

## INTERNATIONAL MONETARY FUND

## Minutes of Executive Board Meeting 69/82

#12

10:00 a.m., September 3, 1969

P.-P. Schweitzer, Chairman  
F. A. Southard, Deputy Managing Director

Executive Directors

E. Asp  
W. B. Dale  
L. Escobar  
  
P. Liefstinck  
B. K. Madan  
  
F. Palamenghi-Crispi  
A. Phillips O.  
  
J. O. Stone  
H. Suzuki  
B. Tann  
  
L. A. Williams  
A. W. Yaméogo

Alternate Executive Directors

S. Jónsson  
J. S. Hooker  
R. H. Arriazu  
M. Horgan  
E. da S. Gomes  
M. A. Merican  
  
G. Huntrods  
C. Bustelo  
M. A. Sandoval  
B. de Maulde  
A. Mansour  
L. Fuenfgelt  
G. P. C. de Kock  
  
J. Roelandts  
  
L. M. Rajaobelina

W. L. Hebbard, Secretary  
C. N. Marsh, Assistant

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Also Present

Asian Department: H. Jensen. European Department: L. A. Whittome, Director; W. A. Beveridge, H. Ponsen, A. Wright, A. G. Tyler. Exchange and Trade Relations Department: C. D. Finch, Deputy Director. Legal Department: P. R. Lachman, O. C. A. Snelling. Research Department: D. Kelleher, B. Smith. Secretary's Department: D. Coker, J. A. Kay. Treasurer's Department: W. O. Habermeier, Treasurer; D. S. Cutler. Western Hemisphere Department: J. F. van Houten. Bureau of Statistics: W. E. Davies. Technical Assistants to Executive Directors: H. Bobadilla, J. M. Chona, D. Frommel, B. Jensen, R. Patti, H. G. Schneider, J. Skutle, J. A. Sogo, P. Stek, W. Stoop, G. F. Taylor, N. Tsukagoshi, J. R. Vallet.

1. DEATH OF MR. M. W. O'DONNELL

The Chairman announced the death of Mr. M. W. O'Donnell, former Executive Director of the Fund, and said that he had sent a cable of condolence.

2. APPROVAL OF MINUTES

The minutes of Meetings 69/44, 69/47, 69/48, 69/52, 69/53, 69/56, 69/58, 69/59, 69/60, 69/62, 69/63, and 69/64 were approved.

3. JAPAN - DISCOUNT RATE

Mr. Suzuki reported that the discount rate of Japan had been increased from 5.84 per cent per annum to 6.25 per cent per annum, and the ratio of reserve requirements to demand deposits had been increased from 1 per cent to 1.5 per cent. The increases were precautionary measures taken to prevent excessive economic expansion, and to ensure stable growth of the Japanese economy. In addition, the method of quoting discount rates and interest rates in general had been changed from the "per diem" basis hitherto followed, to an "annual percentage" basis, in order to conform with world practice.

4. AUSTRALIA - 1969 ARTICLE VIII CONSULTATION

The Executive Board considered the staff report on the 1969 Article VIII consultation with Australia (SM/69/111, 7/18/69, Sup. 1, 7/22/69, Sup. 2, 7/25/69, and Sup. 3, 8/29/69).

Mr. Stone observed that the staff report, including the supplements, was very comprehensive, and there was nothing that he could usefully add to it at that time.

Mr. Dale said that growth and restructuring of the Australian economy had been vigorous over recent years; manufacturing output had advanced sharply overall, particularly in terms of productivity, and a mineral and associated foreign investment boom had been superimposed on that strong advance. Meanwhile, farm output had recovered from the previous drought levels. With that rapid growth, financial arrangements had recently tended to produce what appeared to be the danger of excess liquidity. Some progressive weakening of the Commonwealth fiscal situation had contributed to that development, as had central bank financing of agricultural stocks and the rather unexpectedly strong balance of payments. The expansion, while strong, and in danger of becoming excessive, seemed nonetheless to have remained rather remarkably

well balanced. Recent evidence in Supplement 3 of the report, however, suggested a trend toward overtight labor markets, and perhaps some ominous developments in prices.

Under existing conditions, Mr. Dale observed, the recent fiscal and monetary actions described in Supplement 3 of the report appeared to be definitely on the right track. The fiscal position of the Commonwealth had apparently tipped distinctly in a counterinflationary direction, particularly when account was taken of the interesting indications on page 3 of Supplement 3 of the report (for 1968/69) and on pages 3 and 4 (for 1969/70), of the distinction between domestic and overall transactions in the budget--incidentally, that was a statistical and analytical tool whose wider use would be worthwhile. Monetary policy had also been shifted toward restraint through what seemed to be appropriate employment of both open market operations and higher reserve requirements. The associated interest rate developments also seemed to be an appropriate step toward improved financial arrangements.

