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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 83/103

3:00 p.m., July 13, 1983

J. de Larosière, Chairman
W. B. Dale, Deputy Managing Director

Executive Directors	Alternate Executive Directors
	L. K. Doe, Temporary
J. de Groote	
	P. D. Péroz, Temporary
	R. J. J. Costa, Temporary
	T. A. Connors, Temporary
M. Finaish	T. Alhaimus
T. Hirao	T. Yamashita
J. E. Ismael	Jaafar A.
	D. I. S. Shaw, Temporary
	C. Robalino
G. Laske	G. Grosche
G. Lovato	C. P. Caranicas
R. N. Malhotra	
Y. A. Nimatallah	
J. J. Polak	
	K. G. Morrell
G. Salehkhou	
	E. I. M. Mtei
	S. E. Conrado, Temporary
J. Tvedt	A. Lindø
	C. Taylor
Zhang Z.	Wang E.

L. Van Houtven, Secretary
B. J. Owen, Assistant

Also Present

External Relations Department: N. K. Humphreys, H. P. Puentes. Legal Department: G. P. Nicoletopoulos, Director; G. F. Rea, Deputy General Counsel; W. E. Holder, Ph. Lachman, A. O. Liuksila. Middle Eastern Department: S. von Post. Research Department: A. Crockett, Deputy Director; R. R. Rhomberg, Deputy Director; C. P. Blackwell, J. E. Blalock. Secretary's Department: J. W. Lang, Jr., Deputy Secretary; A. Wright, Deputy Secretary. Treasurer's Department: W. O. Habermeier, Counsellor and Treasurer; D. Williams, Deputy Treasurer; D. H. Brown, A. G. Chandavarkar, W. L. Coats, Jr., D. S. Cutler, D. Gupta, O. Roncesvalles, M. A. Tareen, P. van den Bogaerde, G. Wittich. Bureau of Language Services: A. J. Beith, Director. Personal Assistant to the Managing Director: N. Carter. Advisors to Executive Directors: J. R. N. Almeida, C. J. Batliwalla, S. El-Khouri, S. M. Hassan, I. R. Panday. Assistants to Executive Directors: E. M. Ainley, H. Arias, L. Barbone, R. Bernardo, J. Bulloch, M. Camara, M. B. Chatah, L. E. J. Coene, G. Ercel, I. Fridriksson, M. Hull, H. Kobayashi, M. J. Kooymans, P. Leeahtam, V. K. S. Nair, Y. Okubo, J. K. Orleans-Lindsay, E. Portas, M. Z. M. Qureshi, J. Reddy, J. Schuijer, M. Toro.

1. REPORT BY MANAGING DIRECTOR

The Managing Director said that while he had been in Geneva on July 8 to address the Economic and Social Council of the United Nations (ECOSOC), he had met a number of Ambassadors to the United Nations at a luncheon on that day, and had had useful conversations with them on matters pertaining to the Fund--the international monetary situation, the role of the institution, the indebtedness of deficit countries--as well as on matters concerning UNCTAD and its recently completed Sixth Conference in Belgrade. The nature of the questions raised had revealed the interest in and growing understanding of the necessity of adjustment efforts, and of the ways in which the Fund could help member countries to carry them out.

The meeting of the G-10 Deputies had taken place in Paris on the same day, the Managing Director noted, and he had returned there that evening to have an informal dinner with some of the participants, and had thus been briefed further about the G-10 meeting.

On Monday, July 11, he had participated in the meeting of the Governors of central banks at the Bank for International Settlements (BIS) in Basle, the Managing Director observed. He had been asked to explain the Fund's liquidity situation, which he had done on the basis of the information circulated to the Executive Board, together with the views of Executive Directors. He had explained that the long-standing policy of the Board was not to commit more resources than the Fund had on hand or had arranged to obtain in a suitable manner. Thus, he had stressed the importance of the Fund's not being caught in a commitment gap, which had reached SDR 2.4 billion and could well rise to SDR 6 billion toward the end of 1983. It was therefore a matter of urgent necessity, he had stressed, to cover the gap, irrespective of the progress with the approval of the quota increase that was under way in member countries. No one had denied the need to fill the gap on the grounds that Fund quotas would eventually be increased.

