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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 83/129

3:00 p.m., September 2, 1983

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

Executive Directors	Alternate Executive Directors
	J. K. Orleans-Lindsay, Temporary
	H. G. Schneider
B. de Maulde	X. Blandin
A. Donoso	
R. D. Erb	
	T. Alhaimus
T. Hirao	T. Yamashita
	J. Reddy, Temporary
R. K. Joyce	
A. Kafka	C. Robalino
G. Laske	G. Grosche
G. Lovato	
R. N. Malhotra	
Y. A. Nimatallah	
J. J. Polak	
	K. G. Morrell
G. Salehkhou	
	E. I. M. Mtei
	E. Portas, Temporary
N. Wicks	
	Wang E.

A. Wright, Acting Secretary
J. A. Kay, Assistant

Also Present

African Department: F. d'A. Collings. Asian Department: S. Shah, H. O. Roden. European Department: M. Xafa. External Relations Department: R. W. Russell. Legal Department: G. P. Nicoletopoulos, Director; J. G. Evans Jr., Deputy General Counsel; S. A. Silard. Research Department: W. C. Hood, Economic Counsellor and Director; N. M. Kaibni, T. K. Morrison. Treasurer's Department: W. O. Habermeier, Counsellor and Treasurer; D. Berthet, D. S. Cutler, D. Gupta, Q. M. Hafiz, N. Hayashi, T. Leddy, D. V. Pritchett, T. M. Tran, G. Wittich. Western Hemisphere Department: S. T. Beza, Associate Director. Personal Assistant to the Managing Director: N. Carter. Advisors to Executive Directors: A. A. Agah, T. A. Connors, S. El-Khouri, S. M. Hassan, P. Kohnert, Y. Okubo, P. D. Péroz. Assistants to Executive Directors: H. A. Arias, L. Barbone, R. Bernardo, J. Bulloch, M. Camara, M. B. Chatah, G. Gomel, V. Govindarajan, A. K. Juusela, H. Kobayashi, P. Leeahtam, W. Moerke, V. K. S. Nair, G. W. K. Pickering, J. Schuijer.

1. FUND LIQUIDITY POSITION AND FINANCING NEEDS

The Executive Directors continued from the previous meeting (EBM/83/128, 9/2/83) their consideration of a report on the Fund's current and prospective liquidity position and financing needs (EBS/83/170, 8/12/83).

Mr. Morrell stated that he was in general agreement with the staff's projections of the Fund's liquidity position until April 1984, although there was more than the usual uncertainty because of the unresolved matter of enlarged access. In the tables prepared by the staff, he had found three particularly significant points. First, of a total of SDR 22.2 billion in undisbursed ordinary and borrowed resources on hand on August 1, 1983, SDR 12.9 billion would be disbursed by April 30, 1984, only eight months hence. Second, the commitment gap in terms of borrowed resources would amount to SDR 6 billion by the end of 1983, in the absence of the conclusion of satisfactory loan arrangements, and SDR 7.8 billion by April 1984. Third, unless the Eighth Quota Review were completed, the Fund's uncommitted ordinary resources would be no more than SDR 4 billion by April 1984. Clearly, such a position would be untenable in view of the Fund's other liabilities. The importance of concluding the Eighth General Review of Quotas and completing further borrowing arrangements could not be overstated. Insofar as borrowing arrangements were concerned, he welcomed the statement that Saudi Arabia was prepared to offer a new line of credit amounting to some SDR 3 billion if the industrial countries or the Bank for International Settlements (BIS) provided a similar amount. He looked forward to hearing in the near future that such an arrangement had been successfully concluded. The estimates for future liquidity needs in EBS/83/133 indicated that even after the agreements to borrow SDR 6 billion were in place, matters would not be easy. He was rather surprised by the forecast that some smaller non-GAB industrial countries might well demand some SDR 3.5 billion of the Fund's resources before April 1986. As none of them at present was making use of the Fund's resources, he wondered what circumstances the staff envisaged that might bring about such a substantial increase in the use of resources.

Table 2 of EBS/83/133, Mr. Morrell noted, showed that the Fund would be confronted with a further need for borrowed resources of between SDR 8.3 billion and SDR 15.5 billion by April 1986. In those circumstances, he wondered how the staff envisaged that the commitments implied in allowing access of 125 percent of quota a year would be financed. He also understood that the staff was predicting some instances of systemic stress. While the forecast clearly indicated that further borrowing would be required, his authorities in general were not yet convinced that the step of borrowing on the private capital markets was desirable.

