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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 83/181

10:00 a.m., December 23, 1983

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

Executive Directors	Alternate Executive Directors
	W. B. Tshishimbi
	L. K. Doe, Temporary
	G. Ercel, Temporary
B. de Maulde	X. Blandin
A. Donoso	
R. D. Erb	
M. Finaish	T. Alhaimus
T. Hirao	T. Yamashita
J. E. Ismael	
	G. W. K. Pickering, Temporary
A. Kafka	C. Robalino
	G. Grosche
G. Lovato	C. P. Caranicas
R. N. Malhotra	A. S. Jayawardena
Y. A. Nimatallah	J. E. Suraisry
J. J. Polak	T. de Vries
A. R. G. Prowse	
G. Salehkhou	O. Kabbaj
	E. I. M. Mtei
	S. E. Conrado, Temporary
	A. Lindå
N. Wicks	T. A. Clark
	Wang E.

A. Wright, Acting Secretary
R. S. Laurent, Assistant

Also Present

African Department: O. B. Makalou, Deputy Director. Asian Department: K. A. Al-Eyd, R. H. Nord. European Department: M. Z. Khan, V. Marie. Exchange and Trade Relations Department: D. K. Palmer, Associate Director. External Relations Department: H. O. Hartmann. Legal Department: J. G. Evans, Jr., Deputy General Counsel; G. F. Rae, Deputy General Counsel; W. E. Holder, Ph. Lachman. Middle Eastern Department: F. Drees, S. Thayanithy. Research Department: R. R. Rhomberg, Deputy Director. Treasurer's Department: W. O. Habermeier, Counsellor and Treasurer; D. Williams, Deputy Treasurer; M. N. Bhuiyan, D. H. Brown, S. I. Fawzi, R. B. Hicks, B. E. Keuppens, T. Leddy, M. A. Tareen, T. M. Tran, G. Wittich. Personal Assistant to the Managing Director: S. P. Collins. Advisors to Executive Directors: A. A. Agah, E. A. Ajayi, S. El-Khouri, K. A. Hansen, S. M. Hassan, W. Moerke, Y. Okubo, I. R. Panday. Assistants to Executive Directors: E. M. Ainley, H. Alaoui-Abdallaoui, J. Bulloch, M. Camara, M. B. Chatah, L. E. J. M. Coene, C. Flamant, I. Fridriksson, G. Gomel, V. Govindarajan, D. Hammann, N. U. Haque, A. K. Juusela, H. Kobayashi, M. J. Kooymans, M. Rasyid, A. A. Scholten, S. Sornyanyontr, Wang C.-Y., J. C. Williams, A. Yasseri.

1. GUIDELINES FOR BORROWING BY FUND - REVIEW

The Executive Directors considered a paper reviewing the guidelines for borrowing by the Fund (EBS/83/187, 8/26/83).

The Chairman made the following statement:

When the paper reviewing the guidelines for borrowing by the Fund (EBS/83/187) was issued in late August 1983, no decision had been taken on the future of the enlarged access policy and on the scale of members' access to Fund resources. The limits of members' access to the Fund's resources under the enlarged access policy have been agreed for 1984, and the staff has reviewed those sections of EBS/83/187 that made some use of projections of the Fund's future needs to borrow. This applies in particular to Section II, paragraph 3, "Future Borrowing Needs" (EBS/83/187, p. 9).

It may be recalled that the starting point for the discussion of future borrowing needs in EBS/83/187 was the projected total of borrowing plus unused lines of credit at the end of 1983. The projection used is very close to what is now expected to be the position. As regards future borrowing needs, it was assumed that additional borrowing through April 1986 would be in the range of SDR 8.3 billion to SDR 13.1 billion, based on access of 102/307 percent to 125/375 percent, respectively, of members' quotas. Given the decision to review the limits under the enlarged access policy annually, a projection of any range of likely borrowing needs through April 1986 becomes highly uncertain. Borrowing needs for 1984 are presently estimated to fall between SDR 2.5 billion and SDR 4 billion, but this estimate does not provide for any use of the Fund's resources by a participant in the General Arrangements to Borrow (GAB). Furthermore, in the absence of agreed limits on access in 1985 and beyond, it is difficult to provide an estimate for use of Fund resources after 1984. It may, however, be reasonable to assume that the range for the period through April 1986 would be lower than the SDR 8.3 billion to 13.1 billion indicated in EBS/83/187.

In EBS/83/187, the conclusion was drawn that the total of borrowing for the guidelines should be limited to 60 percent, that is, the present upper limit. It was also tentatively suggested that it would be "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." In the light of developments since the issuance of EBS/83/187, there now seems no reason for suggesting consideration of a possible increase. On the other hand, given the considerable uncertainties involved and the strong need for the Fund to have adequate room for maneuver to deal with strains in the system, there remain good reasons for maintaining the present limits.

Mr. Nimatallah made the following statement:

I would like to emphasize that Saudi Arabia remains firmly committed to a strong Fund, playing a central role in the international adjustment process. The borrowing guidelines, adopted by the Executive Board in January 1982, provide a sound basis on which the Fund can respond effectively to the financing needs of its members. They also show that the Fund is prudent in managing its resources and in its borrowing policies, thereby providing lenders with essential assurance. Saudi Arabia, therefore, attaches considerable importance to these guidelines.

The present review of the guidelines is both necessary and appropriate, now that the Eighth Quota Review has been completed. Although our experience is limited, the guidelines appear to be serving their purpose. They have given the Fund ample scope to meet its borrowing requirements. The Fund's outstanding borrowing and unused credit lines at end-1983 will amount to just over SDR 20 billion or 33 percent of old quotas, well within the 50-60 percent ceiling. Equally important, the guidelines have given lenders confidence in the Fund and in its borrowing policies.

The guidelines, therefore, strike the right balance between prudence, on the one hand, and flexibility, on the other. This balance should not be disturbed, especially after a quota increase that will anyway raise the Fund's capacity to borrow. By early 1984, after the new quotas are paid in and the SDR 6 billion loan is concluded, outstanding borrowing and unused credit lines 1/ will total SDR 35 billion, or 39 percent of new quotas. This is considerably below even the lower 50 percent ceiling. I fully endorse the statement made on page 3 of the staff paper (EBS/83/187):

> 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.

I cannot, therefore, understand why the staff proposes to replace the existing 50-60 percent range with a single borrowing ceiling of either 60 percent or two thirds of new quotas. The staff argues that the lower 50 percent ceiling is now superfluous.

1/ The calculation assumes that the staff proposal, to include two thirds of the enlarged GAB and associated arrangements in the total of outstanding borrowing and unused credit lines, will be accepted by the Executive Board.

