of the conditionality attached to such flows. He concluded that, in addition to this financing program of US$70 billion, there was a need over the longer term to address the underlying deficiencies of the international monetary and financial system that had contributed to the present difficulties.

The spokesman for Group B acknowledged the serious financial problems of many developing countries and noted that additional funding might be needed. He stated that it was important to differentiate structural problems from those which were largely due to the current economic situation. The Group B countries were aware that the least developed countries were less well placed than other developing countries to benefit from an upturn in the world economy, and that such countries should be the beneficiaries of a special effort on the part of the international community.

Commenting on the introductory statement made by the UNCTAD spokesman, he noted that Group B was of the opinion that efforts to mobilize resources should continue within the existing institutional framework. He stated that the decision to increase IMF quotas and the enlargement of the General Arrangement to Borrow showed that the current system is capable of flexibility. He further stated that measures to improve the functioning of the international monetary system were being studied by the competent institutions. On the specific policy proposals made by the UNCTAD secretariat, he cautioned against discussion of topics at UNCTAD VI which UNCTAD was neither technically nor juridically competent to handle. In particular, he emphasized that, in discussing the foreign debt of developing countries, delegations to UNCTAD VI should be careful not to compromise the delicate balance which had been worked out between governments, private banks, and the IMF.

The representative of the Federal Republic of Germany, speaking on behalf of the European Communities (EC), associated the member states of the EC completely with the statement by the spokesman for Group B, but added a number of comments. He stated that additional financing was still needed for developing countries and that the EC had been in favor of a larger increase in resources for the IMF than had been agreed upon at the Interim Committee meeting; he urged all member countries of the IMF to ratify the Eighth Quota Review as soon as possible. He went on to emphasize, however, that current problems could not be solved only by the provision of additional funding, but that the correct balance between appropriate domestic adjustment policies and financing should be struck in developing countries. To achieve this, he stated, a strong IMF was necessary. He noted that, on the issue of debt relief, the EC remained attached to a case-by-case approach. In conclusion, he stated that the EC did not feel it appropriate for UNCTAD to become a forum for a debate on the reform of the international financial institutions. While a general discussion could be held on problems with a view to formulating suggestions, the actual decision-making remained the responsibility of the governing bodies of the IMF and the World Bank.

The spokesman for Group D outlined the state of chronic crisis in the world capitalist economy, arguing that the capitalist system operated in such a way as to serve the interests of monopolies at the expense of developing countries. He stated that developing countries shared a variety of important advantages in their economic relations with Group D countries, such as having equal rights and, in a number of respects, enjoying unilateral advantages. He noted that the Group D countries were ready to pursue the further development of their financial and economic relations with the developing countries but, he said, the same criteria to measure cooperation that were appropriate for the developed market economy countries could not be applied to the Group D countries. In particular, it was pointless to demand that the Group D countries provide a fixed proportion of their national product as aid for developing countries.

The representative of New Zealand associated himself with the Group B statement, and drew attention to the address of the Prime Minister of New Zealand to the European Management Forum at Davos, Switzerland, in January 1983. Summarizing various points made in this address, he noted that the responsibility for solving the current problems of the financial and trading systems should be assumed by all countries. Unstable exchange rates, he said, distorted commercial policy and affected the capability of countries to service debt out of export earnings. He stated that he did not wish to question the jurisdictional competence of any international organization, but he felt there was no monopoly on wisdom and that neither the financial nor the trading system should be immune from systematic scrutiny.

The spokesman for the Group of 77 welcomed the link which was being made between trade, finance, and development. He said that the Group of 77 accepted the main thrust of UNCTAD document TD/275 and wished to draw attention to the current economic crisis which was threatening to undermine the efforts and achievements of developing countries during recent decades. He stated that the Group of 77 had long urged Group B countries to facilitate the access of developing countries to international capital markets, but access had now become very difficult. He recalled recent statements by officials of both private and official financial and monetary institutions indicating a growing awareness of the need for a strengthening of international capital markets, and he suggested this topic should be discussed in depth at Belgrade. He also stated that the issue of a fundamental reform of the international monetary system should be considered at UNCTAD VI and, while it had to be accepted that decisions in UNCTAD would not result in measures such as increases in IMF quotas, the Group of 77 believed that UNCTAD was an appropriate forum in which to argue the case for the need for a certain level of resource transfers on favorable conditions to the developing countries. He added, however, that developing countries would need more effective management of their domestic economies.