Mr. Portas said that, like Mr. Wicks, he doubted whether it should be a fundamental principle of the Fund to avoid the emergence of a commitment gap in the Fund's liquidity at all costs. On previous occasions, his chair had indicated the need for a more realistic assessment of the institution's liquidity, not only on a commitment basis but also on the traditional cash or disbursement basis. Only thus could a reasonably long-term view of the Fund's financing requirements be obtained. There was still room for more refinement of the data with a better differentiation between the shorter-term and longer-term liquidity positions of the Fund. Using such an approach, on a disbursement basis, the immediate liquidity situation of the Fund was not as pressing as might be deduced from the staff paper. It would be possible for the Fund to continue disbursing resources to meet members' financing requirements for some time to come. In those circumstances, the Fund should continue its proper role without restricting its financing of members' external imbalances.

Nevertheless, Mr. Portas went on, any commitment gap should be kept within reasonable limits. The present rapidly widening gap did indicate the need for action to secure new borrowing arrangements at an early date in order to prevent any serious deterioration of liquidity even on a disbursement basis. The Managing Director's efforts had been most helpful.

The staff paper made it clear that the Fund would need to borrow more resources, whatever access limits were agreed upon, Mr. Portas commented. For the foreseeable future, borrowing seemed likely to be a more rather than a less permanent feature of the Fund's operation. In those circumstances, early access to private markets, even on an experimental basis, might be quite appropriate. While official borrowing should be undertaken by priority, he doubted whether the Fund could escape having to go to the private markets at a later stage. It would therefore be worthwhile to gain experience in that field, while the Fund was still in a relatively good position.

Mr. Erb said that he had no problems with the staff's estimate of the Fund's liquidity position to the end of FY 1984. As to whether a commitment gap should be allowed to develop, the position of his chair had long been that it was desirable to keep the Fund's commitments in line with the available resources. In that light, it would be desirable to complete the current borrowing program in the near future, as it was clear that an overall commitment gap would develop toward the end of the year. For the longer term, it was important to ensure that commitments did not exceed the available resources. Beyond the end of 1983, he could only refer to the points that he had made during the discussion on access limits with respect to the link between the Fund's resource requirements and the policy on access to those resources, as well as assumptions about the state of the world economy.

Mr. Salehkhou remarked that although developments directly affecting the Fund's finances had largely been in line with the staff's estimates and projections, little had been done by way of reducing pressure on the Fund's resources and improving the short-term and medium-term prospects for its liquidity position. The Fund was perhaps overcautious in its forecast of changes in its liquidity position--a sound and responsible attitude--but the prospective commitment gap for end-December 1983 and end-April 1984 was a major matter of concern. The non-oil developing countries expected the Fund to pursue or intensify its leadership role on the international financial scene at a time when the members' access to other sources of financing was being sharply reduced. Other lenders and participants in world capital markets were increasingly making the provision of additional resources to countries in difficulty contingent upon parallel Fund assistance. The continuation of sufficient capital flows to Third World countries--clearly crucial not only to world economic recovery but also to the stability of the international financial environment--was therefore dependent upon the maintenance of a strong Fund and on the improvement of its financial structure.

The Fund should be in a position to help its members to achieve domestic external adjustments without excessive hardship for their people, Mr. Salehkhou observed. In those circumstances, it was disturbing to note that, while all Executive Directors spoke in favor of strengthening the Fund and particularly improving its liquidity position, in recent months the Fund's response to present difficulties and its proposals for their solution had been largely inconsistent both with its goals and with the Fund's responsibilities in the international field.