The balance of payments, Mr. Dale noted, continued strong, especially so far as trade was concerned. Surprisingly little of the apparent gathering inflationary pressure seemed to have spilled over into rising imports. In relation to the external situation, he found particularly interesting the comments in the full paragraph on page 22 of Part I of the basic report on the relationship between the growth in domestic liquidity and the official reserves. He did not recall having seen such comments previously, and he thought in the future those relationships might be worth exploring further, both for other countries and for the membership as a whole.

It appeared to Mr. Dale that Australian policy had moved onto a course of greater restraint early enough for really severe measures to be unnecessary. He hoped that that judgment would prove correct, and believed that the future prospects for Australia were very bright.

Mr. Huntrods said that as far as past performance was concerned, one could not fail to be impressed by the consummate skill with which the Australian authorities had managed their affairs, and he fully endorsed the tribute to them contained in the first paragraph of the staff appraisal in the report. The past skill of the authorities was in itself sufficient to engender confidence that the emerging problems would be equally successfully surmounted. The areas of difficulty were clearly pointed up in the staff appraisal, and it was obvious that they were in the forefront of the Australian authorities' minds. Certainly the buildup of liquidity at the time when resources were coming under severe strain, and demand pressures were increasing, was giving cause for some concern. Though it seemed from Supplement 3 of the report that the rate of expansion of private consumption in the first half of 1969

was less than had been expected, he noted that a resumption of rapid growth, especially in the fourth quarter, was deemed probable. That served to underline the stress laid by the staff on the importance of absorbing liquidity; and in view of the staff's comments on the interest rate structure and the need to attract private savings, contained on pages 22 and 23 of Part I of the report, it was interesting to note that the July Commonwealth cash loan had raised only some \$A 96 million, despite the rise in yields on government securities which had taken place. This compared with \$A 125 million raised by the first loan of the previous financial year. That seemed to be a somewhat disappointing result, and he imagined that it might have been a factor in the subsequent decision to increase the banks' statutory reserve deposits--the maximum interest rate banks could charge on overdrafts--and the banks' maximum fixed deposit interest rates. He then asked whether the staff would give its view of the result of the loan, and whether, in the circumstances it was as satisfactory as might have been hoped.

The overall effect of the budget seemed to Mr. Huntrods to be more expansionary than might have been hoped, even though the rise in domestic expenditure on goods and services was lower than in previous years. Moreover, on page 14 of Part I of the report it was forecast that the Commonwealth Government would take a strong line in connection with large increases in assistance to the State governments. It seemed to him, however, that the Premiers' Conference and Loan Council meeting had apparently resulted in an even larger increase in that assistance for 1969/70--10 per cent--than for 1968/69--7.8 per cent. He therefore asked the staff for comments on the appropriateness of the budget in present circumstances, especially in view of the authorities' decision to tighten monetary policy so soon before the budget was completed..

Turning to the balance of payments prospects, Mr. Huntrods wondered whether the views expressed at the bottom of page 10 of Part I of the report might not be slightly overoptimistic. Although there was likely to be a substantial rise in the volume of exports, export receipts might be affected by the recent decline in wheat prices arising from overproduction; further, the surplus from the recent Australian harvest must have increased the difficulty of overseas sales. On the import side, he believed that the forecast for 1969/70 might be somewhat low. While the average imports had remained reasonably stable over a number of years, they had been exceptionally low in 1968/69, partly as a result of cuts in defense imports. He noticed that the Australian pre-budget White Paper had said that to assume that the trade account would again be close to balance would be leaning toward the more favorable end of the range of possibilities. Further, it was interesting to note that the figures for July 1969 did show a sharp rise in imports, although it would be wrong to pay too much attention to one month's figures.

Mr. Huntrods believed that the picture of prospects for capital inflow painted by the Australian authorities, as described on page 12 of Part I of the report, might be somewhat overoptimistic. He noticed, in that respect, that the prebudget White Paper again took a somewhat more cautious line, and indicated that forecasts of other capital inflows on private account sometimes could not be much better than a guess. Fund raising abroad had become more difficult, and it seemed more realistic to expect that new direct investment from abroad would be less in the current year than in the preceding one. Total investment in institutional loans appeared to have declined in the preceding year, and it seemed prudent to allow for further decline in the current year.

