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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 82/143

3:00 p.m., November 5, 1982

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

Executive Directors	Alternate Executive Directors
	M. K. Diallo, Temporary
J. Anson	C. Taylor
J. de Groote	
	A. Le Lorier
A. Donoso	
R. D. Erb	C. Dallara
	T. Alhaimus
	V. Supinit
T. Hirao	T. Yamashita
	M. Casey
A. Kafka	
G. Laske	G. Grosche
G. Lovato	C. P. Caranicas
	A. S. Jayawardena
	J. E. Suraisry
	T. de Vries
A. R. G. Prowse	
G. Salehkhou	O. Kabbaj
	J. A. K. Munthali, Temporary
	E. Portas, Temporary
	L. Vidvei
	Jiang H., Temporary

L. Van Houtven, Secretary
J. A. Kay, Assistant

Also Present

European Department: L. A. Whittome, Counsellor and Director; B. Rose, Deputy Director; P. de Fontenay, U. Dell'Anno, A. Knobl, L. J. Lipschitz, S. M. Thakur, P. van den Boogaerde, H. Vittas. Exchange and Trade Relations Department: S. Mookerjee, Deputy Director; L. L. Perez. External Relations Department: G. P. Newman. Legal Department: G. P. Nicoletopoulos, Director; J. G. Evans, Jr., Deputy General Counsel; A. O. Liuksila. Research Department: C. F. Schwartz, Associate Director and Director of Adjustment Studies; K.-Y. Chu, N. M. Kaibni, G. Khatchadourian, L. Schmitz. Treasurer's Department: W. O. Habermeier, Counsellor and Treasurer; W. L. Coats, D. S. Cutler, Q. M. Hafiz, M. Sami, G. Wittich. Personal Assistant to the Managing Director: N. Carter. Advisors to Executive Directors: S. R. Abiad, S. El-Khouri, M. A. Janjua, P. Kohnert, H.-S. Lee, P. D. Péroz. Assistants to Executive Directors: E. M. Ainley, L. Barbone, L. E. J. Coene, T. A. Connors, G. Ercel, I. Fridriksson, M. J. Kooymans, V. K. S. Nair, J. R. Novaes de Almeida, Y. Okubo, G. W. K. Pickering, D. V. Pritchett, M. Z. M. Qureshi, J. Reddy, C. A. Salinas, J. Schuijer, D. I. S. Shaw, H. Suzuki, A. Yasseri.

1. AUSTRALIA - PURCHASE TRANSACTION - BUFFER STOCK FINANCING FACILITY - SPECIAL STOCKS UNDER INTERNATIONAL SUGAR AGREEMENT

The Executive Directors considered a request from Australia for a purchase equivalent to SDR 32.463 million under the buffer stock financing facility (EBS/82/183, 10/8/82; and Supplement 1, 11/4/82).

Mr. Prowse made the following statement:

Australia has requested a purchase of SDR 32.463 million in connection with its obligation to accumulate special stock of sugar under the International Sugar Agreement. Australia previously made a purchase under the buffer stock financing facility to finance obligatory sugar stock accumulations in 1979.

The proposed purchase is, in amount and form, typical of purchases under this special facility, which is designed to assist and encourage primary producers to participate in buffer stock arrangements (and to accept related constraints on their exports), which are seen as beneficial to the industry as a whole through reducing volatility in prices and supplies to the market. In the present depressed and uncertain markets for primary exports--including, of course, sugar--it is more important than ever that this special facility should operate effectively, be seen to operate effectively, and be available to producers as they need it and as they meet its requirements.

The buffer stock financing facility is a highly specialized facility with restrictive special conditions on eligibility. It is evident from EBS/82/183 that the Australian request meets the special conditions for eligibility under the buffer stock financing facility.

Apart from the special conditions of the buffer stock financing facility itself, purchases under the facility must, of course, be consistent with the Fund's general policies and requirements. These requirements include that of balance of payments "need." In view, inter alia, of the unusual formulation that the staff has used in its paper to assist the assessment of "need" in this case, it might be helpful, perhaps even necessary, to comment--even if only briefly--on the concept of need and its application under the buffer stock financing facility and also on the facts of the present case.