First, Mr. Salehkhou considered, there was an undesirable trend toward a sharp tightening of the conditionality attached to both credit tranches and special facilities. Not only did such a trend encourage more countries to seek economic adjustment through administrative regulations and import restrictions; it also resulted in smaller structural adjustments, as most new arrangements with the Fund tended to be of short duration. Second, despite the needs of Third World countries for short-term and medium-term balance of payments assistance, the Eighth General Review of Quotas had clearly resulted in an unduly small increase, implying that substantial recourse to borrowed resources would be a permanent feature of the Fund's financing. Third, there appeared to be a systematic attempt to reduce members' access to Fund resources. The reluctance of many large surplus members, particularly industrial countries, to enter into new borrowing arrangements with the Fund for the purpose of permitting enlarged access to continue seemed to make it inevitable for the Fund to address itself to the private markets to increase its resources. Such a move should continue to be resisted despite the depletion of the Fund's uncommitted ordinary resources, and additional financing should be sought from member countries in strong balance of payments positions. Borrowing from member governments and central banks helped to preserve the integrity and independence of the Fund, and to maintain its cooperative character. Member governments were bound by the Articles of Agreement and were expected to act both responsibly and in line with the general principles of the Fund. During the past year, the availability of resources from members had enabled the Fund to play a strong leadership role in alleviating the strain on the international financial system. He wondered how efficient the Fund would have been during the past year had it been dependent on private international markets to supplement its resources. Besides undermining the Fund's capacity to carry out its stabilization function, such recourse to the private capital markets would certainly put the international banking system in a position to try to influence the policies of the Fund. Still more dangerous, recourse to the private capital markets would reduce the Fund to the role of a mere debt collector or guarantor of lending by private international banks. In brief, there was a pressing need for the Fund to find a solution to its financing problems and to preserve the liquid character of its claims, while continuing to offer the assistance for which it was established and carrying on the leadership role it had recently come to play.

Mr. Laske remarked that the Fund's liquidity position had not changed greatly since the Executive Board had discussed the topic six months previously. Not unexpectedly, the commitment gap had widened, and it might reach as much as SDR 6 billion by the end of 1983. However, on a disbursement basis the Fund seemed to be well equipped for the foreseeable future to honor the commitments that it had entered into in stand-by arrangements. Although the Fund's liquidity situation was tight, it was not unduly worrying. The Saudi Arabian authorities had indicated their readiness to make available additional loans to the Fund, a matter for which they deserved great commendation. Other talks were in progress about additional loans to the Fund, and Executive Directors should try not to disturb them. For the longer term, it was clear that the Fund would not have an abundance of lendable resources at its disposal even after the Eighth Quota Review and the enlargement of the General Arrangements to Borrow came into effect. Consequently, the Fund should exercise extreme caution in selecting the levels of access in the period before the introduction of the Eighth Quota Review. Clearly, what was required was a significant reduction of access in terms of multiples of quotas, accompanied by an early decision gradually to phase out the enlarged access policy as the world economy improved.

Mr. Donoso said that he did see that there was a gap if the arithmetic was carried out on a commitment basis. On the other hand, the SDR 9.1 billion of usable currencies, plus the credit lines in place and not likely to be disbursed by April 1984, when the Eighth General Review of Quotas should come into effect, seemed to be more assuring. He therefore considered the financial situation to be relatively comfortable in view of the events that it was possible to foresee. It was however essential to keep the reserve character of claims intact, and less predictable events might have to be faced. Thus, he understood the importance of maintaining a pool of external liquidity. He therefore endorsed the desirability of avoiding commitment gaps and supported any action to enter new borrowing arrangements.

Mr. Malhotra stated that he too had noted that the Fund's liquidity position had not changed greatly in the past six months. However, the commitment gap expected by the end of April 1984 was large, and he hoped that the Managing Director would succeed in his discussions with various official authorities about bridging it. His chair had in the past stressed the need for other resources, such as the General Arrangements to Borrow and associated arrangements, to be activated as soon as possible.

The difference between the existence of a gap on a commitment basis and the lack of a gap on a disbursement basis was a matter that needed further discussion, Mr. Malhotra considered. In the present difficult circumstances, the Fund must respond effectively to the needs of its members. For that purpose, he had urged the maintenance of access at the present level of multiples of quotas. At the same time, he had urged that the Fund should be enabled to mobilize adequate resources. He was glad to hear that the Managing Director considered that the Fund would be able to finance access at the level of 125 percent of new quotas for one year or 375 percent for three years. Nevertheless, every effort should be made to prevent the access of members in real terms from being reduced. For that purpose, several courses of action could be considered. If there were to be a choice between meeting the legitimate requirements of members and allowing a commitment gap to arise, he would be in favor of meeting the requirements of members, provided that the commitment gap was kept within reasonable limits. As to the provision of additional resources, his preference was to rely on members' quotas. However, the Eighth Quota Review had clearly been inadequate, causing some Directors to talk of reducing access limits to preserve the Fund's liquidity. It was therefore most important that the Ninth Quota Review should be brought forward and that a substantial increase in quotas should take place at that time. Meanwhile, all other financing arrangements should be activated. If still further financing was needed, he would not mind the Fund's approaching the capital markets for a limited time. The staff believed that after April 1986 money would start flowing back into the Fund. If that were true, he would be less hesitant about borrowing from the market, because borrowing would not be for long, and the commitment gap would remain only for a short period.

