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04

February 14, 1986

To: Members of the Executive Board
From: The Acting Secretary
Subject: Final Minutes of Executive Board Meeting 85/49

The following correction has been made in the final minutes of EBM/85/49 (3/25/85):

Page 3, para. 2, line 4: for "(SM/85/64, 2/22/85;"
read "(SM/85/65, 2/22/85;"

A corrected page is attached.

Att: (1)

Other Distribution:
Department Heads

1. EXECUTIVE DIRECTOR

At Informal Session 85/1 (3/25/85), the Chairman bade farewell to Mr. Tshishimbi on the completion of his service with the Executive Board.

2. SURVEILLANCE - ANNUAL REVIEW, AND WAYS OF ENHANCING EFFECTIVENESS

The Executive Directors resumed from the previous meeting their consideration of a paper prepared by the staff for the 1985 annual review of the implementation of surveillance and on ways of enhancing its effectiveness, together with background material (SM/85/65, 2/22/85; and Sup. 1, 2/28/85; Cor. 1, 3/20/85; and Cor. 2, 3/22/85).

The Economic Counsellor noted that it had not been intended that the reference in the sentence quoted by Mr. Sengupta from page 9 of SM/85/65 to not encouraging "inflationary policies in low-inflation countries to ease the adjustment problems of countries that had not succeeded in controlling inflation" should suggest that there might not be a need for expansionary policies. The intention had been to refer strictly to inflationary policies. The general observation by Mr. Dallara, based on a sentence on page 27 of SM/85/65, called attention to the structural improvements in the functioning of goods and labor markets that were needed to significantly improve economic performance and rates of unemployment in industrial countries. Mr. Dallara also indicated that the staff had not paid the same attention as in the World Economic Outlook to the impact on exchange rates of broad macroeconomic and structural policies. However, the entire spectrum of policies had been discussed in Section III.1 of SM/85/65, and structural adjustment was also covered in Section III.4. Certainly, the staff shared Mr. Dallara's point of view on the needed structural policies.

The Director of the Exchange and Trade Relations Department considered that the discussion had been constructive, bringing out the various points of view on the ideas put forward in the staff paper and the problems that might be associated with them. The record of the meeting would be a useful guide and the balance of views would of course be reflected in the summing up of the discussion. His own responses on the issues that had been raised with varying degrees of force should not be interpreted as being slanted in one direction or another. In that connection, it should be noted that although the staff had had the benefit of the work done by other groups, including the G-10 Deputies, who had raised some of the broader issues to be probed in future, it should not be concluded from the emphasis in Section V.2 on the industrial country groupings in which the Fund had participated that advice and suggestions from other groups would not be welcome. The work of the G-5 had been emphasized simply because it was in that and similar groups that such issues of "peer pressure" were being discussed.

The various suggestions made during the discussion would of course be considered carefully by the staff, the Director added. The results should become visible in staff reports prepared during the course of the year or would be reflected in the next paper prepared by the staff on surveillance. Certainly, the staff was in no sense complacent about the state of surveillance; to heighten its effectiveness it would be important to maintain the flow of ideas from all quarters.

In retrospect, some of the language in SM/85/65 had not been as well chosen as it might have been, the Director of the Exchange and Trade Relations Department remarked. For instance, a better word than "bilateral" would have to be found to describe the Fund's surveillance with respect to individual members in contrast to the Fund's relationship with and participation in the work of outside agencies. Similarly, the reference to countries being "committed" only to consult with the Fund had perhaps been misleading in the sense that the word "committed" was used in a nonlegal context. The issue in the latter respect was of course how countries were understood to respond to summings up of Article IV consultation discussions in the Executive Board. Members had not considered that they were required, for instance, to change their fiscal policies if the Executive Board felt that that was desirable; rather, they considered that they were only required to take into account the advice or opinion of the Executive Board. The purpose of the present review of surveillance was in fact to find ways to bring pressure to bear on members to take the Board's advice more seriously. No doubt the Legal Department could cite the provisions enabling the Board to react more strongly if it found that a member was manipulating its exchange rate or the international monetary system, contrary to its obligations under Article IV, Section I(iii). There had been no intention to deal with that issue in the staff paper under discussion.

As the Economic Counsellor had explained, the reference to there being no question of encouraging inflationary policies had been meant to reaffirm the sovereign right of member countries to set their own priorities, the Director added. Expansion might be a necessary priority, but inflation in the current world environment had been thought of as an unacceptable one.

The proposed decision, as drafted, mentioned the Managing Director's summing up because the staff had thought that the Executive Board would wish to emphasize flexibility and willingness to consider ways of improving the Fund's record of surveillance rather than simply continuing past practices, the Director explained. Many of the suggestions in the staff paper had been put forward as ideas for Executive Directors to explore rather than as proposals for endorsement. The summing up would be a guarded description of the degree to which experimentation could proceed in ways that would enhance the outcome with respect to surveillance. It would be up to Executive Directors to consider whether the summing up was correctly guarded without indicating their endorsement of a movement by the staff away from the generally agreed procedures followed in the immediate past.