The concept has been much discussed, defined, and redefined over the years, both generally and specifically in relation to the buffer stock financing facility. Both in the broad and in the particular, it was intensively considered by the Executive Board in the later part of the 1970s; important relevant papers are SM/76/197 and SM/76/197, Supplement 1.

The staff, in EBS/82/183, make the following statement, which is something of a summary of comment on page 9 of SM/76/197: "Judgments about what constitutes a weak reserve position in this context are made on a case-by-case basis, taking into account a wide variety of factors, including, inter alia, the volume of foreign trade (variability of exports and imports), past behavior of reserves (size of gross and net reserves), prospective developments (in them), the traditional level of reserves, and seasonal factors (and the size of short-term foreign liabilities)." I note that I have added the words in parentheses on the basis of the statement in the original documents, because I think they are also important elements in any assessment, including in the present case.

It would no doubt be tedious for the Board for me to explore in detail, on this occasion in relation to this relatively small purchase, the whole history of this matter of "need," but I do want to make a few other brief references to the important basic papers noted above. Thus (in discussing another special facility, the compensatory financing facility) SM/76/197 says: "The balance of payments is a flow concept that does not refer to a moment in time, and no basis exists in the decision on compensatory financing for fixing either the length of the period of balance of payments need or the date of its termination in relation to the time of the drawing." Moreover, it is evident from that paper and others that, subject to certain exceptions, the Fund's policies may make distinctions on the basis of the character or origin of need for the purposes of establishing special facilities, such as the oil facility, the compensatory financing facility, and, I think it may be added, the buffer stock financing facility.

The requirement of need is generally seen in the Fund's deliberations as having three separate aspects, each of which is to be appraised separately and any one of which can justify the balance of payments "need" requirement, as indicated by the use of the conjunction "or" in the Articles. That is, need may be "assessed on the basis of the member's balance of payments position, or its reserve position, or developments in its reserves."

Since emphasis has been placed by the staff on the question of balance of payments deficit in determining the existence of "need," a subject for consideration, one that is still controversial and evolving, is how payments deficits are to be measured. As SM/76/197 has it: "The concept of payments deficit that is most relevant in evaluating need is undoubtedly the one covering net autonomous transactions, i.e., transactions undertaken for their own sake, for which the central authorities have provided the financing, either by drawing on their reserves, by engaging in official borrowing, or by deliberately inducing other residents to borrow. That is, the items below the line that reflect

the financing of the imbalance will comprise official reserve assets and the liabilities that qualify as official financing...." The purposes and effects of official balance of payments financing are to maintain reserves at a level higher than they would otherwise be, or to maintain an exchange rate higher than it would otherwise be, or a combination of both. These purposes serve to distinguish balance of payments financing from the other major category of capital transactions, those associated with capital formation, and the paper notes: "Borrowing that takes the place of the use of reserves clearly does not belong above the line as a factor contributing to a payments surplus or to the reduction of the deficit that would have existed in the absence of the borrowing." In Australia, it is to be noted that the Government has undertaken substantial overseas borrowing to maintain its reserves, and additionally has encouraged semigovernmental bodies to seek financing abroad where they otherwise have sought it domestically. Further, the painfully high level of interest rates in Australia has served to attract substantial inflows of capital that may well be extremely sensitive to interest rate differentials.

The matter of "need" specifically in relation to purchases under the buffer stock financing facility was discussed in 1973 when a proposal before the Executive Board was that the criterion should not apply to this special facility. This was not generally accepted, but there was some support for the suggestion of the staff that the requirement should be interpreted more flexibly in this context, and that view is further recorded in 1975.

Again, the Report of the Executive Directors on the Proposed Second Amendment comments as follows: "Under the concept of need in Article V, Section 3(b)(ii), a member will be able to purchase the currency of other members of the Fund if its balance of payments position or its reserve position is unfavorable or if there is an unfavorable development in its reserves,...even though it does not have a deficit on its balance of payments according to accepted definitions of the balance of payments." It was recognized that one important consequence of the separateness of the aspects of "need" is that the requirement does not bar a member with adequate or even high reserves from using either Fund resources or SDRs. In the papers referred to above, it is suggested that a clear-cut recent instance of this principle is that participants in the European common margins arrangement, some of them with high reserves, routinely draw on the Fund and use SDRs for the settlement of deficits in connection with intervention. Finally, as SM/76/197, Supplement 1 states: "As determination of need almost always entails a judgmental element, a judgment about the need of a member to draw because of its reserve position might be influenced somewhat by the country's balance of payments experience and prospects. A certain use might thus be considered justifiable on the basis of reserves that were on the low side,

though not extremely low, in conjunction with a payments position that was not particularly strong, though perhaps not clearly in deficit.

