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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 83/182

3:00 p.m., December 23, 1983

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

Executive Directors	Alternate Executive Directors
	W. B. Tshishimbi
	L. E. J. M. Coene, 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
	C. Robalino
	G. Grosche
G. Lovato	
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
J. C. Corr, Assistant

Also Present

European Department: 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; Ph. Lachman. Middle Eastern Department: F. Drees. Treasurer's Department: W. O. Habermeier, Counsellor and Treasurer; D. Williams, Deputy Treasurer; D. H. Brown, S. I. Fawzi, R. B. Hicks, B. E. Keuppens, T. Leddy, T. M. Tran, G. Wittich. Personal Assistant to the Managing Director: S. P. Collins. Advisors to Executive Directors: A. A. Agah, E. A. Ajayi, K. A. Hansen, S. M. Hassan, W. Moerke, J.-C. Obame, Y. Okubo, I. R. Panday. Assistants to Executive Directors: E. M. Ainley, H. Alaoui-Abdallaoui, J. Bulloch, M. Camara, M. B. Chatah, G. Ercel, 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., A. Yasseri.

1. RATE OF REMUNERATION

The Executive Directors resumed from the previous meeting (EBM/83/181, 12/23/83) their consideration of a staff paper on methods for determining the rate of remuneration (EBS/83/237, Sup. 2, 12/22/83). They also had before them papers on the rate of remuneration and the Fund's income position (EBS/83/237, 11/2/83; and Sup. 1, 12/20/83), as well as a note by Mr. Polak on a method of determining the rate of remuneration, annexed to EBM/83/181.

Mr. Lovato said that his authorities believed that the Fund's charges should contain an element of concessionality and that he agreed with Mr. Polak that the rate of charge should never be higher than the SDR interest rate. The suggestion that the period of adjustment of the rate of remuneration should be lengthy had some merit, in that it took account of the impact on charges of an increase in the rate. However, proposals that set a fixed period for adjustment to 100 percent of the SDR rate were overly mechanical because they stressed only one element of the problem, while there were many uncertainties in the world financial situation, particularly with regard to the opportunities for the debtor countries to overcome their problems. Therefore, he could not agree to the idea of setting a fixed period of adjustment from the outset. While he favored a gradual increase in the rate of remuneration to equality with the SDR rate in principle, he could accept a modest increase at present, without a fixed timetable for future changes. On that basis, his first preference was for Method 2 in EBS/83/237, Supplement 2.

Mr. Lindå said that he favored a fixed period for the attainment of equality between the rate of remuneration and the SDR rate. The period should not be too long. His preference was for a proposal similar to Method 3B, provided that it was technically feasible.

Mr. Coene remarked that his first preference was for Method 4, which would bring the rate of remuneration gradually in line with the SDR rate. He could also accept Method 3; in that case, the adjustment period would have to be very long.

Mr. Robalino recalled that his original position had been that it would not be prudent to increase the rate of remuneration, but, given the need for a compromise, he could accept an increase, subject to two provisos. First, with regard to the special facilities, access under the compensatory financing facility should be set at 85 percent of quota, with the first segment set at 50 percent. Second, the rate of remuneration should continue to contain an element of concessionality. The increase should therefore be along the lines proposed by Mr. Polak.

Mr. Pickering stated that his authorities strongly held the view that a fixed timetable for achieving a rate of remuneration equal to 100 percent of the SDR rate should be introduced. A reasonable period would be a maximum of two and a half years, beginning in January 1984. Within that constraint, he favored suggestions similar to Method 3A or 3B.

Mr. Ismael recalled that he had originally believed that the best hope of a consensus was for Executive Directors either to agree on a definite increase in the rate of remuneration at a certain time, with a proviso that further increases would be subject to broad review, or to decide in principle that the rate of remuneration should equal the SDR rate, but that the increase should be spread over a given period. On that basis, he had suggested that there could be an immediate increase of 5 percent in the rate of remuneration, beginning on May 1, 1984, subject to review in 1984 but that, in any case, the rate of charge should remain at 6.6 percent. In those circumstances, the prospective deficit in the Fund's budget could be borne by the reserves until the mid-term review of the Fund's net income position in the next financial year. Having listened to the remarks by Executive Directors on the various methods outlined in EBS/83/237, Supplement 2, he was prepared, in a spirit of compromise, to reconsider his decision on the level of charges for the next financial year. His first preference was for Method 2, but if a majority of Executive Directors agreed with Mr. Polak's suggestion, he could accept Method 3A as amended by Mr. Polak.

Mr. de Maulde made the following proposal:

> The rate of remuneration will be raised gradually so that it reaches the SDR interest rate. To that end, the coefficient that is applied to the SDR interest rate to arrive at the rate of remuneration will be increased as follows, until it reaches 1.00: (i) at the beginning of financial year 1985, from 0.85 to 0.88, and (ii) at the beginning of every financial year thereafter by 0.01 for every 16 basis points that the SDR rate in the last week before the beginning of that financial year is below the SDR interest rate in the last week of the previous financial year.