It argues that the ceiling should be raised because the Fund's borrowing needs could be substantial in the period to April 1986, and beyond.

I find these arguments unconvincing and unrealistic. A decision to raise the ceiling now, after only two years' experience, and after a sizable quota increase, would weaken the confidence of lenders in the Fund's borrowing policies. This is particularly true, considering the potential amounts involved. If the borrowing ceiling were set at 60 percent or two thirds of new quotas, the Fund would then be in a position to borrow up to a total of SDR 54 billion to 60 billion. This means the Fund could borrow a further SDR 19 billion to 25 billion, in addition to its outstanding loans and unused credit lines, 1/ over the period until the Ninth Quota Review. The idea that the Fund would borrow anything like these amounts would be disquieting for existing or potential lenders.

I do expect the Fund to continue to play an important role in the period ahead, and I recognize that the Fund will, almost certainly, have to borrow further in order to play that role effectively. But it is very difficult to imagine that the Fund will need new borrowing on the scale contemplated by the staff. I am aware that the projections are very tentative, but judging by experience, they may be revised downward, particularly if the world economic recovery is sustained. It is also very difficult to reconcile potential borrowing on this scale with the universally accepted principle that borrowing by the Fund is temporary. The guidelines themselves state that quotas are, and should remain, the basic source of Fund financing.

Furthermore, even if the Fund's borrowing needs are that substantial, it is less than realistic to expect that the Fund would be able, in practice, to borrow all the amounts that its membership would need. Even if the Fund were to approach the private markets, the most that the Fund could borrow from this source might be in the order of, say, SDR 10 billion over the next three or four years. This is well below the amounts projected by the staff.

For these reasons, I cannot support the staff proposals to abolish the present 50-60 percent range and to raise the borrowing ceiling. I could even go further. The Eighth Quota Review will increase the Fund's ordinary resources considerably, as I have shown in a previous statement (Buff 81/164, 9/4/81) on this subject, the need for borrowing moves in an inverse relationship to the change in quotas. I could, therefore, suggest to leave

1/ The calculation includes the SDR 6 billion loan, and two thirds of the enlarged GAB and associated borrowing arrangements, in the total of unused credit lines.

the borrowing ceiling at only a single limit of 50 percent of new quotas. This would allow the Fund to borrow up to a total of SDR 45 billion. This should be more than adequate for the Fund's potential needs.

I am, however, prepared to go along with retaining the present 50-60 percent range to give the Fund a margin of flexibility. I can do so on the understanding that the lower 50 percent figure is the operative ceiling. If the Fund's borrowing and unused credit lines were to approach that level, it would be necessary for the Board to review the Fund's liquidity position and its borrowing policies before the 50 percent trigger point was reached.

I agree with the staff that the enlargement and revision of the GAB provides a reason to amend the proportion of the GAB to be included in the total of outstanding loans and unused credit lines. The Fund should be in a position, if necessary, to borrow under the enlarged GAB, and associated arrangements, for a substantial proportion of the total. At the same time, the allowance made for possible borrowing under the GAB should not be unrealistically high. The staff's proposal to include two thirds of the enlarged GAB, and associated arrangements, in the total of outstanding borowing and unused credit lines is a sensible compromise, which I support.

Finally, I am willing to review the guidelines after a reasonable period. It might, for example, be useful to review them in, say, two years' time, when we will have the benefit of further experience.

Management should continue to be cautious, prudent, and realistic. My authorities believe that the Fund has a central role to play in the international adjustment process, but they also realize that there are limits to the Fund's capacity to borrow.

On the basis of the above, I cannot support the draft decision in Appendix 2 of the staff paper. I would, however, like to recommend the following decision to my colleagues:

> Executive Directors have reviewed the guidelines for borrowing by the Fund in accordance with paragraph 4 of Decision No. 7040-(82/7).
>
> Executive Directors have agreed that the principles in the preamble to that decision, and the provisions of paragraphs 1, 2, and 5 of that decision shall continue to apply, but that paragraphs 3 and 4 of that decision shall be revised as follows:

3. The total of outstanding borrowing plus unused credit lines under paragraph 2 of Decision No. 7040-(82/7) shall include, in respect of the GAB and borrowing arrangements associated with the GAB, either outstanding borrowing by the Fund under these arrangements, or two thirds of the total of credit lines under 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 gidelines shall be reviewed no later than December 31, 1985, and may be adjusted as a result of that review.

Mr. de Maulde commented that the limit on borrowing expressed as a range of 50-60 percent of total quotas was acceptable, and he would prefer to make no change in it. He would agree with Mr. Nimatallah that the 50 percent figure should be considered important and that the 60 percent figure should be considered quite theoretical.

He had no problems with the proposal to increase the proportion of the GAB included in the total of borrowing plus unused credit lines from one half to two thirds, Mr. de Maulde continued. Nor did he have any problem with modifying the language to deal with the new GAB. Finally, his authorities were convinced that the borrowing needs of the Fund in the future could easily be covered by the GAB and other agreements.

Mr. Hirao noted that guidelines for borrowing constituted one of the fundamentals of the IMF. He agreed with the staff that unless there were clear reasons for making substantive changes, the Fund should maintain the principal features of the guidelines and keep changes to a minimum. The present quarterly limits should be kept unchanged. Owing to recent revisions in the GAB, substantially higher proportions of the total available under the GAB should be included in the Fund's borrowing limits. In conclusion, he could support the proposal for the Executive Board to review the guidelines when the Ninth General Review of Quotas was completed or when changes were made in the GAB or associated arrangements.

Mr. Grosche observed that, generally speaking, in order to retain the confidence of creditors, the Fund ought not to make changes in existing guidelines for borrowing unless there were strong reasons for doing so. While improvements in the criteria were welcome, they should not lead to increases in the ceiling for borrowing. Thus, he agreed on keeping the present limit on borrowing at 50-60 percent of total quotas, expressed as a range. Should the range be abolished, he could not accept a single figure higher than 50 percent.

On the treatment of the GAB, he agreed with the Chairman's suggestion to supplement paragraph 3 of the decision on guidelines for borrowing with a reference to associated borrowing arrangements, Mr. Grosche continued.

He could also go along with the proposal that two thirds of the total of the GAB plus associated borrowing arrangements should be included in the ceiling on Fund borrowing. However, he had some reservations about including in the preamble to the proposed decision any reference that stressed the particular importance of the GAB as a potential source of borrowing. By putting so much emphasis on borrowing, the Board might create the impression that the Fund could be willing to accept some weakening in the importance of quota subscriptions as the main source of its financing.