Balance of payments need in Australia

Against this background, what is the position in the present case? As the staff paper notes, "The interpretation of recent developments in, and the short-term outlook for, Australia's balance of payments and reserves position is not entirely straightforward." Appraisal is difficult because the present situation in respect of Australia's balance of payments is not only uncertain but also largely unprecedented. The current account deficit is, for Australia, extraordinarily high, at about 6.2 per cent of GDP. It is expecially important in these circumstances to look beyond month-to-month movements in the reserves and payments position and to look at the "fundamentals." Some relevant points are:

- It is not conclusive to assess Australia's (or indeed any other country's balance of payments "need" simply on the basis of three months', or, in effect, one months' movement in reserves. The growth in Australia's reserves in September was attributable essentially to unexpected capital inflows (unexpected in terms of the established adverse seasonal pattern), and this disguised the underlying balance of payments position.

- There was a positive swing of $A 1.45 billion in the September 1982 balance of payments outcome as compared with September 1981, but some $A 1.39 billion of this was attributable to the capital account.

- A considerable portion of this increased capital inflow appears to have comprised short-term flows prompted by favorable interest rate differentials between Australia and other developed countries, notably the United States and Japan. On November 3, the yield on Australian Government 26-week Treasury Notes was 15.2 per cent. The influences underlying these recent flows seem basically "financial," and these influences and the direction of the flows they induce could change quickly, possibly stimulating an outflow of similar magnitude. In particular, the strong capital inflow of recent months seems not to be the result of any increasing demand for investment in industry in Australia, or to any recovery in commodity markets or mineral prices, or any pickup in the demand for capital to invest in resource development in Australia. In that respect, there has been no improvement in basic economic conditions, such as might be expected to reflect in longer-term balance of payments prospects.

- Australia's current account deficit, as a percentage of GDP has expanded from 2 per cent in 1979/80 to about 6.2 per cent in 1981/82: its highest level for 30 years. A similar figure is expected for 1982/83.

- The 1981/82 deficit as a percentage of GDP (6.2 per cent) is 2.5 times the arithmetic average for the past 25 years as a whole.

- Underlying this weak current account position has been an adverse and widening inflation differential between Australia and its trading partners. Over the year to the September quarter, Australia's consumer price index rose by 12.3 per cent, compared with weighted average increases of 6.5 per cent in its major OECD trading partners (United States, West Germany, Japan, United Kingdom, France, Canada, Italy, and New Zealand) and 7.8 per cent in all OECD countries over the year to August.

- In Australia, average weekly earnings rose by 15.2 per cent over the year to the June quarter, considerably above the rates being recorded in many other developed countries (e.g., 5.3 per cent in the United States, 3.5 per cent in Japan, 2.5 per cent in Germany, and 7.8 per cent in the United Kingdom). The longer-term balance of payments outlook reflects this basic economic problem of deteriorating competitiveness in Australian industry. Correcting this will take time. Indexes purporting to measure international competitiveness on the basis of unit wage costs suggest a decline of about 13 per cent over the two financial years 1980/81 and 1981/82.

- The outlook for the Australian balance of payments in the period ahead has been further damaged by the current severe drought. Crop production is expected to be down 28 per cent in 1982/83. Taking into account depressed overseas market conditions, and rising costs, the net value of rural production is expected to be down 44 per cent in current prices in 1982/83, and in real terms by 49 per cent.