The proposal was a modification of his original suggestion, Mr. de Maulde continued, to incorporate Mr. Polak's idea that there could be a small increase at the beginning of the next fiscal year.

Mr. Grosche commented that a compromise containing elements of Mr. de Maulde's suggestion and elements of other proposals might find widespread acceptance. He put forward the following proposal:

> 1. The Executive Board agrees that the rate of remuneration will be increased progressively to 100 percent of the SDR interest rate by not later than May 1, 1987.
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> 2. As of May 1, 1984, the rate of remuneration should be increased to [90] percent of the SDR interest rate.
>
> 3. Further increases in the rate of remuneration in relation to the SDR interest rate in the period from May 1, 1984 to October 1, 1985 will be made at the beginning of each quarter by 0.01 percent

for every 1/10 of 1 percent that the average SDR interest rate in the preceding quarter has fallen below the average of the SDR interest rate in the quarter ending April 30, 1984.

4. The rate of remuneration will be raised in three equal installments to achieve 100 percent of the SDR rate on May 1, 1987, beginning on January 1, 1986 unless equality with the SDR rate has already been achieved as described in paragraph 3 above.

Mr. Finaish remarked that there appeared to be widespread acceptance of the idea that the rate of remuneration could be increased beyond 85 percent of the SDR rate. Directors also appeared to be agreeing that the increase in the rate of remuneration should be gradual, although there continued to be differences of opinion on the degree of gradualism. The main area of continuing disagreement was on the question of equality with the SDR rate. Perhaps flexible language could be found to emphasize the desirability of the principle of equality at a future date, rather than ignoring it completely as in Method 1, or expressing it in a rigid manner as in Method 2.

Mr. Polak commented that it was important that the rate of charge should not exceed the SDR interest rate. A provision should therefore be added to Mr. Grosche's proposal to the effect that, if the rate of charge that would follow from the rate of remuneration determined in accordance with paragraphs 2, 3, and 4 of Mr. Grosche's suggestion were to exceed the SDR interest rate, the rate of remuneration would be set at, say, 85 percent of the SDR interest rate or at the level that would reduce the rate of charge to the SDR rate, whichever was higher.

Mr. Erb said that Mr. Polak's suggestion presented some difficulties, because it constituted a mechanical adjustment that Directors would be asked to agree to immediately, whereas future circumstances were uncertain. It should be noted that Fund charges had been set in different ways in the past. For example, between January 1, 1954 and April 30, 1963 there had been a complex set of charges that varied according to the maturity of borrowing from the Fund. At that time, charges had ranged from 4 percent to 5 percent. Other methods of determining charges deserved consideration; for example, suggestions had been made that drawings under the compensatory financing facility should carry a higher rate of charge.

Mr. de Maulde commented that there was merit in the idea of varying the rate of charge according to the maturity of the drawing. If other Directors were prepared to accept lower charges for short-term drawings, he could accept higher charges for longer-term drawings.

Mr. Polak said that he agreed with Mr. Erb that there ought not to be an automatic relationship between the rate of charge and the rate of remuneration. There were many ways in which the Executive Board could determine the rate of charge and, if Directors believed that a given formula would result in a rate of remuneration less than 100 percent of the

SDR rate, they could change the formula for the rate of charge in order to maintain the 100 percent level for the rate of remuneration. His proposal did not exclude such a possibility.

Mr. Erb considered that the period of adjustment proposed by Mr. Grosche was too long. Perhaps adjustments could be made on a monthly, instead of a quarterly, basis.

Mr. Grosche said that he could accept monthly adjustments. However, whether the period was a month or a quarter, it was important that account should be taken of a situation in which interest rates rose within the period, then fell--but not by enough to offset the previous increase--and then rose again. Not every decrease in interest rates should trigger an adjustment of the rate of remuneration, only those decreases that offset the previous increases calculated on a cumulative basis.

Mr. de Maulde stated that, leaving aside for the moment the length of the adjustment period, he could agree with Mr. Grosche's proposal so long as the initial increase in the rate of remuneration from 85 percent of the SDR rate to 90 percent could be accomplished without raising the rate of charge. The initial adjustment should be limited to the maximum level that would not trigger an increase in the rate of charge.

Mr. Grosche replied that if other Directors had difficulty in accepting an increase to 90 percent of the SDR rate at the outset, he was prepared to compromise.

Mr. Wicks commented that Mr. Polak's suggested addition to Mr. Grosche's proposal was too rigid, since the circumstances in which it might be applied were unknown. It could also tend to insulate the administrative budget from the pressures necessary to keep it under control. Perhaps the spirit of Mr. Polak's suggestion could be dealt with if the Executive Board agreed that there would be a review if the rate of charge ever approached a certain percentage of the SDR rate. He agreed with Mr. Erb that the period of adjustment proposed by Mr. Grosche was rather long, particularly if the initial increase was to less than 90 percent.