He did not favor including in paragraph 4 any reference that would make the Board's review of the guidelines on borrowing subject to a change in the GAB or associated arrangements, Mr. Grosche concluded. It was within the Board's discretion to review the guidelines at any time.

Mr. Lindø said that he fully agreed with the staff that the Fund should avoid making any major changes in the borrowing guidelines at present. In fact, for the reasons cited by the staff, his authorities believed that it was important to alter the guidelines as seldom as possible.

Second, expressing the limit on borrowing as a range served a limited purpose, Mr. Lindø went on, and he was satisfied that the Board's regular reviews of the liquidity position of the Fund provided ample opportunities to monitor its borrowing activities. Supplementary reviews could be undertaken whenever the Board deemed it necessary. Consequently, he favored a single percentage limit related to quotas, and he wished to maintain the effective limit at 60 percent.

Third, Mr. Lindø noted, given the broadened applicability of the GAB, his authorities agreed with the staff that the proportion of the GAB to be included in total Fund borrowing, plus unused credit lines, should be raised from the present 50 percent to two thirds of the total of the GAB plus associated borrowing arrangements. In sum, he could support the proposed decision, with a borrowing limit of 60 percent in paragraph 2.

Mr. Ismael stated that while he was committed to a strong Fund, he was concerned that it was not possible to estimate with some degree of confidence the likely demand on the Fund's resources in the years ahead, or at least through April 1986. Given the uncertainty surrounding the outcome of the annual reviews of Fund policies and special facilities, the demand for Fund resources might well remain at the present level, especially in view of doubts about the durability of the present recovery and the various impediments to trade throughout the world.

He would appreciate learning more about the assumptions regarding access limits in coming years that the staff had used in arriving at the figure of SDR 8.3 billion-13.1 billion through April 1986, Mr. Ismael continued. As the Fund should preserve flexibility and room for maneuver in dealing with members' adjustment programs, and with other forms of assistance, he had sympathy with the proposal to increase the borrowing

ceiling to 60 percent of total quotas. However, he was prepared to go along with retaining the present range of 50-60 percent. He could also support the staff's proposal to include two thirds of the enlarged GAB and associated arrangements in the total of outstanding borrowing and unused credit lines.

Mr. Doe questioned whether it was necessary to make an explicit reference in the preamble to the GAB-related arrangements. In his view, the importance of the resources that could be mobilized under those arrangements was sufficiently stressed in the second sentence of the preamble, which read: "However, borrowing by the Fund provides an important temporary supplement to its resources."

He had some difficulty with the proposed amendment to paragraph 2, which seemed to introduce excessive rigidity into the financial operations of the Fund, Mr. Doe went on. After all, the borrowing needs of members--the major ingredient in determining the Fund's financial requirements--were quite difficult to forecast with any degree of accuracy. Together with the uncertainty associated with the concept of unused credit lines, the difficulties in forecasting members' needs were likely to make reliance on a single ratio as a limit to Fund borrowing altogether too unstable. Furthermore, if estimates of the timing of borrowing and resource availability proved faulty, the Board might find it even more difficult to determine policy according to a single guideline. In addition, the prudent management of Fund resources required adequate monitoring in order to detect potential difficulties far ahead of time. Thus, he would prefer to maintain the original text of paragraph 2, although he would be willing to consider raising the range.

He had no major difficulty in accepting the proposed amendment in paragraph 3, reflecting changes in the conditions of access to Fund resources that could arise from activation of the GAB and related arrangements, Mr. Doe said. His only hesitation concerned the proposal to include two thirds of GAB resources in the outstanding amount of borrowing and unused credit lines. He would be inclined toward a figure somewhere between 50 percent and the two thirds proposed; perhaps 60 percent would be suitable.

As to paragraph 4, he would appreciate some clarification about the nature and magnitude of the changes in the GAB and related arrangements, Mr. Doe concluded. For instance, would a review be undertaken simply as a result of modifications in the amount of the GAB and related resources or in the terms of financing and maturity? If so, would a review be undertaken irrespective of the magnitude of such changes? Finally, he would prefer the original formulation of paragraph 5.

Mr. Lovato commented that the proposals submitted by the staff were well argued but left him unconvinced. Before going into specifics, he wished to reiterate that quotas should remain the primary source of financing for the Fund; borrowing should play a supplementary role and be only

temporary. He did not share the view expressed on page 13 of EBS/83/187 that the Fund's decision on the GAB placed greater emphasis on potential borrowing relative to quotas than had existed when the present guidelines had been adopted. He did agree with the staff that, unless there were a clear reason for making substantive changes, the confidence of creditors in the prudence of Fund policies on borrowing was likely to be strengthened if the Fund kept the principal features of the guidelines unchanged.

The first proposal to replace the present range with a single limit did not seem to change the current state of affairs from either a practical or an operational standpoint, Mr. Lovato remarked, especially if the assessment by the Executive Board was to be replaced by a similar assessment based on an understanding between the Managing Director and the Board. Unlike the staff, however, he believed that the Board's assessment of the technical factors, if and when actual borrowing reached 50 percent of quotas, was an important action and far from superfluous. As he, like the staff, saw virtue in keeping the guidelines unchanged, he would like to keep the present text. He also had a preference for Board discussion and assessment before actual borrowing reached the limit of 50 percent of quotas.

Although the recent changes in the size and applicability of the GAB were matters of fact, he doubted whether they required different treatment under the guidelines, Mr. Lovato continued. The staff itself stated that selecting a proportion of the GAB higher than the present 50 percent in the total figure for resources including credit lines might undercut the Fund's ability to borrow from other sources. Besides, as the staff suggested, a situation might arise in which not all lenders would participate or in which, even if all lenders were to participate, they would not provide the full amount of the credit line assigned to them.

Finally, both the updated projections presented by the staff and the Managing Director indicated that the borrowing needs of the Fund would be lower than previously foreseen, Mr. Lovato observed. Therefore, he would not support an increase in the present limit on borrowing.

Mr. Conrado said that he could go along with the staff proposal to replace the existing range with a single ceiling of 60 percent of new quotas. However, if a majority in the Executive Board felt that it was inappropriate to adjust the current range, he would not object to keeping it unchanged on the understanding that 60 percent would be the upper limit and that the Executive Board would undertake an assessment when the ratio reached 50 percent of quotas. Although there might be no reason to consider a figure greater than 60 percent, it was reasonable to maintain the present limits in the face of the uncertainties still plaguing the international economic environment.