- Foreign exchange reserves currently represent 2.5 months' imports of goods and services. This is much lower than throughout the 1960s and most of the 1970s, and, given Australia's position as an exporter of primary commodities to volatile markets, leaves no margin for safety. The following table illustrates the position:

Foreign Exchange to Imports (Australia)

Months of Imports

1961-65	6.0	1976-80	1.9
1966-70	3.9	1981-82	1.7
1971-75	7.5	1982 Sept.	2.5

- Clearly the ratio has been deteriorating. It has picked up to about 2.5 months recently. But the ratio needs to be considerably increased. Australia has survived in recent years with an even lower ratio of reserves to imports through approaches to the BIS for cover, by drawing on its IMF reserve tranche, by substantial compensatory overseas borrowing, and so on. But it is clear that there is a need for a more comfortable level of foreign exchange than 2.5 months' imports represents.

- Nor does it seem that this level has been regarded by the Board in other cases as an indication of reserve ease. For recent drawings under the buffer stock financing facility, the average has been about 1.9 months. Rather similar results are obtained for recent drawings under the compensatory financing facility. The average level of reserves has again averaged out at 1.9 months of imports, with some countries drawing with reserves (not limited to foreign exchange) as high as four and six months' imports. Australia supported those drawings, as did the Board, and the reference here is only to illustrate the point.

The exchange value of the Australian dollar

- The Australian dollar has depreciated substantially over the past 15 months, by about 11 per cent in terms of the trade-weighted index and 17 per cent against the U.S. dollar. Over the latest four months, these depreciations have been 4.8 per cent and 8.1 per cent, respectively. Such depreciations do not suggest that the Australian authorities have been satisfied with the balance of payments position. Indeed, they are symptomatic of the underlying weakness in the fundamentals.

Government borrowing overseas

- The Australian Government has been borrowing overseas to support the balance of payments. Recent borrowings have been a £100 million loan and a ¥ 20 billion loan in July, a US$400 million loan in September, and ¥ 15.5 billion and DM 200 million loans in October. These amount to about $A 800 million. Importantly, if government borrowing is excluded, net monetary movements in September increased by $A 555 million, but did not fully offset the losses in July and August, $A 704 million. This is, of course, relevant to the staff comment about September offsetting July and August results.

It is evident that the Australian authorities are concerned at the balance of payments situation. The preceding considerations suggest that if the Australian authorities had done nothing they would have a clear-cut balance of payments need of major dimensions. But because Australia has been moving its exchange rate down and undertaking large-scale government borrowings overseas and maintaining its interest rates at painfully high levels, it cannot be deemed in any common sense of the words not to have a balance of payments need.

For the information of Directors I have prepared three tables (see Annex):

(1) Australia: Official Reserve Assets and Imports
(2) Australia: Current Account of the Balance of Payments as a Percentage of GDP
(3) Australia: Australian Dollar Exchange Rates

I commend to the Executive Board the proposed purchase by Australia under the buffer stock financing facility.

The Director of the European Department made the following statement:

Page 8 of EBS/82/183 (10/8/82) contains the following passage: "Developments in the first two months (July-August) of 1982/83 provide evidence of a payments deficit being substantiated by a significant loss of reserves. In order to bolster reserves, the authorities have arranged substantial foreign borrowings. The staff believes that the proposed purchase will be justified by a balance of payments need if, at the time of Board consideration of the request, the deficit incurred during July-August has not subsequently been reversed."

The latest figures on the balance of payments position are as follows. Information received from the Australian authorities shows that in September 1982 there was an overall surplus on the balance of payments of SDR 861 million, made up of a current account deficit of SDR 633 million and a net apparent capital inflow of SDR 1,494 million. For the third quarter as a whole, there was an overall balance of payments surplus of SDR 340 million, made up of a current account deficit of SDR 1,900 million and a net apparent capital inflow, including overseas borrowing by the Australian Government, of SDR 2,240 million. Thus, the overall deficit incurred during July and August has subsequently been reversed.

The Australian authorities have pointed out, however, that the Government has recently been borrowing substantial amounts overseas to support the balance of payments. The Government borrowed SDR 61 million (net) in July-August, and the overall payments deficit, excluding this borrowing, amounted to SDR 603 million. In September, the Government borrowed SDR 324 million (net), and the overall surplus, excluding this borrowing, was SDR 537 million. For the quarter as a whole, there was an overall deficit of SDR 66 million, excluding official borrowing.