The problem of the Fund's need to borrow had thereby been clearly posed, the Managing Director said. He had explained the views that the management and staff had been developing in the recent past to deal with the problem, adding that he would be meeting the next day with the Minister of Finance of Saudi Arabia. Although no decisions had been taken, the discussion had been constructive, and the requirements of the Fund were understood.

He had informed the Saudi Arabian Minister of Finance, Mr. Abal-Khail, of what he had told the central bank Governors, and of what he had in turn been authorized by them to say to the Minister, the Managing Director stated. He had been heartened by the Minister's most cooperative attitude.

Further work was needed on various technical matters, both with the BIS and with the Saudi Arabian authorities, the Managing Director said. He expressed the hope that, based on the understanding of the Fund's problems and the cooperative attitude taken toward their solution, it would be possible to reach final decisions by the time of the monthly meeting of the BIS scheduled for September.

2. SDR INTEREST RATE AND RELATED MATTERS, AND OFFICIAL ADOPTION OF TERM "SDR"

The Executive Directors resumed from the previous meeting their consideration of a staff paper on the SDR interest rate and related matters (SM/83/137, 6/21/83), together with a proposal to adopt officially the term "SDR" (SM/83/139, 6/21/83).

The Deputy Managing Director indicated that changes in the SDR interest rate, including the method of calculation, required a special majority of 70 percent of the total voting power for adoption, as did changes in the rate of remuneration. That majority would thus apply to the proposals in subparagraphs (i) and (ii) on pages 12 and 13 of SM/83/137. The special majority did not apply to the greater frequency of payments, either with respect to interest on the SDR and charges or with respect to remuneration, which was proposed in subparagraph (iii) on page 13 of that paper. Taken as a separate issue, the frequency of payment could be decided by a simple majority, but as an economic matter, it was nonethless, an element in the calculation of the real return on the SDR and reserve positions. Thus, technically, a 70 percent majority for the adoption of the decision as a whole would be required, and would be generally in the spirit of the voting provisions.

The normal way to conclude the discussion, the Deputy Managing Director added, would be to prepare a draft decision that would encompass all the changes that had been proposed and approved.

Mr. Laske welcomed clarification of the voting procedures on the two aspects of the matter under discussion. Would it be possible to leave open the question whether or not the decision should cover all aspects, or whether they should be dealt with separately?

Mr. Malhotra wondered whether a similar issue had arisen in the past. If the frequency of payment resulted in an effective increase in the SDR interest rate, the rate of remuneration, or charges, as the whole tenor of the staff paper suggested, there would seem to be a prima facie case for applying the provision calling for a 70 percent majority of the total voting power. If the issue had to be decided, further time would be needed to consider it.

The Deputy Managing Director said that the issue need not be decided forthwith.

Mr. Alhaimus said that he agreed with the staff's proposals. His chair had consistently called for an improvement in the SDR, and the changes suggested were a modest contribution in that direction. Although he had the same concerns as others relating to the possible additional cost of using the SDR, he also looked forward to more fundamental steps to enhance the role of the SDR, particularly through the resumption of allocations.

He could accept the adoption of the term "SDR," which had already become sufficiently familiar, Mr. Alhaimus indicated.

Mr. Zhang said that he could go along with the staff proposals as a whole. From a purely technical point of view, the changes suggested would tend to strengthen the role of the SDR as an international reserve asset. However, he had some reservations about the third part of the proposals. Changing the frequency of payment from an annual to a quarterly basis would inevitably increase the financial burden of the borrowing developing countries.

He supported the proposal to adopt officially the term "SDR," Mr. Zhang stated.

Mr. Morrell said that he could support the proposals enumerated in the conclusions of SM/83/137. They were broadly in line with the position taken by his chair during the discussions held in 1982. The attractiveness of the SDR as a reserve asset should be enhanced by the improvement of its yield, compared with that on other investment assets. Weekly adjustments in the SDR rate would be more convenient administratively than daily fixings and would entail no significant departure from market rates. He had also noted that the quarterly payment of interest would increase the effective yield to the holders of SDRs, through the compounding effect. He supported the proposal to increase the frequency of payment on the balance of the merits of the case, even though increased yield would be translated into increased costs for the net users of SDRs, many of which were countries with heavy debt burdens.

Finally, Mr. Morrell stated, he supported the proposed adoption of the acronym "SDR."