Miss Fuenfgelt was encouraged by the strong overall yearly growth of the developing economy of Australia, which had taken place in an environment of relative price stability, although price increases of 3 per cent per year were somewhat higher than would be desired for a completely satisfactory performance. Nevertheless, the degree of stability had been enough to inspire the confidence of investors inside the country and abroad, and to attract foreign capital and foreign labor, which were needed for the development of the country. Structural changes made in the economy during recent years had helped to make its expansion less dependent on weather conditions, and to assure a greater degree of continuity in growth. The exploitation of mineral resources, termed in the report as "spectacular developments," should give further impetus to continued growth and additional structural changes. However, that favorable outlook was dampened somewhat by the danger that Australia might be at the brink of overheating. Many sectors of the economy were operating at full capacity; and so private and public demand in the forthcoming months would determine whether severe bottlenecks would develop. During the previous five-year period, private consumption had lagged behind the growth of GNP, and, therefore, room had been left for noninflationary financing of increasing investment. Recently, however, there had been a rapid acceleration of private consumption--although somewhat less than had been expected in the first half of 1969. Wage developments would be a crucial factor, and the tightening labor market would make the task of the Arbitration Commission in the national wage case in October a difficult one. Further tightening of the labor market could only be avoided if immigration would remain at least at its present level. It would be necessary to have a sufficient number of people, with the required proportions of skilled and trained ones needed by Australia. She asked for the staff's opinion of the situation and of the outlook for the future.

In the fiscal field, Miss Fuenfgelt noted that considerable progress had been made in reducing deficits in the federal budget; the statistics in Supplement 3 showing how much revenues had increased and expenditures reduced in comparison to original estimates were quite impressive. She hoped that the same restraint would be exercised in the new budget, at

least as long as high demand and pressure on domestic resources continued. There seemed to be uncertainty with respect to developments in regional public budgets, which in the past had largely counteracted the policy of restraint of the Commonwealth. It was never an easy task to convince State and local authorities to adapt their spending intentions to cyclical necessities as seen by a central government. In the Commonwealth, however, the authorities were to be commended for their assurance to the Fund's representatives that a strong line would be taken against any large increases in expenditures of the State and local authorities. She added that the question asked by Mr. Huntrods concerning the Commonwealth Premiers' Conference in June had also occurred to her.

Miss Fuenfgelt believed that the steps which had been taken in the monetary field to reduce liquidity in the banking and private sectors were timely and appropriate. The recent measures taken to moderate the growth in bank lending by increasing statutory reserve deposits, announced on July 31, 1969, seemed to be at least as helpful as the policy of influencing interest rates by open market operations with Commonwealth securities; but in the foreseeable future there seemed to be scope for tightening rather than for easing both types of policies.

Miss Fuenfgelt then asked a question with respect to the policy of the Australian authorities on participation of foreign capital in the country. She remembered that some time ago the press had reported that the Government was considering measures to avoid extensive participation of foreign capital in Australian enterprises, and the staff report, on page 106 of Part II, gave some information on measures taken by the Australian Stock Exchanges to resist foreign takeovers. Since such measures exerted a strong influence on future capital input, she asked whether the authorities now intended to place restrictions on foreign participation in Australian enterprise, or whether the previous liberal policy would be continued.

Mr. Madan congratulated the Australian authorities on an impressive record of steady economic growth despite unfavorable weather conditions and a deterioration in the terms of trade during the past few years. The economy on the whole had displayed considerable resilience and had made significant progress toward diversification. Further, growth had been achieved without erosion of relative price and financial stability. A high level of employment had been maintained without undue cost-push pressure on prices. Although the discovery of mineral wealth, aided by the inflow of capital and an increase in productivity from better techniques in all sectors, had contributed to the steady growth, the skill and dexterity of the authorities in adapting policy postures to the changing environment played a commendable role in redeploying resources necessary to sustain the buoyant trend of the economy. The balance of payments position and international reserves had also been generally satisfactory.

However, Mr. Madan observed the emergence of some cautionary signals. Because of increased demand, fed primarily by private fixed investment and increased government outlays, the economy might have to reckon with some degree of overheating. For the present, however, the balance between growth and stability appeared to have been well maintained, and due regard had been given to balance of payments considerations. On the horizon could be seen the reflection of danger from the recent tightening of the labor market. Although the authorities, assisted by the high rate of immigration, had in the past achieved marked success in that difficult area, he hoped that they would be able to continue to contain those pressures. The report referred to the emergence of large stocks of wheat because of selling problems, and he wondered whether those stocks resulted from a continued increase in productivity, or from an earlier policy of a deliberate shift from sheep raising to wheat production. He asked for staff comment regarding the relative outlook for those two primary-producing segments of the economy.

Turning to the overall scope for fiscal and monetary policies, Mr. Madan said that while there appeared to be a shift to reliance on monetary policy in the immediate future, that did not minimize the significance of fiscal policy. Nor had there been a loss of flexibility in the fiscal system, though the appropriate forms of fiscal action might have been changed. He believed that the present emphasis on restraining outlays by the Federal Government on the one hand, and on improving the fiscal position of States on the other hand, was well placed. The budget deficits of the States had shown a marked increase, even after considering the greatly increased volume of grants from the Commonwealth Government. That aspect of federal finance was familiar to many other countries as well, particularly with respect to the contrast between the relative rigidity of State revenues as against the elasticity of central government tax receipts. He believed that more attention to that question, especially in terms of greater initiative by the States, might contribute to further improvement of the fiscal position. In the field of monetary policy, he was interested in the effect of open market operations on liquidity, on interest rates and yields, and on prices of securities. He welcomed flexibility in the interest rates, as they had historically been maintained at a comparatively low level; they had been influenced largely by the continuous capital inflow, which was based on considerations other than interest rates. The recent change in the pattern of capital inflow, with a reduction in direct private investment and an increase in portfolio investment, had brought a need for greater responsiveness of interest rates to external factors. The emphasis of monetary policy on credits for rural investment seemed well placed.