The Treasurer said that he would comment, first on the presentation of the Fund's liquidity; second, on the estimates put forward by the staff; and, third, on some of the fundamental questions raised by Executive Directors regarding the assessment of the Fund's liquidity, with special reference to the commitment gap and the minimum cash position that the Fund could afford to hold. Regarding the presentation of the Fund's liquidity, it was clear that the task for the staff was to set out the position in a convincing fashion. However, the Fund's liquidity position was a complex issue with many different elements to be covered. In EBS/83/170 the staff had clearly put down not only its estimate of the demand for the Fund's resources but also the various elements of supply. He thought that all the elements were covered. On the demand side were many different items, such as reserve tranches, loan claims, stand-by arrangements, extended arrangements, and compensatory financing. Naturally, demand was influenced by the Fund's policies on access to resources and by the fact that members had the right to approach the Fund for amounts that they desired in the light of the pressure on their balance of payments at any moment in time. On the supply side, the situation changed every quarter in response to events beyond the control of the Fund, whether the resources were in currencies or SDRs. With regard to lines of credit, some currencies were usable while others were not because of weakness in members' balance of payments positions. Some, like the GAB, could be called upon if it was possible to convince the participants that there was a shortage of liquidity in the Fund and that the circumstances were right for activation.

The staff had shown the Fund's liquidity on a commitment basis, on a disbursement basis, on a stock basis, and on a flow basis, the Treasurer continued. It had made estimates for one year, two years, and three years ahead. Naturally, as all those matters were included in a single paper, it was bound to be complicated. In that regard, Executive Directors had expressed their praise and support on an earlier occasion for the attempts by the staff to provide a reasonably concise summary. On the present occasion, there were three pages of annex and five of appendix; on another occasion, it might be possible to present a summary and put other material in an appendix. Although his own views on presentation would be rather different, he had been listening closely to the advice of Executive Directors, and the form of EBS/83/170 was the outcome of that advice. While he was open to guidance on the presentation of the Fund's liquidity, the present paper certainly reflected numerous debates by the Executive Board.

The staff could give concrete replies to all Mr. Polak's comments outside the meeting, but he would deal with one forthwith, the Treasurer observed. In Appendix Table 2 on page 25, line 1 was called "Quota Ratio." Mr. Polak felt that the correct term was "debt ratio." He himself believed that the term "quota ratio" was appropriate because footnote 2 defined the quota ratio, in language taken from the decision on the Guidelines for Borrowing, as "the ratio of the total of outstanding borrowing and unused credit lines to total quotas." A "debt ratio" would not include unused credit lines, which were usually considered to be a support to the financial position of an institution, rather than a debt. Credit lines became debts only once they were used. The staff would have preferred to have excluded unused lines of credit, but the Executive Board had included them in the Guidelines for Borrowing. He had dealt with the matter of presentation at some length because he was worried that the staff might be unable to present the Fund's liquidity in a manner that would be convincing to Executive Directors and would enable them to draw their own conclusions.

One point that had been worrying him, the Treasurer continued, was that the Executive Directors had been taking the staff's estimates with undue precision. For instance, changes in the order of SDR 1 billion or SDR 2 billion in an estimate amounting to SDR 10-15 billion could not be considered an admission of an error in the previous estimates. It might even be a disadvantage if the figures were changed too frequently. Fine-tuning estimates with large margins of error would only contribute to potential misunderstandings instead of clarifying the Fund's position.

Regarding the estimates themselves, the Treasurer remarked that, in any circumstances, forecasting events two years ahead was an uncertain exercise. Moreover, the future policy on access to the Fund's resources was as yet unclear. The estimates had therefore been made on the assumptions of the present access policy. Moreover, world economic circumstances were particularly difficult to forecast at the present time. Nevertheless, the Fund was better equipped than most to make some forecast because the outlook for the world economy, using various possible scenarios, was regularly discussed by Executive Directors; and the area departments had great experience in judging the likelihood that members would need to draw on the Fund, although they were less certain when it came to timing. Consequently, the figures that the staff had presented to cover the period until spring 1986 were reasonable figures. While they might rise or fall by several billion SDRs, thus making some difference in the actual financing of the Fund's transactions, they would provide a useful basis for discussing an uncertain future. If the Executive Directors decided to ignore them, they ran the risk of not being prepared for events that were likely to lie ahead.