In present circumstances, borrowing by the Fund did not violate the basic principle that quotas should remain the main source of Fund resources or that Fund financing ought to be temporary, Mr. Conrado remarked. Fund financing could be considered temporary as long as it was linked to the

successful implementation of adjustment. However, the severity and duration of the present adjustment were not comparable to periods of adjustment in the past. The longer the period of adjustment lasted and the more numerous the uncertainties surrounding it became, the greater the need for flexibility in international monetary arrangements would be. The Fund should have sufficient flexibility to deal with any further strains on the international monetary system, should the strength or timing of the forces of economic recovery fail to produce the expected results. Borrowing might provide the Fund with the necessary room for maneuver in coping with unforeseen difficulties.

As to the proposal that the GAB should be included in the ceiling for Fund borrowing and lines of credit, he agreed that the Fund should be able to borrow appropriately under the enlarged GAB and associated arrangements, Mr. Conrado concluded. He therefore supported the proposal to include two thirds of the total of the GAB plus associated borrowing arrangements in the total of Fund borrowing plus new credit lines.

Mr. Wicks commented that he regarded the guidelines for Fund borrowing simply as a technique for giving assurance to creditors. He did not regard the guidelines as part of the general process of financial planning in which the Executive Board engaged during its regular reviews of the Fund's liquidity, at which time the Board considered the Fund's general borrowing position. Whatever the outcome of the present discussion, Directors should not consider that a certain amount of resources would definitely be forthcoming from lenders, because the Board would still have to decide how the Fund's future borrowing requirements were to be financed. He would also like to support the point made by several Directors that, in line with maintaining the central role of quotas in financing the Fund's activities, he hoped to see a lowering of the borrowing limit as a long-term objective, as the international financial situation improved.

As to the ceiling on, or range of, outstanding borrowing as a proportion of total Fund quotas, Mr. Wicks continued, he could accept an increase to 60 percent if other Executive Directors were content with that figure. However, if it caused difficulty, he could go along with retaining the present guideline. As to how much of the GAB should be included, it would be well to continue the present practice of including half of the total GAB in the definition of borrowing and unused credit lines. Again, if other Executive Directors--particularly those from countries that were substantial lenders to the Fund--thought that it would be helpful, he would not oppose the inclusion of two thirds of GAB lines of credit in the Fund's borrowing limit. Finally, it would be better to undertake the next review of the guidelines in two years' time instead of waiting for the completion of the Ninth General Review of Quotas.

Mr. Wang expressed support for the proposed amendments to the decision. Although he would prefer the limit on borrowing to be set at 60 percent of total Fund quotas, he could go along with the majority of the Board.

Mr. Mtei said that, while there was a need for the Fund to borrow to supplement its resources in the short run, the principal source of financing for the Fund should continue to be the quota subscriptions of member countries. If the resources of the Fund proved inadequate to meet the financing needs of members, the Fund could not rely solely on borrowing; rather, it would have to consider speeding up the Ninth General Review of Quotas.

The present guidelines had been established to enhance creditors' confidence in the way in which the Fund was financed and in its ability to service its debts, Mr. Mtei continued. Although formal guidelines might be of some significance, confidence would depend on the willingness of members to support the Fund in its efforts to assist countries undertaking adjustment policies while maintaining prudent debt management.

Although in principle he had no objection to simplifying the guidelines, he did not find the staff's arguments in favor of adopting a single ceiling of 60 percent to be convincing, Mr. Mtei remarked. There continued to be uncertainties regarding unused credit lines, so that there was still a need for a lower limit to serve as a trigger point. Moreover, the staff had not demonstrated that setting the ceiling in the form of a range had led to complications in practice. He would thus prefer a ceiling expressed as a range rather than as a single limit.

Given the inadequacy of the quota increase under the Eighth General Review--a point that his chair had repeatedly stressed during recent months--and given the unpredictable nature of developments in the international financial system, Mr. Mtei observed, the Fund had to have room for maneuver to meet the general needs of its members and to play its role in adjustment. However, the Fund's access to borrowing should not be so easy as to delay consideration of future increases in quotas, a delay that would jeopardize the cooperative nature of the Fund. The growing need for resources should be met by an adequate increase in quotas.

He had no problem with the proposed adjustment in the treatment of the GAB under the guidelines, Mr. Mtei remarked. As the staff had shown, the adjustment was justified by the substantial enlargement of the GAB and its broadened applicability. He favored the inclusion of two thirds of the enlarged GAB and associated arrangements in the total of outstanding loans and unused credit lines. In conclusion, he hoped that the conditions for activating the GAB would be made more flexible to enhance the Fund's ability to respond to the needs of its entire membership.

Mr. Polak considered that assuring the financial strength of the Fund depended upon the prudence of management and the Executive Board in setting and administering the policy on access to Fund resources. He was not convinced that a borrowing ceiling, especially one so high as had been proposed, would contribute greatly to the impression of stability that could be created by the policy of prudence to which he had referred. Indeed, a borrowing ceiling could even detract from the impression of stability. Nevertheless, since some Executive Directors were strongly attached to

having those guidelines, he was prepared to maintain the present arrangements, although he would have preferred a single ratio of 50 percent of quotas. He concurred with the proposed treatment of the GAB.

Mr. Erb stated that the current preamble should be retained. Guideline 2 should also be retained, including a range of 50-60 percent of total quotas for the total of outstanding borrowing plus unused credit lines. He could go along with a decision to include two thirds of the GAB and associated borrowing arrangements. Finally, he agreed with Mr. Nimatallah that the Board should review the guidelines in December 1985.

Mr. Prowse said that the present limits should be retained, as Mr. Nimatallah had suggested. In general, he agreed with Mr. Nimatallah and could support retention of the 50-60 percent range, although he would not have been surprised if management had made a case for a 50 percent limit in view of the increase in quotas. He could also accept the proposal that the total of outstanding borrowing plus unused credit lines should include two thirds of the total of credit lines under the GAB, and he could support the idea for a review of the guidelines in two years' time.

He had two substantial comments, Mr. Prowse went on. First, he had found the staff's remarks about the relative importance of borrowing, as presented on page 11, to be somewhat surprising and not in accordance with the current policy. Second, once the trigger had been activated, the Executive Board was supposed to consider the technical factors that would determine the availability of unused lines of credit. The proposed action was fairly limited. On the other hand, Mr. Nimatallah had said that if the Fund's borrowing plus unused credit lines were to approach the 50 percent level that he regarded as the operative ceiling, the Board should review the Fund's liquidity position and its borrowing policies. Did Mr. Nimatallah adhere to that position, or was he willing to accept the limited review under the present guidelines? He himself believed that the review prescribed by the guidelines was more limited than he would wish to see conducted under those circumstances; he would favor a more wide-ranging review of the type proposed by Mr. Nimatallah. Either the change in procedures for conducting the review could be recorded as an understanding, or else the existing decision could be amended accordingly. Moreover, Mr. Nimatallah had suggested that the review should take place before the 50 percent point was reached, whereas the decision as it stood envisaged a review after the 50 percent point had been reached. He would appreciate further clarification on that matter.