For the long term, Mr. Madan believed that continuation of a reasonable rate of growth hinged on a strong balance of payments position. The present satisfactory balance of payments position and level of



reserves were linked to a large inflow of foreign capital, which involved an outgo through remittances and repatriation. For some time to come, that might well remain the normal pattern for the Australian economy, although there might be variations in the rate of growth. He hoped that the discoveries of mineral wealth, and a strong increase in exports--especially of nonagricultural products--would provide a base for continued growth of the Australian economy for many years.

Mr. Gomes was impressed with the performance of the Australian authorities in managing the economy. The sustained economic progress over a long sequence of years seemed to be the natural consequence of high standards of economic policy. He congratulated the authorities not only for their skill in Australia, but also for their valuable contribution to a healthy world economy.

As Mr. Gomes saw it, the primary aim of economic policy in Australia was to rapidly increase the economic size of the country both in terms of GNP and of population in order to make the economy of the country more commensurate with its geographic size and the extent of its natural resources. The main economic problem was to accomplish that without creating any fundamental balance of payments problems or distorting the basic national character of the country. The report showed that Australia had been successful in managing its foreign capital policies, its national saving policy, its immigration policy, and its internal investment policy. In fact, the investment ratio of Australia was one of the highest in the world, and a very large part of the resources for financing came from internal sources. Although policy instruments had been adequately managed, small adjustments, like those mentioned in the staff appraisal, were required from time to time in order for an economy to continue to develop properly. The authorities seemed to be making the necessary adjustments, and he believed that their success in the past would continue into the future.

Mr. Suzuki generally agreed with the staff appraisal in the report. He commended the authorities for maintaining an economic environment which had contributed to an impressive growth rate in recent years. If that growth rate were to be maintained, precautionary measures in both the fiscal and monetary fields would be needed to prevent demand from overtaking supply.

The fiscal policy pursued by the authorities seemed to Mr. Suzuki to be a sound one. He welcomed the reduction of the deficit of the Commonwealth budget, although there seemed to be need for a close watch on State and local budgets, because of their expansionary impact on the economy. He also welcomed studies being made on tax structure and the social security system from the viewpoint of avoiding rigidity of the fiscal system. The formula for making grants to the States should be restudied with a view toward securing greater flexibility and cohesiveness in overall fiscal policy.

Concerning monetary policy, Mr. Suzuki believed that making open market sales of government securities to absorb the emerging excess liquidity was correct. However, consideration should be given to modifying existing rules so that the reserve deposit ratio policy could operate more effectively. Australia's basic policy for inducing an inflow of foreign capital and labor seemed to be fruitful. He hoped that the favorable environment for that inflow would be maintained and perhaps improved. Although the report indicated concern over recent changes in the composition of foreign capital inflow, he thought that the basic factor influencing all forms of private capital inflow--the attractiveness of investment opportunity--would continue to be favorable in Australia. Prospects for the future seemed bright, although there might need to be some restructuring of the economy, such as shifting some of the emphasis from agriculture to mining and industry. Such restructuring should be executed in a timely and an orderly manner to avoid both national and international wasted in the allocation of resources.

Mr. Williams observed that in recent years the Australian economy had reached a stage of development where the growth of mining and other nonagricultural sectors had provided a welcome degree of balance to the economy. He thought the authorities deserved congratulations for the way in which the economy was managed. He then made two general observations. First, over the past three years there had been fluctuations in the pattern of personal consumption; in 1967-68, when there had been a drought, consumption had increased. He asked whether that pattern was related to the pattern of immigration, and whether those fluctuations could be expected to continue. Further, he thought that the study planned by the authorities on a system of sales taxes would be timely and useful, regardless of consumption fluctuations.

With reference to interest rates, Mr. Williams detected some enthusiasm of the staff in the report for the release of so-called captive markets. He hoped that the Australian authorities would not completely release those markets. While he did not oppose high interest rates, he felt that at the present stage of the development of Australia, some control should be exercised over interest rates. He then turned to page 24 of Part I of the report, where he thought the view expressed was slightly overconfident. He was concerned about capital flows, because even though there had been a great deal of portfolio investment, there might be an element of speculation therein, given the mining boom. He wondered whether domestic liquidity and capital outflows were not real dangers, and inquired about the opinion of the staff.