Mr. Costa said that his chair supported the proposals in both SM/83/137 and SM/83/139.

Mr. Ismael said that he had no objection to the proposed change in the frequency with which the SDR rate was to be determined, or with fixing the rate weekly, based on Friday's combined market rate. However, he had serious reservations about the proposal to compound interest on the SDR each quarter. He had been informed that charges had been raised in 1982 from 6.25 percent to 6.6 percent and that, partly as a result, the net income target of 3 percent of reserves for the financial year 1982/83 had been substantially exceeded. When the Fund's income position for that year had been reviewed in May (EBM/83/70, 5/16/83), numerous arguments had been put forward by Executive Directors for applying the excess of net income toward reducing the level of charges in the financial year 1983/84. Therefore, in his opinion, it was inappropriate to introduce at the present stage innovations that would increase the cost of using the Fund's resources. A substantial element of concessionality should be maintained in order to encourage members to adopt programs supported by the Fund at an early stage of their difficulties. In the circumstances, his preference was to maintain the annual payment of remuneration on reserve positions and interest on SDR holdings.

Although he had no objection to the change in accounting procedures, so that interest on SDRs and charges, as well as remuneration, could be paid on the first day of the new accounting period, he was not convinced by the rationale for the change. As far as he knew, it was standard banking practice to credit an account with interest on the last day of the payment period.

He supported the staff's recommendation to adopt officially the term "SDR," Mr. Ismael concluded.

The Treasurer, responding to Mr. Lovato's questions about the status of proposals to improve the attributes of the SDR to make it a more useful and competitive reserve asset, noted that the question of dealings in SDRs among official holders at nonofficial rates, within a margin, would be taken up in the paper on the simplification of operations in SDRs. That paper was close to completion by the staff and was presently scheduled for discussion early in September. Further work had also been done by the staff on the role of the Fund as a broker in bringing together parties interested, for instance, in exchanging SDRs against other assets, or in loans. The staff paper on that topic would take longer to complete. Another important subject on which work was under way concerned the appropriate level for the SDR interest rate.

The staff had taken note on a previous occasion of the more fundamental issue to which Mr. Polak had referred, the Treasurer observed, namely, the role of SDRs in financing the Fund. It was a far-reaching question, to which the staff had not yet found the full answer. So far, the issue had been approached as part of a broader analysis of Fund financing, because other techniques were possible, although the SDR might have a role to play as well.

On the more technical questions that had been raised concerning the changes in the method for determining the SDR interest rate, the Treasurer assured Mr. Laske that the staff would have to notify members officially of the new rate established on Friday by the opening of business on Monday. Certain technical questions had to be discussed with the U.S. Treasury, but, with its cooperation, the rate should be available over the weekend.

As for Mr. Laske's remark about the anomaly of not paying SDR interest, charges, and remuneration for the first quarter of 1983 until the end of the year, after payment had been made for the three last quarters, the Treasurer said that it would be feasible from an accounting point of view for interest and charges, which accrued daily, to be paid promptly. The proposal had been made for legal reasons.

A preference had been expressed by Mr. Malhotra for not using the combined market rate for a single day as a reference, but for taking an average rate for two or three days, the Treasurer observed, on the logical grounds that there was no reason to assume that experience was a guide to the future. The same argument could be made about averages, which might be no better than a single rate as an indicator. Moreover, it was standard market practice not to average. It might perhaps be reassuring to note that the shift to fixing the rate 52 times a year instead of 4 times a year was in a sense an averaging process; any aberration within a single day's rate would be quickly offset. The accounting procedures were being changed for technical reasons, in order to simplify the present method, not to change their nature or the amount of interest and charges that accrued.

It would not be possible to give members the choice of quarterly or annual payment of SDR interest and charges, the Treasurer said in response to Mr. Sangare's suggestion, because of the possibility of creating imbalances between the charges received from net users and the interest paid to creditors. The equivalence of the two items was a key feature of the Special Drawing Account. Although many developing countries were net users of SDRs, others had significant SDR holdings. Furthermore, some industrial countries made large net use of SDRs; their costs would also rise.

Mr. Malhotra asked whether the same would apply to remuneration.

The Treasurer replied that although over a recent period debtor positions in the General Resources Account had been exclusively those of countries classified as developing, those debtor positions nevertheless created creditor positions that were remunerated. There were developing and industrial countries among the creditors.