Mr. Nimatallah explained that, in his statement, he had said, "...if the Fund's borrowing on unused credit lines were to approach that level," which was different from saying "...when it reached that level." He would prefer for the Board to undertake a review before borrowing reached 50 percent of quotas.

Mr. Salehkhou observed that, two years previously, the intention of the Board in adopting the guidelines had been primarily to strengthen the confidence of current and prospective creditors in the Fund's borrowing

policy; the guidelines had served as a clear indication that the Fund was being prudently managed, particularly with respect to financing. He largely concurred with the staff's view that frequent amendments to the decision on the guidelines did not seem desirable, for they might affect confidence in the consistency of Fund policies. However, the Executive Board should not hesitate to introduce changes aiming at greater flexibility. Moreover, the amendment of the guidelines should leave enough room for maneuver for the Executive Board and management to ensure the continuity of borrowing. Obviously, a number of amendments to the guidelines had become necessary, particularly in connection with access to Fund resources after the Eighth General Review and the establishment of new arrangements for supplementing ordinary resources.

The changes suggested by the staff seemed reasonable and in line with the general principles that had led to the adoption of the guidelines, Mr. Salehkhou continued. Specifically, the lower limit of the range for the total of outstanding borrowing plus unused credit lines provided for some flexibility and prudent management, as it was intended to trigger a new assessment of the availability of credit lines without having any effect on the continuation of the Fund's normal activities. Nonetheless, he doubted whether there was any need for the figure at the bottom of the range, because of the staff's continuous monitoring of the Fund's liquidity and financing needs and the Executive Board's ability to proceed with an assessment whenever it felt that one was justified.

He could go along with the limit on total borrowing of 60 percent of quotas particularly in view of the large uncertainties involved, Mr. Salehkhou said, and more especially because the proposed treatment of the GAB and associated arrangements would tend to increase borrowing availability excessively, regardless of whether the conditions for activating the GAB and associated arrangements had been met or not. The staff had pointed out that it would be disadvantageous to make available an unduly high proportion of the GAB, but the proportion actually proposed by the staff did not seem to reflect adequately that caution, particularly as the GAB participants interpreted the conditions for activation quite narrowly. The upper limit on borrowing would also seem justified by the nature of the new borrowing arrangements, which were likely to be of shorter duration than those of the past, and even more so by the most recent quota increase, which had clearly been insufficient to meet the Fund's needs for new resources.

While he could support the proposed changes, Mr. Salehkhou concluded, the Board also ought to consider a scheme allowing the Fund to increase its ordinary resources as an alternative to undertaking more borrowing or accepting a smaller role in world adjustment. Such a scheme would strengthen the provision that quota subscriptions should remain the basic source of Fund financing.

Mr. Malhotra said that quotas should indeed continue to be the main source of Fund financing. However, the most recent quota increase had been inadequate, so that the Fund would have to borrow in order to supplement its ordinary resources. In current circumstances, the proposal for

a single limit of 60 percent of quotas on total borrowing appeared reasonable. However, if the general view of the Executive Board was that the present range of 50-60 percent should continue, he would have no difficulty in accepting that position either. With regard to the portion of the GAB to be included, he concurred with the staff proposals.

Mr. Ercel agreed with the views expressed by the Chairman in his statement. Borrowing should not exceed 60 percent of total Fund quotas, and he would prefer a single limit rather than a range for borrowing.

Mr. Alhaimus commented that he agreed with the staff proposals regarding the GAB and endorsed the Chairman's suggestion for retaining the present limits.

Mr. Donoso said that if access limits were going to be maintained at 102 percent to 125 percent of countries' quotas through 1985, there was a possibility that total borrowing could reach 50 percent of total quotas. It would not be useful to select a limit that the Fund might reach or wish to exceed. Thus, he favored the 60 percent limit proposed by the Chairman, with the inclusion of two thirds of the GAB and associated arrangements.

Mr. Robalino remarked that he supported a limit of 60 percent of total Fund quotas for outstanding borrowing plus unused credit lines. He also agreed that the ceiling on outstanding borrowing should include two thirds of the funds available under the GAB. Finally, he agreed with the proposal to hold the next review of the guidelines for borrowing in two years.

Mr. Pickering expressed agreement with the Chairman's statement. He had no problems with the revisions pertaining to the inclusion of two thirds of the GAB and associated arrangements. For the record, he wished to record that his Irish authorities would not object to a single figure of 60 percent or even a slightly higher one if it met with broad support.

The Treasurer recalled that a question had been raised about why a change in the GAB and associated arrangements should call for a review of the guidelines for borrowing. One possible reason for review was that another associated arrangement could be concluded; in the current GAB decision, the Board had not placed any limit on further associated arrangements. Another reason was that there might be changes in the amount of the GAB and associated arrangements. After all, reviews of the GAB would not necessarily take place at the same time as the Fund's quota reviews.

An implied question had also been raised about why a sentence had been added to the first paragraph of the preamble, the Treasurer continued. Of course, it was for the Board to decide whether anything should be added to the preamble, but the references to the GAB in the proposed decision all had the same rationale. Throughout the amendments to the guidelines suggested by the staff, the point was implicit that GAB resources had become much larger in terms of Fund quotas than in the past. Moreover, in principle, the usability of the GAB had been expanded.

Mr. Prowse commented that the proposed addition to paragraph 4 of the decision--reading "or when there is a change in the GAB or associated arrangements"--might provide altogether too much of a hair trigger, because the term "a change" seemed to mean any change, and it was entirely possible that changes could occur that would not justify a review of the guidelines on borrowing. Should Executive Directors decide to include the additional clause, they might wish to qualify it by saying that the change would have to be "substantial" or "significant."

As the Treasurer considered that the guidelines would be of consequence to outsiders, Mr. Prowse went on, they would no doubt ask themselves why the Fund had included a reference to the GAB in the preamble. It would be well for Executive Directors to consider the perceptions of outsiders reading the proposed decision. The weight of argument, as suggested by Mr. Nimatallah, was that there was much to be said for not changing the rules, since a change would affect outsiders' perceptions. The rules had been in place for only a short while. He did not believe that the Fund should imply that borrowing would become more important in the future than it had been in the past. In any event, the resources of the GAB would be available to the Fund only on a contingency basis rather than on a regular basis.