Mr. Williams repeated the view expressed at the last consultation discussion (EBM/68/3, 1/15/68) on the useful role Australia could play

as an intermediary for rechanneling funds to other developing countries, and he believed it was a policy that the Australian authorities should consider. In looking over the pattern of aid, he noted that, quite correctly, Australia still concentrated on regional assistance. But Table 48 on page 84 of Part II of the report, showed that exports had increased, particularly to other sterling area countries, and he thought it might be wise for the authorities to attempt to diversify their export markets.

Mr. Horgan was impressed by Australia's tremendous potential for rapid development. The report showed that continued progress in harnessing the country's vast mineral and other resources depended on the maintenance of a high inflow of both people and capital. The policies of the authorities in those matters augured well for the future development of the country. He then referred to the expectation in the report that the authorities' open market operations would make a significant contribution toward reducing excess liquidity in the economy. He believed that scope for increasing sales of government securities at interest yields which, even after recent increases, were low by international standards, was somewhat limited. The fact that the Government had had to make substantial foreign borrowings at high cost in order to finance public expenditures suggested that there was no great flexibility in the internal capital market.

Mr. Horgan referred to a comment in the staff appraisal that the rate of growth in the public sector should be limited to leave room for expansion in the private sector. He pointed out that Supplement 3 of the report indicated that the total outlay in the 1969/70 Commonwealth Government budget had increased 8 per cent over the 1968/69 figure; the latter had increased 6.1 per cent over the 1967/68 one. That increase seemed to be due primarily to increases in social welfare benefits. To that extent, the budget seemed to depart from the recommendations in the staff appraisal, and he inquired how the staff had reacted when that information had been received. Admittedly, the deficit between receipts and outlays of all Commonwealth authorities had decreased substantially in 1968/69--to \$A 344 million, compared with \$A 581 million in 1967/68--and a further substantial reduction was envisaged in 1969/70, when the deficit was expected to be only \$A 3 million. He wondered how realistic that estimate was, considering the increases in expenditure and the fact that the additional revenue was expected to come from normal "buoyancy" without any new taxes or increases in existing rates.

Mr. Horgan referred to the staff's attempt to estimate the effect of the devaluation of sterling on the Australian economy, and thought it was a useful exercise. As the findings seemed to suggest that the effect on Australia had been rather negligible, he inquired whether the benefit to the United Kingdom, so far as Australia was concerned, was also negligible. Further, it was interesting that the Australian

authorities had paid substantial compensation within the country for losses incurred by exporters as a result of the devaluation; that indicated how difficult it was for a country such as Australia to withstand a devaluation of a major currency. In that respect, he was puzzled by the statement in the first paragraph on page 8 of Part I, which stated that some of the statutory marketing authorities were precluded from obtaining forward exchange cover on sales contracts expressed in terms of sterling. It was then stated on page 30 of Part II that compensation was to be paid neither where the increased competition had come primarily from an overseas affiliated company, nor when losses were suffered by exporters who had failed to take out forward cover. Therefore, it appeared that exporters who had failed to take out forward cover were deprived of compensation, even though they had been prevented by the exchange control regulations from taking out that forward cover. He asked the staff to clarify that point.

Mr. Liefertinck fully endorsed the opinion expressed in the staff appraisal on page 21 of the report that while self-equilibrating factors had played an important role in determining Australia's economic performance, that should not detract from the credit due to the timely policy adjustments made by the authorities throughout the 1960's. In his opinion, however, today, there was a high degree of vulnerability in the Australian economy, in particular with respect to the balance of payments, perhaps both in the short run and in the long run. In the short run, if relative price stability could not be maintained internally, then there was some danger that imports would increase and exports decline. Therefore, he believed that the authorities should consider high liquidity one of their most important problems. It might be dealt with by means of a neutral fiscal policy, certainly not an expansionary one; and that policy should be applied to the whole of both public and private sectors, in view of the lack of flexibility in the taxation field. However, there was danger that a reduction of central government expenditures might be overcompensated for by the expansionary policies of the States and municipalities; central control of those non-Commonwealth sectors should therefore be strengthened. In addition, he felt that open market operations in the monetary field, if vigorously pursued and supported by an adequate interest rate policy, could be helpful. They would then affect not only the liquidity of the banks, but also that of other institutions that played an important role in the money market.

Mr. Liefertinck then turned to the comment on page 23 of Part I, that it would be advisable to hold monetary weapons as much as possible in reserve for use in the event of balance of payments difficulties, and that the major avenue for keeping domestic demand within bounds would be a moderation of the growth in public sector expenditure. He hoped that comment was not to be interpreted as meaning that the staff

felt that monetary policy should not become operative when there were no great balance of payments difficulties. He believed, instead, that a balanced use of the fiscal and monetary instruments would bring the best results.

