

March 3, 1997

**Concluding Remarks by the Chairman
Capital Account Convertibility and the Role of the Fund:
Review of Experience and Consideration
of a Possible Amendment of the Articles
Executive Board Seminar 97/2—February 26, 1997**

This has been a fruitful discussion. Directors recognized that, in light of the forces shaping the international monetary system, particularly the very rapid growth and increased integration of international capital markets, it was timely for the Fund to consider how to ensure that it discharges effectively its mandate of overseeing the international monetary system, if necessary by a possible change in the Articles of Agreement.

Directors agreed that an open and liberal system of capital movements is beneficial because it contributes to an efficient allocation of world savings and investment, and thereby promotes economic growth and prosperity. At the same time, Directors recognized that capital account liberalization should be an orderly and sustainable process, as part of a broad and well-sequenced reform effort involving sound macroeconomic policies and strong financial systems. Directors believed that the Fund, as the principal international monetary institution with universal membership, was uniquely placed to promote capital account liberalization and the smooth operation of international capital markets. It was, of course, observed that the absence of a formal mandate to foster capital account liberalization had not prevented the Fund from playing an important role in encouraging and supporting members' efforts toward liberalization and in monitoring international capital markets. Nevertheless, it was also pointed out that global integration was no longer limited to goods and services, but now encompassed capital flows, and it was in the common interest of all members for the Fund to promote global integration. Therefore, most, if not all, Directors supported an amendment of the Fund's Articles at least to include the liberalization of capital movements in the mandate of the Fund; a few Directors, while not opposed to an amendment, felt that there was no urgency to rush to an amendment and that more work needed to be done, particularly in defining the operations to be covered and the nature of the transitional and emergency measures to be adopted for the implementation of this mandate.

Directors supported the intensification of the Fund's surveillance and technical assistance efforts in promoting capital account convertibility. Indeed, Directors endorsed a broadening of those efforts to devote greater attention in Article IV consultations to regulations governing capital movements, including assessments of the role of specific controls, their appropriateness, and the scope for their removal, taking into account the specific circumstances of individual members. The expansion in the Fund's information on the regulatory framework for capital movements was seen as a key part of this effort.

In discussing the architecture of possible amendments to the Articles of Agreement, Directors considered that more work was needed on the details, especially the operational implications of an expanded mandate for the Fund. Nevertheless, there was substantial agreement on several broad principles.

First, Directors recognized the importance of amending Article I to make the promotion of orderly and sustainable capital account liberalization a specific purpose of the Fund.

Second, many, if not most, Directors agreed that the Fund should be given also jurisdiction over capital movements.

Third, all Directors agreed that any extension of jurisdiction would have to allow for sufficient flexibility through transitional provisions and approval policies. Progress in that domain was seen basically as a process. In that context, Directors emphasized the importance of sequencing liberalization with structural measures, especially in the monetary and financial sector, and of pacing liberalization to the circumstances of each individual member. Directors were also sensitive to the possible needs of countries to impose temporary restrictions as a means of addressing sudden surges in capital flows. In that context, it was generally agreed that, given its mandate to oversee the international monetary system, the Fund should play a central role in determining when macroeconomic and balance of payments considerations supported adherence to—or permitted exemptions from—obligations relating to capital account liberalization; an amendment inspired by those considerations would indeed serve as a useful means of preventing backsliding.

Finally, on the scope of jurisdiction, Directors who supported an extension of jurisdiction generally agreed with the staff on the limitations of a narrow approach, and considered it important to go beyond payments and transfers to include at least certain underlying transactions in both inward and outward directions. As to the underlying transactions that would be included, Directors urged more work on defining what would be the desirable extent of the jurisdiction of the Fund, with due respect to the Fund's purposes and the institutional responsibilities of other international organizations and initiatives. Some noted that the distinction between portfolio and foreign direct investment flows was useful in that regard. Others referred to a distinction based on the right of establishment. I note, also, the reference made at the end of our discussion to the possible listing and definition of measures. All are avenues to be pursued in our work over the next few weeks and months.

Directors discussed a number of other issues, all of which will be explored further. For example, a number of Directors stressed the importance of ensuring that Fund jurisdiction did not interfere with members' right to impose restrictions, particularly for prudential reasons. With respect to the financing implications of an amendment, Directors underscored that moral hazard was to be avoided in financing capital outflows, and thus the need to retain a distinct constraint on the financing of such flows by the Fund. While some Directors were of the view that this could be achieved by retaining a specific limitation in the Articles on the financing of

large or sustained capital outflows, others were of the view that the Fund should delete that provision and rely on other provisions of the Articles and Fund policies, to be defined, as a means of maintaining that constraint. Several Directors mentioned that, in preparing for an amendment of the Articles, we should be mindful that here we are dealing with prerogatives of national parliaments and that we should adapt our language accordingly.

Regarding next steps, the Interim Committee has requested the Executive Board to report on possible changes in the Fund's Articles by its forthcoming meeting. In responding to this request, I would suggest that the staff prepare a brief paper that addresses the key issues raised in today's meeting, including the coverage of transactions included in an extension of the Fund's jurisdiction and financing by the Fund. This paper would serve as the basis for a new meeting of the Executive Board that would aim to continue our work, in a more formal format, in identifying and, if possible, agreeing upon recommendations to the Interim Committee and preparing our report to the Interim Committee on the progress that has been made and remains to be made on this subject.