The Chairman, summarizing the expressions of view by Executive Directors, observed that the sense of the meeting was to keep the limit on outstanding borrowing plus unused credit lines at 50-60 percent of total Fund quotas. The total of outstanding borrowing plus unused credit lines would include two thirds of the GAB. Finally, the Board would conduct a review of the guidelines for borrowing at the time of the Ninth General Review of Quotas. Mr. Prowse had raised a good point in suggesting that the reference to a change in the GAB or associated arrangements should be preceded by the word "significant," and he noted the interpretation favored by Mr. Nimatallah. The proposed final sentence in the first paragraph of the preamble would be omitted from the revised text.

The Executive Board then turned to the proposed decision, which it approved.

The decision was:

> 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 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 percent of the total of Fund quotas. If the total of outstanding borrowing plus unused credit lines reaches 50 percent 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 percent, but shall not exceed 60 percent of total quotas.

3. 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 these arrangements, or two thirds of the total of credit lines under 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 Ninth General Review of Quotas, or when there is a significant change in the GAB or associated arrangements, and may be adjusted as a result of such reviews.

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. 7589-(83/181), adopted
December 23, 1983

2. RATE OF REMUNERATION

The Executive Directors considered a staff paper on the rate of remuneration and the Fund's income position (EBS/83/237, 11/2/83; Sup. 1, 12/20/83; and Sup. 2, 12/22/83).

Mr. Mtei commented that any decision adopted by the Board had to safeguard the element of concessionality of Fund resources. Otherwise, the International Monetary Fund would not remain what it had originally been conceived to be. He could not, therefore, support an arrangement aiming at 100 percent of the SDR rate for remuneration, irrespective of its impact on other aspects of the Fund's operations. He would support Method 1 in the staff paper, under which the Board might raise the remuneration coefficient to 87.5 percent on May 1, 1984 and would hold annual reviews to decide whether to raise it further, if and when conditions permitted, having regard to the fundamental principles of safeguarding some concessionality in Fund resources.

Mr. Erb, thanking the staff for the rapid preparation of EBS/83/237, Supplement 2, observed that the method that provided a potential basis for consensus in the Board would be Method 3. Table 1 in EBS/83/237, Supplement 2 showed the option recommended by him: the remuneration coefficient should rise to 87 percent on January 1, 1984 and by 1 percentage point a month thereafter until it reached parity on January 1, 1985, an adjustment period that he found acceptable. It was unacceptable to him that the remuneration coefficient should be raised over either two and one-half years or five years; perhaps there was a period between one year and two and one-half years on which a consensus of the Board could be reached. If so, he could accept it. As a general principle, the longer the start of the period of adjustment was delayed beyond May 1, 1984, and the longer the period was stretched beyond one year, the more important it became to have a provision permitting an acceleration of the adjustment in the coefficient of remuneration if the SDR rate declined during any subperiod. Within Method 3, his preference would be for some form of Variant A, because Variant B would end up becoming difficult to implement, while Variant A would be potentially easier.

Mr. Polak commented that his proposal (reproduced in the Annex) was similar to Variant A at the bottom of page 2 of Supplement 2, but differed from that variant in two respects. First, his suggestion had not been to increase the coefficient of remuneration over five years by 3 percentage points at the beginning of each financial year, with an additional increase of 1 percentage point thereafter for every 0.1 percentage point that the SDR interest rate in the last week of the financial year was below the rate of the last week of any previous financial year, beginning at the end of fiscal year 1984. His proposal was not meant to be cumulative but rather alternative. Second, his suggestion was that the interest rate should be compared in the last week of the financial year not merely with the preceding year but also with any of the previous years in the period, to avoid getting an additional increase in the rate as a result of a rise followed by a decline.

The important point had been made by Mr. Mtei, and also by Mr. Malhotra, that the Fund should not raise the rate of remuneration without having regard to what happened to charges, Mr. Polak continued. The Executive Board should decide on a definite time for the proposed changes; but there could also be changes in interest rates, the outstanding business of the

Fund, and the Fund budget, the impact of any of which could be substantial. The answer was to add to the formulae a safeguard clause, under which none of the methods or variants would be applied beyond a point where the rate of charge would exceed the SDR interest rate. Thus, the Fund would recognize that there would never be negative concessionality.

Mr. de Maulde said that his preference was for Method 4, which correctly described his earlier proposal. He wished, however, to point out that a fall in the SDR interest rate by 2.05 percentage points would produce a remuneration coefficient of 100 percent under present conditions, all other things being equal. The text as written, which said that every 1 percentage point increase in the SDR rate would produce an increase of only 0.5 percentage point in the rate of remuneration, was therefore rather one-sided.

Mr. Grosche commented that, first, the Board should come to a decision on a precise timetable on when equality between the rate of remuneration and SDR interest rates would be reached, assuming that interest rates on the market remained unchanged. The timetable should avoid too rapid an increase in charges. Second, if international interest rates were to fall, the Board should speed up adjustment of the coefficient without adjusting charges. Third, if international interest rates were to increase, the Board should lengthen the adjustment period. It followed that he had some sympathy in principle with the approach outlined by the staff in Method 3, Variant B. He continued to be flexible on the time horizon for the full adjustment.

Mr. Hirao stated that his preference was for Method 3, under which equalization could be completed within a specified period of time. One year or two and one-half years would be preferable. He could go along with Variant A; he also had some interest in Variant B, if it did not become overcomplex.

Mr. Malhotra observed that Method 6 took account of some of his concerns, namely, that, in accordance with the Articles of Agreement, there had to be a flexible approach to fixing the rate of remuneration, considering all the relevant variables that might be in operation at a particular time. Table 4 illustrated that, at an SDR interest rate of 8.75 percent and with a 10 percent grant element, the rate of charge would be 6 percent; the rate of remuneration would be 6.6 percent, or 75.4 percent of the SDR interest rate, a figure below the minimum mentioned in the Articles. At the same SDR interest rate, but with a 5 percent grant element, the rate of charge would be 7.4 percent and the rate of remuneration 7.9 percent, or 90.3 percent of the SDR interest rate.

Executive Directors should first take a stance on the appropriate level of the grant element, Mr. Malhotra suggested. If the rate of remuneration were raised to 100 percent, all future increments to the Fund's administrative expenditure, and reserves, would, under the current method for computing charges be reflected in the rate of charge. Given the cooperative nature of the Fund, would it be fair for the entire additional burden of such expenditure of reserves to be loaded onto borrowers?