In the longer term, Mr. Liefstinck thought that the economy had the balance of payments would become more vulnerable because they were so heavily dependent on a high level of capital inflow from abroad. The composition of that flow had been changed in recent years by an increase in portfolio investment in relation to direct investment. Portfolio investments could reasonably be expected to remain in the country so long as there was sufficient confidence in the stability of the par value of the currency, and in the prospects for profit. It was remarkable that the capital inflow had been achieved despite capital export restraints which had been imposed by countries like the United States and the United Kingdom; surprisingly, the capital outflow to Australia did not appear to have been greatly affected by those measures. While that inflow was welcome to Australia, he asked the staff what the effect might be on the United Kingdom, in view of its present balance of payments difficulties.

Mr. Liefstinck then turned to the earmarking of internal savings; he felt that the practice should receive reconsideration in view of the vulnerability of the economy. He asked whether savings that were earmarked for construction of buildings would have to be spent for that purpose or else remain uninvested for some time.

Mr. Yaméogo said that from 1960 to 1967 foreign aid provided by Australia had increased every year. In 1960 it had been 0.40 per cent of GNP, and in 1967 it had been 0.70 per cent of GNP. He welcomed that increase, because some other countries had been decreasing their contributions to foreign aid. His only reservation was that on page 95 of Part II it was shown that most of that foreign aid was provided to countries located very near to Australia. He wished that the Australian authorities would make an effort to diversify their aid geographically.

The staff representative turned first to the question whether the new budget was appropriate in present circumstances. At the time of the consultation, the staff had indicated its view on the sort of budget policy that appeared most desirable in the current situation of strongly rising domestic demand; that view had been further elaborated in the appraisal. Subsequently, on receipt of the new budget figures, the staff was pleased to see that the Commonwealth Government had reduced the rate of increase in those expenditures that had an immediate internal effect. It was also glad that the increase in revenue was stronger than it had believed possible, given the fact that this time there had been no rise in major tax rates. As a result, the Commonwealth Government had greatly

reduced the budget deficit. On the other hand, the total level of Commonwealth Government expenditures--excluding expenditures that were transfers to State or other government authorities, and transfers to private persons--was rising at a faster rate in the present fiscal year than in the previous one. On balance, the staff had been somewhat disappointed by the budget, but in appraising the budget it felt that it should be recognized that elections would be held very soon in Australia, the economy was in fact in excellent condition, reserves had increased in the past fiscal year, economic growth was more rapid than it had been previously, and the overall outlook for the future was very promising. Under those circumstances, a decisively contractionary budget could hardly have been expected.

The staff representative referred to Mr. Huntrods' question on the results of the cash and conversion loan in July. It was true that the net amount raised was less for the July loan of 1969 than it had been for the 1968 July loan. However, very sizable sums had been successfully converted in July 1969, and in that sense the results of the loan were more encouraging than, for example, the result of the one in May 1969. In May, an increase in interest rates was expected by Australian investors, and so conversions were much less than had been hoped. In addition, although in the case of the July loan the amount of new money raised was less than in the preceding year, the needs of the Commonwealth Government were also less than in 1968 because the deficit was so much smaller. Upon consideration of all facets of the July 1969 effort, it might be said that in some sense it was successful.

Concerning Mr. Horgan's question whether the expectation of a very small budget deficit was realistic in the present circumstances, the staff representative replied that experience had proven that the Australian authorities had, in the past, successfully estimated budget revenue very accurately. The staff had no reason to believe that the revenue forecast in the new budget--which was the main reason for the reduced deficit--was overoptimistic and would not be realized. It was, of course, based partly on the expectation of another year of good growth of the economy as a whole, and of continued increases in incomes. In the preceding year revenue had, in fact, been greater than had been forecast.

The staff representative turned to Mr. Lieftinck's observation on that part of the staff appraisal that said that it would be advisable to hold monetary weapons as much as possible in reserve for use in the unforeseen event of balance of payment difficulties. The staff confirmed Mr. Lieftinck's view that this should not be read as meaning that monetary weapons should be used only when there were balance of payments difficulties. Some emphasis was intended to be placed on the words "as much as possible." What was possible would be determined by the current domestic situation.

Concerning Miss Fuenfgelt's question whether there was any indication that the Australian Government was contemplating a change in its traditionally liberal attitude in regard to capital imports, the staff representative said that there were no such indications. It was obvious, of course, that the very large inflows to Australia in the last few years had made control over the resources of the economy a subject of political discussion. But there had not been any change in the Government's attitude, despite certain unfortunate statements that might have appeared in the press. Concerning Mr. Williams' question whether there had been any indication of the proportion of the capital inflow which had been speculative, he replied that a large part of the inflow had been in the form of portfolio investment, but it was hard to say to what extent that might be called speculative. He then referred to Mr. Liefertinck's request--also concerning capital import--for more information on the impact of restrictive measures taken by other countries to restrain their capital outflows. Table 54 on page 97 of Part II showed that "other direct investments" by the United Kingdom had been falling in the past few years, whereas the investment from "undistributed income" from the United Kingdom had increased. Further, portfolio investment coming from the United Kingdom had risen substantially, in particular during 1967/68.