While complete balance of payments data are not available for October, the Australian authorities have also informed the staff that, on the basis of preliminary and tentative data, the current account deficit in that month was over SDR 600 million, or about the same as the monthly average in the third calendar quarter of 1982. In October, government borrowing contributed about SDR 175 million to gross reserves, while private sector foreign exchange transactions led to an increase of about SDR 265 million, reflecting private capital inflows in the first half of the month.

From this updating of the passage quoted in the first paragraph above, it is not clear whether the test of balance of payments need has or has not been met.

Extending his remarks, the Director of the European Department made the following additional statement:

The statement on page 8 of the staff paper--that the proposed purchase would be justified by a balance of payments need if, at the time of Board consideration of the request, the deficit incurred during July/August has not subsequently been reversed--should however not be taken to imply that we should base our judgments solely on the Australian balance of payments and reserve position in September, or indeed, in any other very short period. Rather, as I think the text on pages 2 and 4 of the staff paper makes plain--and indeed the same note is reflected in the staff appraisal--the staff thinks that the question of Australia's need has to be considered from a number of angles.

In this connection, we have again taken a careful look at the Board discussion that took place on the subject of need in 1976. I referred to that discussion at the Board meeting on Wednesday, and I want to repeat what I said then, namely, that in my personal view it is fair to summarize that discussion by saying that Executive Directors resisted suggestions for a

codification of practices or principles in connection with the question of balance of payments need. They also stressed that there were factors other than the three aspects commonly referred to--the overall balance of payments position, the reserve position, and the developments in reserves--that should be taken into account. My own view is that against this background we should have regard in the present case, first, to the fact that Australia has, and expects to continue to have, a substantial current account deficit of nearly SDR 9 billion in 1981/82 and over SDR 9 billion prospectively in 1982/83, in each year equivalent to about 6 per cent of GDP, and far above the figures that prevailed in the two previous decades; second, to the fact that the Australian authorities have permitted a substantial depreciation of the exchange rate in effective trade-weighted terms; and third, to the fact that the Australian authorities have felt a need to bolster reserves by arranging substantial overseas loans. These last two facts indicate that Australian policy actions are most evidently based on a perception by the authorities of a balance of payments need.

There is the separate but associated question whether Australian reserves are low. This is a particularly difficult matter of judgment. At the end of September--the latest date for which we have firm figures--reserves, with gold valued according to Australian practice (i.e., at 100 per cent of the average monthly price in London) were equal to about four months' imports. With gold valued at SDR 35 per ounce--as it is also in IFS--the figure is less than three-months' imports. As was noted in EBS/82/183, Australia is a primary commodity exporter and therefore subject to large swings in the terms of trade. In addition, Mr. Prowse has developed the case that reserves are low by historical standards.

Taking all these factors into account, my overall judgment would be that, while the case is by no means clear-cut, the requirement of need is satisfied in this case, especially if we act on the principle that, in such matters, the members should be given the benefit of the doubt.

Mr. Hirao said that it seemed clear that the request by the Australian authorities for a purchase of some SDR 32 million under the 1977 International Sugar Agreement would be consistent with the requirements of the buffer stock financing facility. Australia had accumulated its special stocks of sugar by the end of June 1982, and they were valued in accordance with the relevant decision and procedures.

On the question of Australia's need to use the Fund's resources because of the balance of payments or reserve position, Mr. Hirao went on, it was worth noting that there had been large swings in Australia's external transactions. Indeed, a large swing of that sort had once again

been witnessed in the most recent quarter. During July and August 1982, Australia's gross international reserves had shown a decline of about SDR 515 million, and there had been an overall payments deficit of SDR 603 million, excluding government borrowings of SDR 61 million. Gross international reserves had increased substantially during September, due mainly to unexpected capital inflows, largely accounted for by the favorable interest rate differentials between Australia and other countries. They were therefore likely to be subject to quick reversal. In addition, the Government had borrowed some SDR 324 million for deficit financing. Executive Directors would recall that SM/76/197 (page 6), on the requirement of need, had said, inter alia, that "borrowing that takes the place of the use of reserves clearly does not belong above the line as a factor contributing to a payments surplus or to the reduction of the deficit that would have existed in the absence of the borrowing." There was therefore a strong case for excluding government sector borrowing, above the line. On that basis, the third quarter as a whole had been in overall deficit in the amount of SDR 66 million.

