

DOCUMENT OF INTERNATIONAL MONETARY FUND AND NOT FOR PUBLIC USE

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Correction 1

CONFIDENTIAL

September 16, 1988

To: Members of the Executive Board

From: The Acting Secretary

Subject: Report of the Executive Board to the Interim Committee of the
Board of Governors on Overdue Financial Obligations to the Fund

The following correction has been made in EBS/88/166, Revision 2
(9/9/88):

Page 2, para. 2, lines 9 and 10: for "institution. Moreover, while...
they do not"
read "institution. These costs have...
these actions do not"

A corrected page is attached.

Att: (1)

INTERNATIONAL MONETARY FUND

Report of the Executive Board to the
Interim Committee of the Board of Governors
on Overdue Financial Obligations to the Fund

September 9, 1988

1. Introduction

The communiqué of the Interim Committee issued after its meeting on April 14-15, 1988 stated that:

In its discussion of conditionality, the Committee reaffirmed the cooperative nature of the Fund and stressed the importance of preserving the revolving character of its resources. Members should continue to give the highest priority to fulfilling their financial and other obligations to the institution. Failure to honor these obligations had adverse effects on overdue members' financial standing and imposed an undue burden on other members. The Committee requested the Executive Board to review the question of the overdue financial obligations and to submit a report at the next meeting of the Committee on measures to reduce and eventually eliminate arrears.

In the 1970s, most of the members now facing protracted arrears to the Fund relied heavily on foreign assistance or other capital inflows to finance their sizable external imbalances. By the early 1980s, the economic and external payments positions of these countries had weakened markedly, reflecting both adverse external developments and inadequate economic policies. Serious debt servicing difficulties emerged and capital inflows, especially from private sources, declined sharply. These members found it increasingly difficult to meet their debt service obligations, including those to the Fund. It should be emphasized, however, that most members faced with adverse external circumstances have managed to stay current on their financial obligations to the Fund.

Overdue financial obligations to the Fund have increased from SDR 60 million at the end of 1983 to SDR 2.4 billion as of end-August 1988, of which SDR 1.9 billion was overdue for six months or more (see Attachment I, Table 1). Fund credit outstanding to the 13 members presently subject to complaints amounted to SDR 3.5 billion as of August 31, 1988 (Attachment I, Table 2), or 13 percent of total Fund credit outstanding. Eight of these members have been declared ineligible to use the general resources of the Fund.

The problem of protracted overdue obligations to the Fund, while remaining confined to a relatively few members, poses serious costs and risks not only for the individual members concerned but for the membership at large and for the Fund itself, affecting its financial integrity and the credibility of the economic programs supported by the Fund. It is vital for the financial position and future role of the Fund in the international monetary system as a cooperative monetary institution that the problem of arrears be solved early. A few Directors indicated that the willingness of their authorities to agree to increases in the Fund's resources could be impaired, while a large majority of the Board considers that a substantial increase in quotas to be decided before April 30, 1989 is well justified. Executive Directors have emphasized the Fund's central role in the international monetary system and its function in supporting policies without which the effectiveness of financial assistance provided by other creditors and donors would be seriously undermined. Resolution of the cases of arrears and restoration of access of the members concerned to Fund resources are therefore of broad international interest. Solutions in many of the present cases of protracted arrears will require special attention and exceptional efforts by the international community at large. The intent would be to pave the way for a restoration of orderly relations with all creditors and donors, renewed financial flows, and a resumption of sustained economic growth.

To meet the problem of overdue obligations, the Fund has implemented and adapted over time a series of policies and practices, summarized in Attachment II. It has also taken steps to strengthen its financial position, primarily by protecting income from the effects of overdue charges and building up its precautionary balances, financed by its debtor and creditor members through the "burden sharing" mechanism (Attachment I, Table 3). These protective actions have, however, imposed substantial direct costs on members, debtors and creditors alike, that meet their obligations to the institution. These costs have been particularly burdensome on those countries which have made use of Fund resources and continue to meet their obligations to the institution, often in the face of very difficult circumstances. Moreover, while basically protecting the Fund's income position, these actions do not fully address the risks and effects on the Fund's liquidity and financial position arising from overdue repurchases.

Executive Directors are of the view that there is an urgent need for new initiatives to solve the problem of arrears and to prevent its reemergence. This report proposes for the Committee's consideration and guidance a framework for a revitalized and strengthened approach to resolving the problem of arrears, consisting of three broad elements: preventive actions, intensified international collaboration, and remedial measures. The Executive Board also intends to maintain and, as appropriate and feasible, strengthen measures to safeguard the financial position of the Fund in light of the problem of overdue financial obligations to the Fund.