A speaker had raised the question of the difference between the figures for outstanding loan claims, which had been put at SDR 14.6 billion in EBS/83/133 and SDR 15.5 billion in EBS/83/170, the Treasurer recalled. He himself saw no real difference. All that it showed was that claims on the Fund were tending to rise; a change of SDR 0.9 billion was after all very small. The figures relating to enlarged access under various hypothetical ceilings had been left untouched, first, because the difference would not be significant and, second, because it was important not only for Executive Directors but also for outsiders to have reasonably firm figures with which to work. The figure of SDR 13.8 billion, representing the estimated demand for Fund resources with a ceiling of 102 percent of quota a year, and the figure of SDR 15.9 million representing the demand for Fund resources with a ceiling of 110 percent a year, had remained from the earlier paper. The similarity between the two figures mentioned by Mr. Polak, SDR 15.5 billion in the liquidity paper and SDR 15.9 billion for the 110 percent ceiling in the access paper, was therefore purely coincidental. The underlying assumptions were quite different. The estimates for the liquidity paper had been made on the assumption that no country's absolute access would be reduced. It would not be possible to combine that assumption with one based on specific uniform ceilings on access for all members, as the two series would not be comparable. Although they might not be far from each other, he was unable to judge how far they would be away since there was no way in which the figures could be made strictly comparable.

Regarding the estimate of the demand for compensatory financing, the Treasurer remarked that the staff had originally assumed that the demand for such financing would amount to between SDR 4 billion and SDR 6 billion in the two years FY 1985 and FY 1986. The Research Department had now indicated that the demand was likely to be at the higher end of the range, mainly because it was now thought probable there would be a demand for compensatory financing by countries with larger quotas than had earlier been considered likely.

He had also been asked how the staff had arrived at the figure of SDR 3.5 billion for possible commitments to some smaller non-GAB industrial countries, the Treasurer said. The estimates for developing countries had been arrived at by considering each country in turn against the background of the world economic outlook. However, in estimating the figure of SDR 3.5 billion, the staff had considered the ten smaller industrial countries with a present average quota of about SDR 400 million, which would rise to about SDR 650 million after the new quotas came into effect. Quite a number of the smaller industrial countries had current account deficits. Taken together, their claims on the Fund could well exceed SDR 3.5 billion, and many of them were borrowing heavily in the international capital markets. Whether that borrowing was sustainable remained to be seen. In the circumstances, SDR 3.5 billion for the two years to April 1986 seemed a rather prudent estimate.

A speaker had asked him to reconcile the data in EBS/83/170 with the Chairman's statement that the estimated demand for the Fund's resources with a ceiling of 125 percent of quota would be financeable, the Treasurer recalled. His assumption was that if the ceiling were to be 125 percent of quota, the demand for stand-by and extended arrangements would be in the neighborhood of SDR 20 billion, of which about SDR 13 billion would have to come from borrowing, under the policy on the mix of ordinary and borrowed resources. The question then was how the SDR 20 billion could be financed. Assuming that the Eighth Quota Review came fully into effect, SDR 7 billion would come from ordinary resources, making about SDR 15 billion of usable assets. Of course, if the Eighth Quota Review came into effect without some important members whose currencies were "usable," such as the SDR 5.3 billion for the United States, it would be necessary to review the ceilings, and it was doubtful whether the Fund could finance a demand for SDR 20 billion. Naturally, it was the assumption that all, or most, members would accept their quota increase.

As to the need to borrow SDR 13 billion, he assumed that an enlargement of the General Arrangements to Borrow (GAB) would take place, and that the agreement with Saudi Arabia would come into effect, the Treasurer went on. More specifically, he had assumed that the GAB would be enlarged to SDR 18.5 billion including the associated arrangement, and that all existing debts under the GAB would be paid off in November 1983. It was understood that the whole of the SDR 18.5 billion would not be available at any given moment, as some of the lenders might be in a weak balance of payments position. Nevertheless, it had to be assumed that the world economic situation would remain difficult, and he foresaw demand for the Fund's resources that would lie somewhere between SDR 14 billion with a ceiling of 102 percent of quota a year and SDR 20 billion with a ceiling of 125 percent of quota a year. He also foresaw that some comparatively large countries were likely to make application to the Fund for stand-by or extended arrangements, and one of the requirements for activation of the GAB was that the Fund should have to finance arrangements for members whose disequilibria could well lead to an impairment of the international monetary system.