Furthermore, as SM/76/197 also stated, it could be argued that while the indirect balance of payments effect on monetary policy and other relevant actions of the authorities could not be quantified, there were cases in which an inducement offered by the authorities seemed the most reasonable explanation for a certain capital inflow, in which circumstances the borrowing undoubtedly belonged below the line in measuring the payments balance, Mr. Hirao went on. In any event, Australia's current account had been running sizable deficits in the past two years, and it was again expected to record a deficit of over SDR 9 billion for the current fiscal year, equal to 6 per cent of gross domestic product. He could therefore support the proposed decision.

Mr. de Vries commented that the difficulty of the case was made evident by the presentation of two separate statements by the staff, and it was clearly difficult to come to any hard-and-fast conclusions. Naturally, he fully agreed with Mr. Prowse that the buffer stock facility should operate effectively, and that Australia had met the conditions for eligibility under the facility. For him personally the difficulty lay in deciding whether the general requirement of need had been met. The purpose of the requirement of need, he recalled, was to ensure that access to the Fund's resources was limited to situations in which the Fund could be of the most help. In addition, the Fund's liquidity was at present tight, and there was therefore a special need to conserve resources for those cases in which Fund assistance was really needed. Second, with the rise in the Fund's lending activities, its actions had become subject to scrutiny by outsiders and the press; it was therefore particularly important to adhere to the Articles when carrying out the Fund's role. Article V, Section 3(b)(ii) of the Articles of Agreement read in part: "The member represents that it has a need to make the purchase because of its balance of payments or its reserve position or developments in its reserves." He took that provision to mean that there were three separate elements, each of which--balance of payments position, reserve position, and developments in reserves--would suffice to establish the requirement

of need. Developments in reserves applied almost exclusively either to reserve centers or to members with currency arrangements that might have to repurchase balances in their own currencies under those arrangements. That provision therefore did not apply to Australia.

As to Australia's reserve position, Mr. de Vries noted that Australia's reserves had more than doubled in the twelve months ended September 1982, from SDR 1,700 million to about SDR 4,500 million. Related to purchases from abroad, Australia's reserves had risen from 1.7 months of imports in 1981/82 to 2.5 months of imports in September 1982. Furthermore, Mr. Prowse's figures had shown a strongly rising trend in reserves from a low point in 1979/80 to September 1981. His conclusion was that the movement in Australia's reserves did not establish a requirement of need. On the other hand, the rise in those reserves did not mean that the requirement of need could not be established under any of the other criteria.

The remaining criterion, Mr. de Vries went on, was that of the balance of payments position. Australia certainly had a large and perhaps even unsustainable current account deficit, amounting to 6 per cent of gross domestic product. Even if the official borrowing were discounted, private capital inflows had been more or less sufficient to offset the current account deficit. Therefore, it might well be that Australia faced a need for adjustment without having a balance of payments need.

The only remaining question was the nature of the private capital inflows that had financed the current account deficit, Mr. de Vries considered. They might certainly have been induced by policy measures that the Australian authorities had taken for that purpose, thus also establishing a payments need; but that did not seem to have happened. His feeling was that the Australian authorities had been surprised by the capital inflows and were not quite aware of how they had come about. Mr. Prowse, for instance, had said that the increase in capital flows appeared to have comprised short-term capital flows prompted by interest rate differentials, while the longer-term inflows of recent months seemed not to have been the result of any increase in demand for investment in industry. His conclusion was that the staff, in writing its paper, had not been clear whether the test of balance of payments need had or had not been met.

His own conclusion, Mr. de Vries went on, was that there existed too much doubt to conclude that the requirement of need had in fact been met.

It was essential, Mr. de Vries observed, to apply uniform treatment to all members without sacrificing the Fund's principles or setting precedents. In the present circumstances, there were three possible lines of action. First, the Fund could defer the present request to see whether a payments need developed with more clarity in the immediate future; it would be interesting to know how long the request could be delayed without depriving the Australian authorities of the possibility of applying for

such a drawing. Second, Executive Directors could ask the staff to investigate more closely the capital inflows of the past few months so as to reach a clearer understanding of whether there was a payments need. For instance, had most of the fixed capital flows been compensatory, or had they been autonomous? Another possibility might be to approve the present request, with the proviso that as soon as the staff had determined that the requirement of need had been met in a satisfactory fashion, the amount would be made available without further action by the Executive Board. Third, the Executive Board might approve the request by the Australian authorities, while asking them to represent to the Fund that, if subsequent data showed that the requirement of need had not been met, they would make a prompt repurchase. While his authorities did not particularly like that technique when applied to drawings under the compensatory financing facility, in the present instance it might provide a solution.