The staff representative then mentioned Mr. Madan's interesting question concerning the relative prospects of sheep raising against wheat farming. In reply, he said that the Australian authorities felt that prospects for wool were presently stronger than those for wheat. They had in fact introduced a degree of restriction on the planting of wheat in the current season.

The staff representative turned to Mr. Horgan's question concerning the statement made on page 8 of Part I that losses by some statutory marketing authorities had been incurred because those authorities had been precluded from obtaining forward cover. The statement on page 30 of Part II did not refer to statutory marketing authorities but instead referred to private exporters who could have obtained forward exchange cover; they were therefore not compensated for losses they had incurred because of the devaluation.

The staff representative referred to Mr. Liefertinck's question concerning the earmarking of savings, and replied that there was no formal earmarking procedure. A similar result was achieved by a different procedure; it might be said that certain domestic private savings in Australia would have to be used for a specific purpose, such as construction, in the sense that certain financial institutions that were under official control had been strongly directed to use part of their resources in a specific sector, such as building.

Finally, the staff representative confirmed that Mr. Williams was right in his opinion that the pattern of consumption in Australia

had been closely related to immigration over a number of years. The high level of immigration had helped to increase personal savings because immigrants were, by nature, inclined to place a high priority on saving for their future.

Mr. Stone observed that the time and thought which had been devoted by the Executive Directors to discussing the Australian economy at such a busy time had been a tribute to the country. He then added some information to that which the staff representative had given. He first took up the point raised by a number of Executive Directors concerning the authorities' statement, referred to on page 14 of Part I about the strong line the Government was expected to take against large increases in grants to local and State authorities at the Premiers' Conference and Loan Council Meeting in June. Table 8 on page 14 of Supplement 3, showing the actual outcome of the meeting, made clear that there had been increases in Commonwealth payments to State and local authorities. He pointed out, as a technical observation, that the very large increase in those payments consisted of a large number of different elements, many of which had not been determined at the Premiers' Conference and Loan Council. For example, those meetings did not determine the level of general revenue grants; those were the result of past decisions of various kinds, and related to purposes such as the running costs of universities. Specific capital payments were handled in the same way, and generally related to such projects as universities and roads. Upon consideration of all the details, the outcome of those meetings was not perhaps very different from what had been expected by the Commonwealth authorities at the time of the consultation.

Mr. Stone then referred to the comment that it appeared that the recommendations contained in the staff appraisal concerning the then forthcoming budget had not been fully followed when the budget was completed. He pointed out that at the time that the budget was being prepared, the recommendations in the appraisal had not yet been available. He did not intend to suggest that if the report had been available to the authorities their decisions would necessarily have been different, but he supposed that there was at least that possibility.

Concerning Mr. Huntrods' remark that imports in 1969/70 might be higher than had been forecast, Mr. Stone agreed that the July 1969 figures had in fact shown a sharp rise. However, special factors had affected the import level in that month; imports of defense material and several similar other items had been very high. It was quite possible that imports might be higher than had been estimated for the year, but one very important point should not be overlooked; utilization of Australian domestic petroleum production would assume significance during the year, and that should have a tendency to reduce imports.



On the matter of capital inflows, Mr. Stone was inclined to agree with many of the comments which Executive Directors had made. It was true that capital inflow was always uncertain, and the conditions in capital markets of the world suggested that it would be prudent to allow for a reduction in capital inflows during 1969/70. If that occurred, it could have a direct effect on capital expenditure, and would tend to modify the influences adding to monetary liquidity. For many years now, people in Australia had strongly questioned the wisdom of the authorities' policy of "relying" on inflows of capital. However, over a period of time, the course of events had proven that the authorities' policy was fully justified. It was possible, of course, that at some time Australia might be faced with problems in the field of the capital account; when a country had a large current account deficit, and a large capital inflow, there was always a possibility of those problems. However, those were only some of the many problems with which the authorities were contending in their efforts to achieve maximum growth of their economy while attaining their other objectives of reasonable price stability and full employment. The authorities were far from being overconfident or complacent. They would have to deal with these problems if and when they arose.

Mr. Stone turned to Miss Fuenfgelt's observation that price increases of 3 per cent per annum were above what she thought would constitute a completely satisfactory performance, and he entirely shared her view. He hoped that the Australian authorities would manage to restrain price increases, but he could not give complete assurance on that point. He also agreed with Mr. Madan's comment that the Australian economy might, and Mr. Stone stressed the word "might," have to reckon with a degree of overheating in the future. Mr. Stone believed that was largely the view of the authorities, and if the overheating did occur, he hoped and trusted that appropriate measures would be taken to deal with the situation. Mr. Stone turned to Miss Fuenfgelt's comment that further tightening of the labor market could only be avoided if immigration could be maintained at least at its present high level, and said that the level of net immigration in 1968/69 had been at its highest since 1951, which had been the time of the peak of the postwar immigration. It was his understanding that in 1969/70 the previous year's level would be maintained, if not exceeded. However, he pointed out that a large inflow of immigrants added not only to the labor supply, but also to the demand upon the resources in the economy, including housing, schools, hospitals, roads, and various other facilities.