The staff representative from the Treasurer's Department explained that interest and charges on members' SDR positions were calculated at the close of each day, with the exception of the day on which SDR interest and charges were debited and credited. For that purpose, the books were closed on that day to show the balance; after the amount of interest and charges had been determined, the books reopened, and the debit and credit entries were made. Therefore, whether those debits and credits were entered on the closing day of the period or on the opening of the first day of the next period was of no consequence whatsoever for the calculation of interest on holdings and on charges on net use. The only difference was the period for which the payments were shown in the books of the Special Drawing Rights Department. The change in the accounting procedure would simplify the calculations and clarify what was in fact being done.

The Deputy General Counsel explained that the proposal to pay interest and charges that had accrued during the current quarter at the end of the year, in accordance with the present rules, was based on the principle of retroactivity. The accepted practice of the Fund was to avoid decisions that were retroactive in effect, at least to the extent that members could suffer detriment. The proposals under discussion related to the acceleration of a future date for the payment of interest and charges accruing during the current quarter; presumably, holders had adjusted their positions to take into account, among other things, that payment of charges would not be due until the end of the year, giving them time in the interim period to make further adjustments to their holdings to avoid charges on a net basis. To deprive members of that flexibility by accelerating the date of payment, so close to the end of the quarter, could run counter to the principle of retroactivity. Such acceleration should, therefore, be avoided.

The Articles of Agreement did not explicitly provide that interest and charges on SDRs should always be paid on the same date, the Deputy General Counsel remarked, but the whole concept of the SDR system written into the Articles did presuppose a balance between interest and charges. That balance would obviously be upset if members were given an option to pay charges at different dates from the date on which interest was paid.

A minor editorial amendment to the draft of the new Rule B-6 would eliminate a certain lack of clarity, the Deputy General Counsel said. He suggested that the proviso read "...provided that if the text is in a language in which a different usage has become established, then that usage may be retained."

The Deputy Managing Director summed up the discussion. He noted that Mr. Wicks, supported by several other Executive Directors, had encouraged the staff to do further work on the broader topic of the SDR, its role in the system, and its further development in accordance with the Articles of Agreement. Several other Directors had supported the idea. It seemed appropriate to include such a separate work program in the overall program of work that would be drawn up for the period following the Annual Meeting in order to maintain the momentum.

On the particular proposals before the Executive Board, the Deputy Managing Director noted, there had been no opposition to the proposals in subparagraphs (i) and (ii) relating to the calculation of the rates and the use of a single reference day. On the proposal in subparagraph (iii) to pay interest on the SDR, charges, and remuneration more frequently, a number of Directors had indicated concern about the effect due to compounding on the users of SDRs and of the Fund's general resources. The effect of the slight increase in the rate of remuneration could of course be felt eventually in the rate of charge in the General Resources Account. Four Executive Directors had indicated unequivocally that they would not support the proposal in subparagraph (iii) on page 13 of SM/83/137, but four other Directors had taken a less certain position. But on the most cautious calculation of the positions of Executive Directors on the proposal, and on the assumption that a package decision would require a 70 percent majority of the total voting power, the required majority for accepting the proposal would be achieved. Thus, it would be unnecessary to consider the question of a separate decision, as had been mentioned at the beginning of the meeting.

It was clear that Directors were willing to have the Fund adopt officially the term "SDR," the Deputy Managing Director said, despite the suggestion that a more suitable name be considered whenever the Articles of Agreement were amended. There had not been widespread support for

Mr. Polak's suggestion that the term "SDR" be used in all languages. Therefore, it seemed appropriate to adopt Rule B-6 as amended. The amendments to the relevant rules, together with draft decisions, would be circulated for approval on a lapse of time basis (see EBD/83/196, 7/21/83).

DECISION TAKEN SINCE PREVIOUS BOARD MEETING

The following decision was adopted by the Executive Board without meeting in the period between EBM/83/102 (7/13/83) and EBM/83/103 (7/13/83).

3. EXECUTIVE BOARD TRAVEL

Travel by an Assistant to an Executive Director as set forth in EBAP/83/186 (7/12/83) is approved.

APPROVED: January 4, 1984

ALAN WRIGHT
Acting Secretary