The fact that the amount was small, Mr. de Vries went on, was of no great assistance because the Fund would not wish to compromise its principles even for a small amount. Certainly, the Australian economy would not suffer greatly if the authorities' request was not met. He had difficulty with the request because it seemed to set an unfortunate precedent; he had outlined some ways in which he hoped to meet the Australian authorities' desires without compromising the principles of the Fund.

Miss Le Lorier commented that the staff had clearly shown that the requested drawing did comply with all the criteria set forth in Decision No. 5597-(77/171), adopted December 16, 1977. She would therefore concentrate on an assessment of Australia's balance of payments need in relation to a drawing under the buffer stock financing facility. The purpose of a buffer stock was to try to prevent problems from emerging in a country's balance of payments position; its effects were indirect and prospective, and they were beneficial not only to producers but also to consumers. On those grounds, it had even been suggested in the past that it might be possible to relieve purchases of Fund resources to finance buffer stock contributions from the requirement of need. While the Executive Board had never agreed to such a proposal, it had nevertheless favored more flexibility in applying the decision governing the buffer stock facility. She would therefore bear in mind that the member country should always receive the benefit of the doubt.

Nevertheless, Miss Le Lorier remarked, she could well understand the staff's hesitation. First, the requested purchase amounted only to 0.15 per cent of Australia's import payments. It was therefore rather difficult to accept the arguments that possible future payments difficulties could be related to the freezing of a part of the Australian reserves in the Buffer Stock Account.

She also found it difficult to discover an economic rationale for Australia's requirement of need, Miss Le Lorier went on. The purpose of the Fund was to assist members when they experienced a need for foreign exchange. In the present instance, neither the Fund's liquidity, nor the level of reserves of Australia would be greatly affected by the outcome

of the discussion. On the other hand, payments difficulties that had occurred around the time of the contribution to the buffer stock should suffice to establish a payments need, and the size of the purchase had presumably no bearing on the matter, at least in principle.

Taking up the two aspects of requirement of need discussed in 1976--the balance of payments position and the reserves position--Miss Le Lorier noted that SM/76/197 had stated that a certain use of Fund resources might be considered justifiable on the grounds that a country's reserves were on the low side, although not extremely low, in conjunction with a payments position that was not particularly strong, although perhaps not clearly in deficit. The sentence had obviously been cautiously drafted and was consistent with the case-by-case approach that had been used.

In dealing with the level of reserves, Miss Le Lorier observed, it was normal to take into account a number of factors such as the volume of foreign trade and its variability, the traditional level of reserves, the size of gross and net reserves, and prospective changes. She would therefore have appreciated further details on changes in net reserves. She had found the staff report rather brief in its assessment of Australia's reserves vis-à-vis the many yardsticks that had been used. It would have been helpful, for instance, to have had a comparison in terms of months of imports with the level of reserves of other countries that had benefited from recent buffer stock facility drawings. Malaysia, for instance, had had reserves of more than two months' imports. If the staff was able to confirm that Australia's reserves were comparable to those of such a country, she would have no difficulty in considering them compatible with the requested purchase. Australia's reserve position might be considered, if not weak, on the low side.

There could be no doubt about the poor state of the part of the balance of payments normally considered to be "above the line," Miss Le Lorier stated. The current account deficit had been running at about 6 per cent of gross domestic product, and no major improvement was expected in the near future. Australia's having actively engaged in foreign borrowing rather than drawing down its reserves further or proceeding to a major exchange rate adjustment did not constitute a presumption of absence of balance of payments need. Borrowing that took the place of the use of reserves clearly did not belong above the line as a factor contributing to a payments surplus or to a reduction of the deficit that would have existed in the absence of borrowing. The nature of the recent net private capital inflows would be relevant: were they likely to be short-term flows, and were they likely to continue?