Calculations based on assumed rates of grant elements did not take that factor into account. In the past, the return from unremunerated assets had probably sufficed to cover such increments in expenditure, but there was apparently no cushion currently available in unremunerated positions to absorb such increments. Under the circumstances, the Board could not go so far as to increase the remuneration coefficient to 100 percent of the SDR interest rate, because it would result in an unjust distribution of burdens of the administrative expenditures of the Fund. He was not saying that under no circumstances would the 100 percent coefficient be feasible, but rather that, in light of probable developments during the next few years, equality between the rate of remuneration and the SDR interest rate as a target did not appear feasible or just. Further, the grant element was currently so low that the coefficient could not justifiably be increased, except perhaps in one small step. Thereafter, from time to time, a review of the matter should be conducted in the light of administrative expenditures, reserves, other charges, and the total business of the Fund.

Mr. Wicks remarked that as a point of principle he did not accept that the remuneration rate had to be kept below 100 percent of the SDR interest rate in order to provide concessionality or a grant element to borrowers of the Fund's resources. Borrowers from the Fund were a changing collection of countries; no one should assume that any action taken by the Board in raising the rate of remuneration was directed against any particular set of members, because one feature of the Fund was that any country could become a borrower from it, as his authorities well knew. Moreover, there were other elements of concessionality in the facilities made available by the Fund to its members.

He could not accept Mr. Malhotra's accountancy, Mr. Wicks continued. Were he to accept it, however, it would be according to the logic of his assumptions that if administrative expenses rose, the rate of charge also had to rise, whatever the rate of remuneration. In consequence, if everything else remained constant, he could agree with Mr. Malhotra that borrowers would have to bear the costs.

A well-defined program moving the rate of remuneration toward 100 percent in steps would best meet the concerns of his authorities, Mr. Wicks said. His preference was for three equal semiannual steps beginning on January 1, 1984, so that 100 percent remuneration would be reached by January 1, 1985. Nevertheless, he was willing to contemplate a moderate extension of the period in the interest of achieving some consensus within the Board.

He favored Variant B under Method 3, which bore a close resemblance to the suggestion that he had previously made in the Board, Mr. Wicks concluded. Variant B was already extremely complicated, and he suspected that, when it was expressed as a part of a legal decision its complication would only increase. He would thus prefer a formula based on Variant A, if it could be agreed upon. In order to achieve a consensus, however, he would be willing to look at a solution based on Variant B, which followed the sort of timetable he had indicated earlier.

Mr. Erb recalled that EBS/83/237 showed that at the outset of Fund operations in 1946, and for some years afterward, the effective rate of charge had been relatively high compared with rates then prevailing in the markets of potential capital exporting countries. Later, in 1951, the staff reported that an increase in charges on outstanding balances had made the charges equivalent to prevailing rates on two-year or three-year paper in New York and London. It was worth asking whether that paper had been high-quality government paper or general market paper. If the latter, what had been the relation to government paper? He disagreed with the view that somehow embedded in the principles of the Fund was the notion of concessionality, that the lending rate charged by the Fund at any time should in fact be below the cost of capital to the major capital exporting countries or those financing the Fund's operations. He would thus have trouble with the notion of trying to build in a level of concessionality in relation to market rates. Indeed, he had difficulty with the concept of concessionality per se because it was difficult to measure. Perhaps an appropriate guide would be the opportunity cost of money to the countries borrowing from the Fund. If additional grant calculations were made, the staff should include a discount rate factor that reflected LIBOR with different spreads. Clearly, the grant element in Fund loans would continue to be quite high relative to that rate.

A point had been made by Mr. Malhotra that, when there was a high level of use of Fund resources, the Fund's administrative costs in effect would be spread over a larger bulk of lending, so that the impact on the rate of charges would be smaller than at a time when there were relatively few users of Fund resources, Mr. Erb went on. One way of evening out administrative costs over time would be to take possible fluctuations into account in setting the reserve accumulation target. Such a possibility provided another argument in favor of having the reserve target rise when the rate of use of Fund resources rose, and allowing the reserve target to fall when the rate of use of Fund resources declined. There were also other ways of spreading expenses over time. In any event, it was impossible to attribute administrative costs to either creditors or debtors.

There was a danger in moving in the direction suggested by Mr. Malhotra, Mr. Erb remarked, because a logical implication of his suggestion was that the Fund's administrative expense should be financed by an annual assessment, perhaps in relation to quotas, that would seek to finance the Fund's administrative costs, if the administrative costs could be separated from those of a more general nature. The danger was that certain Executive Directors would then have to approach their national authorities for annual budget allocations, certainly not something that his authorities would eagerly look forward to. Such an assessment would also focus much greater attention on the Fund's administrative costs within his own Government. Indeed, the fact that, at present, administrative costs could not be attributed to any one particular activity made it easier for him to deal with pressures for explicit allocation of the Fund's administrative expenses. In many ways, it was better not to be too clear about how administrative expenses were allocated.

Mr. de Maulde commented that the late 1940s and early 1950s, when the rate of charge had been quite high, had represented a special period in the Fund's history. At the time, the Fund had had very little business. After the introduction of the Marshall Plan for Western Europe, there had been practically no borrowers from the Fund, which had thus experienced extreme difficulties in balancing its budget. Indeed, the Fund had had to deposit its gold with the U.S. Treasury against some paper that provided interest and had later found it somewhat difficult to recover the gold. In any event, the period was hardly comparable to the present one. He did agree with Mr. Erb that it would be extremely unhelpful to have to explain the Fund's administrative expenses to national parliamentary bodies.

Mr. Erb agreed that the circumstances around 1950 had been quite different from those in 1983. If the Fund were to set the rate of remuneration at 100 percent of the SDR rate in circumstances similar to those of 1950, the rate of charge would still be below that point. Perhaps Mr. Malhotra had been considering times at which use of Fund resources would be quite low, so that the administrative burden would be concentrated in a relatively small number of users of Fund resources. His reason for examining the past had been to cite a period in which the rate of charge had been at, or slightly above, the prime borrowing rate of governments. Thus, it was not embedded in the principles of the Fund that the rate of charge somehow always had to be below the cost of capital in the countries that were creditors to the Fund.

Mr. Polak remarked that the period around 1950 had also differed from the present period in that the Articles then had not contained the concept of remuneration. He agreed that the Fund had not been set up on the principle that debtors should always pay less than the market rate. In the past, when there had been insufficient income to meet expenditures, the Fund had found it necessary to raise the rate of charge. The question at present was how far the Fund should raise charges in order to pay remuneration, a quite different point.

The answer to Mr. Malhotra's more technical point--whether the burden of charges would be higher with larger or smaller amounts of Fund business--would depend on the interest rate, Mr. Polak continued. At low interest rates, the charges that would have to be paid rose as the business of the Fund became smaller. At high interest rates, the reverse would be true. He would agree with Mr. Erb that one possible solution might be to work through variations in the additions to reserves in order to prevent the rate of charge from exceeding the SDR interest rate.