The representative of the United States reviewed developments in the international economic system over the past few decades, noting that the system had shown remarkable strength and resiliency and that the Bretton Woods institutions and the GATT-based trading system were proving themselves to be sufficiently flexible to deal with the current economic crisis. The world economy was in the midst of a painful but unavoidable adjustment, but fortunately all leading indicators now pointed to recovery. The key issue facing the international community was whether countries still experiencing acute financial difficulties would be able to make the required economic adjustments in an orderly manner so as to lay the basis for prompt restoration of their creditworthiness and to preserve the stability of the world trading and financial system. He was confident that there would be sufficient international financing to support the efforts of those countries seeking to adjust.

He stated that the United States was supporting a comprehensive strategy to deal with current economic and financial difficulties. This strategy had five main parts. First, and most important in the long run, was orderly and effective adjustment in all countries experiencing payments difficulties. Such adjustment should take place with the support and assistance of the IMF. Second was the continued availability of official balance of payments financing on a sufficient scale, through the IMF. He noted that his Government had supported an increase in IMF quotas of 47.5 per cent, and an expansion of the General Arrangement to

Borrow. Third was the need to work toward consensus among governments and central banks in lending countries to act quickly in response to debt emergencies. The appropriate framework for this response, which should be made effective on a case-by-case basis, was ad hoc arrangements among finance ministries and central banks, often in cooperation with the Bank for International Settlements, to assist countries engaging in negotiations with the IMF and other creditors. Fourth was the assurance of continued commercial bank lending to countries that were pursuing sound policies, including, where needed, adjustment programs. Fifth was the restoration of sustainable economic growth and the preservation and strengthening of the free trading system.

The representative of China stated that he felt UNCTAD VI should be approached as the appropriate forum for reaching a common understanding and agreement between developed and developing countries. In his view, there existed a severe problem of inadequate financial resources in the current international monetary and financial system. The role of private financial resources in improving international financial cooperation should not be overemphasized, since private market lending was not of a concessional nature. He added that, judging by the plight facing the developing countries, the conditionality of multilateral financial institutions had become tighter, and surveillance by the international monetary system did not apply effectively to the large economic powers, even though their economic policies had adverse impacts on global interest rates and exchange rates.

In summing up, the Chairman drew the distinction between the view of the Group of 77, which believed that structural reform of the international financial and monetary system was urgently needed and that a substantial increase in resources should be available to the developing countries from official sources to help finance their economic adjustment programs, and the view of the Group B countries that the present task was to strengthen rather than reform the system and that it was unclear how UNCTAD VI could be useful with regard to the question of IMF resources.

3. Official Development Assistance 1/

The UNCTAD representative noted that total ODA flows from DAC member countries measured in dollar and nominal terms had declined slightly in 1981 from the levels reached in 1980, and that a particularly important factor in the decline had been a reduction in flows from the United States. The overall ratio of ODA to GNP of DAC member countries had declined from 0.33 per cent in 1980 to 0.32 per cent in 1981. The probability that DAC member countries would collectively attain the 0.7 per cent target by 1985 appeared to be nil. In addition, little progress had been made by DAC member countries toward increasing the concessionality of their assistance. The spokesman for Group B

1/ UNCTAD document TD/B/C.3/184.

noted that OECD Ministers had reaffirmed their governments' determination in May 1982 to maintain and, to the best of their ability, to increase the volume of aid to developing countries, while at the same time stressing the importance of efforts to improve the quality and effectiveness of aid. He remarked that the decline in dollar terms of ODA by DAC countries in 1981 had been largely due to special factors such as timing of multilateral contributions and exchange rate effects, and that actual ODA receipts by developing countries, measured in real dollar terms, had remained roughly constant. He also pointed out that the aid figures needed to be seen in the context of the total resource flows to developing countries which, on a net basis and including private flows, had constituted 1.21 per cent of the GNP of the DAC countries in 1981. He stated that ODA in 1980 had accounted for 10 per cent of the least developed countries' GNP, 50 per cent of their current imports, and 80 per cent of their investment, and he emphasized the dependency of such countries on a high and continuing level of aid flows.