In respect of the earmarking of savings in Australia, he agreed with the staff representative's comments that there was no formal earmarking, but that the institutional structure resulted in an arrangement closely related to earmarking. However, there was some difference; for a country which set maintenance of a large immigration program as

one of its objectives, it was important to maintain an appropriate level of social infrastructure, in order to attract--certainly not to repel--prospective immigrants who might be considering a move to Australia. Under those circumstances, some degree of designating capital to ensure that those basic facilities would be made available was almost unavoidable.

Concerning the Australian external aid program, Mr. Stone said that the concentration of the program in the region near Australia, particularly in the Territory of Papua and New Guinea, had been a subject of much discussion in Australia. He believed that the policy was absolutely appropriate; Papua and New Guinea were very close to Australia, and what was more important, Australia stood in a position of trust to them under the United Nations, originally under the League of Nations.

Mr. Stone turned to Mr. Horgan's comment that since the Australian authorities had to borrow from abroad to finance the budget, there seemed little possibility of open market operations in the normal sense. The view of the authorities was that they would borrow as much as possible from the local capital market, and obtain the balance from abroad; in that sense Mr. Horgan was correct. But, if the amount which could be borrowed by issuing long-term securities to the nonbank public were greater than that required to finance the deficit, so much the better. That course would still be taken in order to exercise a measure of control over liquidity. Thus, he believed that open market operations were not only possible, but were considered by the authorities as an important part of monetary policy. Mr. Horgan had also mentioned that since the effect of the devaluation of sterling seemed to have been rather negligible in Australia, perhaps the benefits to the United Kingdom, so far as the Australian market was concerned, might also have been negligible. The Reserve Bank had commented on that matter in its annual report, by saying that the downward trend in the proportion of imports from the United Kingdom had continued despite the devaluation of sterling, but that Japan had made strong gains in the Australian market. He believed it did not necessarily follow that the devaluation of sterling had not provided benefits to the United Kingdom in the Australian market, because the United Kingdom's share of the Australian market might have been much less without the devaluation.

Mr. Stone referred to Mr. Lieftinck's comment that the stability of capital already in Australia depended to a large degree on confidence in the par value of the Australian dollar and also on the prospects of profits of Australian companies. He thought it was unnecessary to comment on the Australian dollar, but he stated that Australian companies had tended to be sufficiently profitable in the past to attract investment, and he saw no reason why that should not continue. Indeed, price to earnings ratios, and other indications of profitable investment opportunities, appeared more favorable in Australia than in most other major capital markets in the world today.

As there were no further comments, the discussion on the 1969 Article VIII consultation with Australia was concluded.

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Directors without meeting in the period between EBM/69/81 (8/13/69) and EBM/69/82 (9/3/69).

5. PERU - CONSULTATION UNDER STAND-BY ARRANGEMENT

Peru has consulted the Fund pursuant to paragraph 6 of the stand-by arrangement for Peru (EBS/68/240, Sup. 2, 11/8/68). No additional understandings are found to be necessary for further purchases under the stand-by arrangement (EBS/69/218, 8/13/69).

Decision No. 2827-(69/82), adopted  
August 15, 1969

6. HAITI - VOLUNTARY REPURCHASE

The Fund accepts the offer of Haiti to repurchase Haitian gourdes equivalent to \$87,500 by paying Mexican pesos equivalent to that amount (EBS/69/231, 8/22/69).

Decision No. 2828-(69/82), adopted  
August 25, 1969

7. CONFERENCE ON A WORLD TRADE MODEL - FUND REPRESENTATION

The Executive Board approves Fund representation at the first annual conference on constructing a world trade and payments model by linking existing national economic models, as set forth in EBAP/69/149 (8/11/69).

Adopted August 14, 1969

8. ANNUAL MEETING - REPRESENTATION EXPENSES OF EXECUTIVE DIRECTORS AND ALTERNATES

The Executive Board approves the report of the Committee on Executive Board Administrative Matters on the rules for the reimbursement of representation expenses of Executive Directors

and Alternates at the time of the 1969 Annual Meetings, as set forth in EBAP/69/146 (8/8/69).

Adopted August 13, 1969

9. STAFF ASSIGNMENTS IN MEMBER COUNTRIES

The arrangements relating to staff assignments in member countries set forth in EBAP/69/150 (8/11/69) are approved.

Adopted August 14, 1969

10. EXECUTIVE BOARD TRAVEL

Travel by an Executive Director as set forth in EBAP/69/136, Sup. 1 (8/12/69) is approved.

APPROVED BY THE EXECUTIVE BOARD:  
Meeting 69/100, October 24, 1969

PIERRE-PAUL SCHWEITZER  
Chairman

ROGER V. ANDERSON  
Acting Secretary