In those circumstances, the Treasurer remarked, he had assumed that somewhere in the neighborhood of SDR 12 billion, or possibly more, of the SDR 18.5 billion in the enlarged GAB would be usable, with the remainder unusable because participants had balance of payments problems. Leaving some margin for likely calls by the GAB participants in the reserve tranche and perhaps the first credit tranche, it would be reasonable to assume that the GAB would be able to provide SDR 10 billion, leaving a gap of SDR 3 billion to be financed in other ways. It would be rather strange if the Fund could not find an additional SDR 3 billion by April 1986 if the world payments system continued to be under the pressures that had been assumed. Consequently, he assumed that the Fund could finance the likely demand with ceilings of 125 percent in one year or 375 percent in three years. Naturally, one important assumption was that the SDR 6 billion in loans that the Managing Director was seeking at the moment would be available before the Eighth General Review of Quotas went into effect. In brief, with the Eighth Quota Increase, the enlargement of the GAB and its use on a significant scale, and SDR 6 billion of new borrowing before the Eighth General Review went into effect, the residual borrowing should be manageable.

Regarding the position on the commitment gap, the Treasurer reminded Executive Directors that the rule by which the Fund lived was that the Fund should cover all its commitments in advance, whether through ordinary or through borrowed resources. The rule was a prudent one because the alternative was to allow a commitment gap to arise and then assume that it was possible to borrow at any time and at any price, to close that gap. Such a procedure was not in accordance with the present rules of the Fund, and a change in that direction would be a fundamental matter requiring a complete reconsideration of the present authority to borrow. The Fund would have to be sure that it could borrow at any time without restriction to cover any commitment that might arise. Consequently, it would not be easy to reach the conclusion that a commitment gap did not matter simply because it could be covered. The Fund's working rule was that while commitment gaps could be permitted to arise, they should be both temporary and small. On a previous occasion when a commitment gap had arisen, the Executive Board had agreed that it was small, and that it could be considered temporary because it was known that the second part of the SDR 8 billion credit line from the Saudi Arabian Monetary Agency (SAMA) would become usable.

None of those circumstances prevailed at the present time, the Treasurer went on. A commitment gap had appeared in March 1983; since then, the Fund had committed itself to at least one large debtor country; the commitment gap had been increasing, and there was no certain prospect that the Fund could cover that gap by borrowing. The gap would reach SDR 4 billion shortly and was likely to reach SDR 6 billion in the not too distant future. The present gap was therefore neither small nor short term.

Furthermore, the fact that the Fund had a working rule for the management of its liquidity was well known in financial circles, the Treasurer commented. If the Fund did not observe its own rule on the management of its liquidity, there was a risk that its public image would be damaged. Indeed, the question had been asked in the banking departments of central banks that had invested their reserves in the Fund by acquiring large reserve tranche positions whether the Fund was in fact observing its own rule of liquidity management. If the managers of such operations began to question whether the Fund was observing its own rules, they were likely to begin to question whether a reserve position in the Fund was as liquid as they had assumed.

The next question to be considered, the Treasurer continued, was how large the commitment gap could become. Most members of the Executive Board felt that the Fund's cash resources were falling rapidly, while its liabilities were rising. He himself had not seen the liquidity of the Fund under such strain. By the end of 1983, the Fund's cash position would be equal to roughly one third of its liabilities, and that might well be the point at which those who held reserve tranche positions would ask themselves whether they were safe positions to hold. Naturally, the circumstances were perhaps as relevant as the absolute figures, and the circumstances were not favorable. There might, for instance, be some additional demands on the Fund, as had been recognized by the membership when it had tried to accelerate the quota review procedure earlier in the year and to expand the General Arrangements to Borrow. Neither of those two changes was yet in effect. Moreover, the extent of the uncertainty in the world economy was so great that the same amount of liquidity did not go as far in 1983 as it had in 1981. It would be unfortunate to base a judgment on the Fund's liquidity exclusively on the comparison of demands on the Fund with its cash position. It was of course up to the Executive Board to give guidance on what it considered to be the appropriate policy.

Taking up a technical point by Mr. Wicks, the Treasurer recalled that the staff had said that it would be necessary to have at least SDR 8-10 billion in ordinary resources in the spring of 1986, and he had inquired what the comparable figure would be for the spring of 1984. The figure would be very different. By the spring of 1986, it was hoped that the world would be in a period of economic recovery and that the strains on the system would be diminished. Second, by that time, he hoped that the Fund would be receiving considerable inflows through the repurchases of drawings that had to be made in the past 18 months or so. Neither of those elements were likely to be present by the spring of 1984. Consequently, in his view, the figure would have to be substantially higher if it were to be comparable with that for the spring of 1986.