The spokesman for the Group of 77 said that the situation as regards ODA was highly unsatisfactory and that the quantity and quality of ODA flows must be improved. He stated that the way in which this subject had been approached in UNCTAD was also unsatisfactory, given its vital importance to a large number of developing countries, and he regretted that a sessional committee had not been set up to deal specifically with this item. He remarked that it was very disappointing that these flows were declining in real terms at a time when the least developed countries were badly hit through deteriorating terms of trade, the collapse of commodity prices, and losses through exchange rate fluctuations. In connection with the difficulties experienced by developing countries in meeting the ODA target, he referred to a statement made by the Prime Minister of New Zealand that new global mechanisms be explored for resource transfers, particularly the SDR development assistance link proposed by the Group of 77.

The representative of China noted that the severe inadequacy of financial flows had forced many developing countries to cut back imports, investment, and consumption, and he noted that, in some low-income developing countries, the rate of economic growth had already fallen behind the rate of population growth. Although his country had always believed that developing countries should base their economic development on their own efforts, the unfavorable world economic situation made it essential that the major developed countries should provide more ODA and preferential loans, reduce tariff barriers, lower interest rates, and stabilize exchange rates. IMF quotas should be increased substantially, immediate consideration should be given to an additional allocation of SDRs, and the conditionality of IMF loans should be relaxed. The seventh IDA replenishment should be completed in the year originally envisaged, and the World Bank should explore ways of expanding its lending capacity. Resolutions on debt adopted in the past, especially those related to the reduction or the cancellation of debt, should be fully implemented, and immediate attention should be given to the debt servicing problems of the developing countries.

In his summing up, the Chairman stated that there was broad agreement that the flow of ODA was inadequate to meet the needs of developing countries, and that greater efforts should be made by developed countries to increase concessional flows in real terms.

4. Evaluation of the operational features of an Export Credit Guarantee Facility (ECGF) 1/

In his introductory statement, the Chairman recalled that the essential objective of the ECGF was the promotion of developing countries' exports. Market access was of vital importance to newly industrialized developing countries, but, with rising protectionism in the industrialized countries, the markets of other developing countries were assuming greater importance. Lack of capital meant that developing country exporters were not in a position to provide the export financing required by developing country importers, and the ECGF offered a solution by allowing developing countries' export papers to be refinanced in international capital markets at favorable rates. The UNCTAD spokesman presented the documentation that had been prepared by the secretariat in response to a request for further clarification in three particular areas by the Intergovernmental Group of Experts which had been working on the proposed facility since January 1982.

The spokesman for Group B noted that a model for a complete scheme of the proposed ECGF was now available for the first time, but that the proposed scheme raised issues of both a fundamental and practical order. A number of Group B countries had significant reservations about its basic concept, while others still required clarification on a number of important issues.

The spokesman for the Group of 77 regretted that the Group B countries were still not prepared to accept the establishment of the facility, particularly since he felt all the technical questions had now been satisfactorily resolved. He called for the World Bank's greater involvement in encouraging the establishment of this facility.

There then followed extensive discussion of specific questions on which Group B countries required further clarification, but in most cases the discussion was inconclusive. In his summing up of the debate, the spokesman for Group B noted that his countries were still not satisfied on the questions of additionality, the beneficiaries of the scheme, the financing of the facility, the proportion of capital subscribed by developing countries, and the relationship of this to voting structure. Group B, he remarked, required satisfactory responses to these questions.

The Sub-Committee adopted a decision requesting the Trade and Development Board at its twenty-sixth session to make appropriate arrangements for the further consideration of an ECGF. 2/

1/ UNCTAD documents TD/B/C.3/183 and Add.1, Add.2, and Add.3.
2/ UNCTAD document TD/B/C.3/L.143.