Mr. Malhotra observed that the early 1950s were not particularly relevant to the present discussion. Concessionality had continued over a long period, much longer than the period referred to by Mr. Erb. Technically, Mr. Wicks was right that any member of the Fund could be a borrower or a creditor at any time. But a large number of member countries that had become free after the period of colonization were low-income countries, and concessionality had long formed part of the Fund's financing, despite progressive increases in the rates of remuneration

and charges. If the rate of remuneration were fixed at 100 percent and Fund revenue contracted, serious difficulties would arise. He also agreed entirely that the Fund should not get into a situation in which contributions were made subject to decisions of national parliaments from year to year, or every few years. It would be best to maintain flexibility in the rate of remuneration.

Mr. Tshishimbi noted that the suggestion that Directors should not take into account the element of concessionality in Fund operations in considering the rate of remuneration failed to explain why there were so many different rates if the Fund had not in fact intended to establish some differentiation between degrees of concessionality in its lending operations. Methods 2 through 5 had in common the fact that the grant element was completely excluded. He would urge the Board to consider Method 6, which did provide for some flexibility. Everyone agreed that the rate of remuneration coefficient should be increased. At the same time, however, consideration should be given to the grant element.

The Treasurer explained that the rates quoted for the early 1950s had been for gilt-edged paper in London and for U.S. Government paper in New York. The staff comparison of Fund charges to market interest rates was thus based on instruments of the highest quality. It was, of course, correct that there had been no authority for the Fund to pay remuneration until the First Amendment of the Articles of Agreement. Before that Amendment, the Fund had had the authority to distribute net income, which had not been used until 1968, a time when the Fund's credit had been expanding sharply relative to quotas, as it was at present. At that time, member countries' reserve positions in the Fund had become an increasingly important part of their total reserves, which had made creditor members feel that they should be compensated for the loss of income consequent to making available reserves through the Fund to other members experiencing balance of payments difficulties. The Fund had therefore made use of the authority to distribute net income on a preferential basis to members holding creditor positions. The distribution had been made at the maximum rate then permitted under the Articles of 2 percent. As mentioned, the subsequent First Amendment of the Articles had prescribed that the Fund pay remuneration on currencies used by the Fund.

Mr. Prowse said that he continued to support the idea of concessionality. As Mr. Wicks had noted, that principle in itself did not require the rate of remuneration to be less than the SDR rate. And, however concessionality was defined, one of the interesting observations that might be made was that, even with substantial administrative expenses, the rate of charge could still be less than the rate of remuneration by a significant amount, even when the rate of remuneration was equal to the SDR rate.

He was concerned that the financial strength of the Fund should be maintained, Mr. Prowse continued. It was impossible to ignore the implication of remuneration for the Fund's financial position.

Present circumstances were not necessarily the most propitious for making a strong increase in the rate of charge, which would be necessary if the Fund moved abruptly to increase the rate of remuneration to 100 percent of the combined market rate, Mr. Prowse remarked. He would favor some of the options that would allow a phasing-in period, a position that seemed to be taken by all Directors who supported moving to 100 percent. Some form of Method 3 would be preferable. At the same time, the increase should not be so large as to discourage member countries from coming to the Fund; the phasing-in period should be as long as possible. If Method B turned out to be not too difficult or too complex, he could accept some form of it.

Mr. Conrado considered it important that an element of concessionality should be maintained, a goal that would be difficult to attain if the increased rate of remuneration were targeted at 100 percent of the SDR rate. He associated himself with many of the comments made by Mr. Malhotra.

On previous occasions, Mr. Conrado went on, he had indicated that his preference would be for the remuneration coefficient to remain unchanged because of the effect that a change would have on charges. Mr. Polak's comment that the Board should not increase the rate of remuneration without paying attention to the effect on charges was important. However, in a spirit of compromise, he would be willing to accept some increase in the rate of remuneration, preferably in equal steps at fixed intervals for perhaps five years, but no fewer than three, to a target below 100 percent of the SDR rate. He could accept a proposal for 85 percent of the rate.

Mr. Nimatallah commented that all the proposed decisions should be reconsidered the following week, if the Board returned to the topic, in order to finalize the various points raised by Directors.

The Executive Directors agreed to continue their discussion in the afternoon.

DECISION TAKEN SINCE PREVIOUS BOARD MEETING

The following decision was adopted by the Executive Board without meeting in the period between EBM/83/180 (12/21/83) and EBM/83/181 (12/23/83).

3. EXECUTIVE BOARD TRAVEL

Travel by an Executive Director as set forth in EBAP/83/299, Supplement 1 (12/20/83) is approved.

APPROVED: May 7, 1984

LEO VAN HOUTVEN
Secretary

A Method for Determining the Rate of Remuneration - Note by Mr. Polak

In connection with the paper "Methods for Determining the Rate of Remuneration" (EBS/83/237, Sup. 2), the following note contains a suggestion for a variant of Method 3A, which appears on pages 2 and 3 of the paper.

Below is a possible formula 1/ for the increase in the coefficient that determines the rate of remuneration, which combines a minimum annual increase of 3 percentage points with an approximate compensation for declines in the SDR interest rate.

The rate of remuneration will be raised gradually so that it reaches the SDR interest rate on or before May 1, 1988. To this end, the coefficient that is applied to the SDR interest rate to arrive at the rate of remuneration shall be increased as follows:

(i) at the beginning of fiscal year 1985, from 0.85 to 0.88, and

(ii) at the beginning of every fiscal year thereafter, until it reaches 1.00, by the higher of

(a) 0.03, or

(b) 0.01 for every 1/10 percentage point that the SDR rate in the last week before the beginning of that fiscal year is below the SDR interest rate in the last week in any previous fiscal year, starting with fiscal year 1984.

1/ Rate of charge = coefficient x SDR rate -

$$\frac{1}{\text{Use of Fund Credit}} \left[\begin{array}{l}\text{coefficient x SDR rate x interest-free resources} \\ + \text{(1-coefficient) x SDR rate x Fund SDR-holdings} \\ - \text{100 (administrative expenses + addition to reserves} \\ - \text{income out of service charges and margins)}\end{array}\right]$$

Fixed assumptions:
Interest-free resources = SDR 3 billion
Fund SDR-holdings = .2 use of Fund credit
Income out of service charges and margins = SDR 100 million

$$\text{Coefficient} = \frac{\text{Rate of remuneration}}{\text{SDR interest rate}}$$