Mr. Erb said that he agreed with Mr. Wicks that it would be unfortunate if the rate of remuneration were to be adjusted downward simply because it equaled the rate of charge. There appeared to be an implication that in such circumstances the net debtors would be paying for the Fund's administrative expenses, with an underlying assumption that those members should not pay for such expenses. At present, net creditors, broadly defined to take account of unremunerated positions, bore the entire burden of administrative expenses.

Mr. Malhotra considered that it was wrong to suggest that the debtor countries were not contributing to the Fund's administrative expenses; indeed, in recent years, charges and front-end fees had amounted to about one third of the administrative expenses. It was true, of course, that creditors had also been contributing to those expenses.

Mr. Erb said that he had specifically referred to net creditors and net borrowers. On that basis, it could be argued that the net creditors financed the Fund's administrative costs at present.

The Deputy Treasurer remarked that, in a sense, both Mr. Erb and Mr. Malhotra were correct. To the extent that the rate of remuneration was below a "market" rate, the Fund's net creditors provided an effective subsidy to the Fund by keeping down the level of remunerated expense. On the other hand, the Fund had only two sources of income: interest on SDR holdings, which was determined by the Executive Board's policy, and income from charges (including the service charges) on outstanding balances. Both sources of income covered all expenses including reserve accumulation. The question of concessionality was a matter of which side of the balance sheet was being examined.

Mr. Malhotra said that he had not intended to suggest that the present rate of remuneration did not contain an element of concessionality. However, if the rate of remuneration was raised to 100 percent of the SDR rate and the rate of charge increased as a result, the cost to borrowers would increase substantially, thereby eliminating concessionality.

Mr. de Maulde stated that, speaking personally, he could accept Mr. Grosche's proposal with a number of amendments. First, the period of adjustment should end on May 1, 1989, not May 1, 1987. Second, the initial increase in the rate of remuneration should be to about 88 percent, not 90 percent. At any rate, the increase should not result in an increase in the rate of charge. Third, if the adjustment period was five years, as he had proposed, the halfway point would be October 1, 1986. Finally, the rate of remuneration should be increased to 100 percent of the SDR rate in five equal installments beginning January 1, 1987, not in three installments beginning January 1, 1986.

Mr. Erb remarked that the period of adjustment in Mr. Grosche's proposal was too long. He could accept an increase in the rate of remuneration to 90 percent of the SDR rate beginning in May 1984, but the proposal should be modified to increase the probability that the level of 100 percent of the SDR rate would be reached by October 1985.

Mr. de Maulde commented that Mr. Erb's suggestion implied that interest rates would not decline in the coming 18-30 months, an unlikely prospect, given the policies being pursued in some major countries.

Mr. Erb replied that it was not a matter of forecasting the course of interest rates, but of ensuring that the rate of remuneration reached 100 percent of the SDR rate in a reasonable period of time, no matter what happened to interest rates.

Mr. Malhotra observed that there were many proposals with various suggested modifications before Directors. It might be difficult for some Directors to consider only one proposal without further consultation with their authorities.

The Chairman remarked that it was important, nevertheless, for Directors to focus on formulas that might provide grounds for a compromise. Quite a few proposals had been put forward, and there appeared to be some convergence of views, although significant differences remained. A considerable number of Directors had found some merit in Method 3A or 3B or in a proposal along the lines of Mr. Polak's, which was fundamentally a variation of Method 3. However, agreement on a proposal acceptable to all Directors would require further compromises.

Mr. Grosche suggested that the Executive Board could meet again on December 27, 1983, allowing Directors time for reflection and for consultation with their authorities.

Mr. Malhotra said that he would prefer the Executive Board to take up the issue again in January 1984.

Mr. de Maulde stated that he agreed with Mr. Malhotra.

Mr. Erb remarked that putting off a decision until January could create uncertainties for the ongoing negotiations with potential lenders to the Fund.

Mr. Polak commented that Mr. Grosche's proposal was a valuable attempt at a compromise solution. He hoped that, after reflection, all Directors would find it acceptable, perhaps at a meeting on December 27 or December 28.

Mr. Prowse observed that the resolution of the current problem might depend on the Executive Board's decisions on other issues. Perhaps a compromise "package" could be considered.

Mr. Erb said that he agreed with Mr. Prowse.

The Chairman stated that the Executive Board would meet again on December 28, 1983 to consider the question of the rate of remuneration, together with decisions on the policy on enlarged access and the access limits for special facilities.

The Executive Directors took note of the Chairman's remarks.

DECISION TAKEN SINCE PREVIOUS BOARD MEETING

The following decision was adopted by the Executive Board without meeting in the period between EBM/83/181 (12/23/83) and EBM/83/182 (12/23/83).

2. UGANDA - TECHNICAL ASSISTANCE

In response to a request from the Governor of the Bank of Uganda for technical assistance, the Executive Board approves the proposal set forth in EBD/83/326 (12/19/83).

Adopted December 23, 1983

APPROVED: May 7, 1984

LEO VAN HOUTVEN
Secretary