The Chairman made the following summing up:

The discussion has highlighted the following points:

(1) The Board has agreed on the liquidity projections for 1983 as contained in the staff paper.

(2) In the light of these projections, Executive Directors noted that the liquidity position of the Fund is coming under increasing strain. Indeed, the commitment gap has already reached SDR 3.5 billion, and, if no further borrowing is arranged in the meanwhile, it will grow to SDR 6 billion at the end of 1983.

(3) There was some discussion on the problems raised by the size of the commitment gap. While considering that the liquidity position and the policies of the Fund should not be solely and continuously geared to a zero commitment gap, the Board agreed

that a commitment gap, if any, should be kept within reasonable limits. The present rate of increase of the commitment gap was regarded by many as unsustainable.

(4) Therefore, Executive Directors stressed the importance of completing the borrowing negotiations under way. The intention of the Saudi Arabian authorities to lend to the Fund, provided that the industrial countries or the BIS group do the same, was highly commended. The hope was expressed that the matter would be concluded shortly, and management was encouraged to continue its discussions.

(5) Looking beyond these short-term problems, the Board stressed the need to have the Eighth Quota Review completed as planned before the end of November 1983.

(6) It was recognized that, while quotas should remain the main resource of the Fund, the continuation of the enlarged access policy would entail recourse to borrowing after 1984. The amount of that borrowing would of course depend very much on the access limits decided on. Positions on access limits, the forms of borrowing by the Fund, and possibly the acceleration of the Ninth Quota Review, did not change in the course of this meeting.

(7) The Executive Board agreed that the liquidity of the Fund and the quality of the claims against the Fund should remain beyond any possibility of doubt.

I shall add some brief personal remarks.

First of all, I wish to stress that the liquidity position of the Fund is more serious than seemed to be implied by some of the speakers today, and I shall give a few simple figures to show why I think so.

If we were to wait until April 1984 without borrowing at all or arranging new lines of credit and assuming that the Eighth Quota Review is still not completed--and this is not an implausible assumption--the Fund's undisbursed ordinary cash resources would be of the order of SDR 8.2 billion, and the amounts available under borrowing lines of credit would be SDR 0.9 billion. Now, against this amount of SDR 9.1 billion in usable resources, we would have about SDR 12 billion in undrawn commitments already decided upon and some SDR 28 billion in reserve tranche positions, which are considered liquid claims upon the Fund. A significant proportion of those SDR 28 billion reserve tranche positions might be encashed because a number of countries who hold these reserve tranche positions are in a vulnerable balance of payments situation. So, compared with SDR 9 billion in cash, we would have already committed SDR 12 billion, and we would be absolutely unable to honor both the encashment of liquid claims and the undrawn commitments. Such a position would not be consistent with the prudent management of any type of institution, let alone the International Monetary Fund. This is why I cannot accept the idea that I should take a relaxed view of the borrowing exercise in which I am rather intensively engaged. April 1984 is just over six months away, and six months will pass quickly. We are in fact barely six months away from what I would call a dramatic situation.

The commitment gap is worrying indeed; it must be closed urgently. Failing to do so would weaken not only our liquidity position, but our image--the image of an institution that is supposed to be the anchor of the system and thus the example of good management--in an uncertain and difficult international environment.

I tell you clearly that, as Managing Director of this institution, I could not envisage letting this figure become any larger. The talks that are to take place in Basle in the coming weeks are certainly of critical importance; and I hope--as I have some reason to do--that they will be successful.

If things prove to be more difficult or take longer than I expect, I shall of course bring the matter to the Executive Board, which will then have to accept its responsibilities. I would of course describe all the options available, including a cutting back of any new commitments.

Mr. Erb commented that he had listened closely to the Treasurer's observations on the possible future uses of the General Arrangements to Borrow. From the standpoint of his own authorities, there were circumstances in which the conditions for the use of the GAB, both participants and nonparticipants, might well exist; that was a decision that should be taken at the time. It would be unwise for the Executive Directors, in considering a period a year or two in advance, to take the line that because at present the world's circumstances were consistent with the activation of the GAB, they might still be so in 1984 or 1985, and that therefore the use of the GAB could reasonably enter into future expectations. It might well be that the circumstances were such that the GAB could not be activated. The Treasurer had said that the GAB could not be used in all circumstances; he himself would say that it could only be used in very limited circumstances. The Treasurer had assumed that the GAB could be used in a difficult international payments situation. He would express the matter more strongly when it came to activating the GAB for use either by participants or by nonparticipants. The GAB should always be kept as a memorandum item, as something that could only be drawn upon in certain circumstances. He would therefore suggest a change in Table 1 of the selected balance sheet data. At present, on page 24 of EBS/83/170 the GAB was shown under heading 3(b) as "unused credit lines." He would prefer to place it in a separate category entitled "conditional credit lines," so that there would be no misunderstanding that special conditions were attached to its use.

The Chairman remarked that Mr. Erb's suggestion seemed to be in line with the conditions governing the use of the General Arrangements to Borrow.

The Treasurer said that he had assumed that Executive Directors were aware of the legal conditions under which the GAB could be activated. One of them was that the Executive Board should, by a majority, agree with the Managing Director that the GAB should be activated in circumstances prevailing at the time. When he had remarked that some large commitments were in prospect, he had meant that they were in prospect for the reasonably near future, not for later years. Mr. Erb was certainly right in saying that it was impossible to predict that the world economy would be in the sort of situation in which the GAB was intended to be activated in 1986. If it was not, then the amounts to be financed, and the demand on the Fund's resources, would be less. In general, the Fund's commitment would seem financeable for 1986, provided that the GAB could be activated if necessary. He would certainly be prepared to consider placing the GAB on a separate line in Table 1 of page 24. He would also consider whether it should come under the subheading "conditional credit lines."

Mr. Nimatallah stated that he would be happy if the Chairman would omit mention of the amount that his authorities might be prepared to lend from his summing up.

Mr. Polak observed that Mr. Erb's remark about the activation of the GAB required careful consideration. It was true that the conditions under which the GAB could be activated were rather special, both in its present and in its enlarged form. Nevertheless, the Netherlands authorities could not conceive of a situation in which the Fund found itself short of resources and yet the GAB could not be activated. The demand and supply conditions for the GAB were closely related. While he had no strong view regarding the presentation in Table 1, care should be taken to avoid any presentation that might create the impression that, however weak the liquidity of the Fund might become, there might be circumstances in which it would still be impossible to activate the GAB. Such a situation would be most harmful, and he felt confident that in one way or another the participants would activate the GAB in those circumstances.

Mr. Malhotra recalled that, when the matter had been discussed in the Interim Committee, the clear impression had been left that the resources of the GAB would be available to the Fund. Naturally, there would have to be consultation and agreement between the participants and the Managing Director, and the preconditions of activation would have to be met.

Nevertheless, it would be rather strange to assume that there would be large and continuing demands on the Fund's resources due to a balance of payments strain on the system as a whole, and then to find, when an impairment of the international system actually came about, that the General Arrangements to Borrow could not be activated, Mr. Malhotra observed. Such a procedure would be inconsistent, and it would be unfortunate to give the impression in the outside world that the Fund had spent a great deal of time putting together an arrangement to cover circumstances that might not arise in the next three years.

Mr. de Maulde commented that Mr. Erb was no doubt legally quite correct. Executive Directors would remember that at the time of the discussion on the enlargement of the GAB, his authorities had favored criteria for activation that were considerably broader than the ones finally agreed to. While he would not like to see the resources of the GAB categorized as "conditional," he would have no objection to showing them on a separate line in Table 1, especially as the paper was internal to the Fund. However, when it came to the activation of the GAB in practice, he agreed entirely with Mr. Polak. Like him, he could not conceive of a situation in which the Fund would be short of resources and the conditions would still not be appropriate for the activation of the GAB.

Mr. Joyce said that, as he understood it, a large part of the figure for reserve positions in the Fund would reflect the reserve tranche positions of the Group of Ten, which would be covered under the existing GAB, quite apart from the extended GAB.

The Treasurer replied that Mr. Joyce was perfectly correct. The reserve tranche positions of the GAB participants as a group were much larger than the present GAB. As to whether those positions could be covered by the enlarged GAB, it could not be assumed that all GAB participants would simultaneously be in a position when they would need to draw on their reserve tranche positions. On the other hand, there had been circumstances when many GAB participants had been close to such a position, and surpluses in the world monetary system had been accumulated outside the GAB countries. Now that the GAB was being extended, the risk that assets would flow outside the group of participants or associated countries had diminished.

Mr. Erb remarked that one of the conditions for the activation of the GAB was that possible uses by participants must be taken into account.

The Executive Directors concluded their discussion of the Fund's liquidity position and financing needs.

APPROVED: March 2, 1984

LEO VAN HOUTVEN
Secretary