If it was agreed that the balance of payments need should be assessed without taking into account the impact of official borrowing, she would have preferred cumulative data rather than the results of one or two months alone, Miss Le Lorier remarked. Excluding official borrowing, the overall balance of payments deficit had amounted to SDR 66 million for the third quarter of 1982. It would have been useful to have equivalent figures for previous quarters, as it was hardly possible to assess the potential volatility of net capital movements from a single figure.

On balance, Miss Le Lorier concluded, she would give paramount importance to the fact that Executive Directors were dealing with a drawing under the buffer stock facility, and that the requirement of need should therefore be applied flexibly. The small size of the drawing did perhaps make the discussion rather less significant than it might otherwise have been. In the circumstances, and particularly in the light of the comments by Mr. Prowse and the Director of the European Department, she could support the proposed request.

Mr. Casey observed that in EBS/82/183 the staff seemed to have been not entirely convinced by Australia's balance of payments need. In essence, it had seemed to suggest that if Australia's reserves increased in September 1982 the buffer stock purchase would not be justified. The reserves did in fact seem to have increased in September, thus giving him some doubts about the balance of payments need, although not such serious doubts as those expressed by Mr. de Vries.

He had been strongly influenced by Mr. Prowse's statement, which was based on a rather broader view of balance of payments need, Mr. Casey went on, and he did not believe that it would be desirable to postpone any decision. The current account deficit was the highest in the past 30 years; it had been brought on not only by a loss of competitiveness but also by a drought that had had a major effect on agricultural exports. Furthermore, although Australia had been existing with reserves equal to about two months' imports, the authorities did not feel that the situation was comfortable. Other actions such as high interest rates, increased government borrowing, and recent devaluations suggested that the authorities were concerned about the reserve picture and the balance of payments situation generally. Consequently, although the balance of payments need was not entirely clear cut, he had been persuaded by Mr. Prowse's arguments. Furthermore, both the staff's written statement and the remarks by the Director of the European Department seemed to imply a more balanced approach to the question of balance of payments need, and in any event the benefit of the doubt should be given to the Australian authorities.

There might be some merit in re-examining the 1976 paper on balance of payments need, Mr. Casey considered. In such a re-examination, his chair would appreciate the opportunity for making some suggestions, especially in relation to the special problems of defining balance of payments need when the country concerned was a member of a monetary union and thus had a fixed exchange rate and no usable reserves.

Although Australia was a high-income country, Mr. Casey went on, it was by no means legally prevented from making the present request. It was however worth noting that the small size of the drawing--amounting to less than 0.2 per cent of total imports--would only increase the reserves from two months to two months and 100 minutes of imports. If there was reason to believe that other roughly similar requests were likely to be made by high-income members in the future, there might be some merit in re-examining the buffer stock decision itself, perhaps specifying that the value of the compensation for stocks should be above a certain proportion

of total exports. In approving the rather unexpected request, he hoped that the authorities would consider an early repurchase even if the early repurchase provisions did not require them to do so.

Mr. Lovato commented that the request by Australia for a purchase under the buffer stock facility raised some difficult questions that did not seem to have been fully answered by the staff. Article V, Section 3 of the Articles of Agreement made it clear that purchases from the Fund were to be allowed only on the condition that the member "has a need to make the purchase because of its balance of payments or its reserve position or developments in its reserves." In its appraisal, the staff had said that "it is by no means self-evident that Australia's reserve position would generally be regarded as a weak one." He agreed with that assessment; it seemed to him that in the course of the past year, thanks to a strengthening of domestic policies, the Australian authorities had succeeded in substantially increasing their reserve position. It was clear that the reserve position of Australia had improved substantially during 1982 and could not therefore provide the basis for a request for Fund assistance.

The other possibility was to base the request on balance of payments need, Mr. Lovato went on. However, on page 8 of EBS/82/183 the staff had written "The staff believes that the proposed purchase will be justified by a balance of payments need if, at the time of Board consideration of the request, the deficit incurred during July-August has not subsequently been reversed." Fortunately for the Australian economy, the deficit in July-August had indeed been reversed, and by a substantial margin at that, as confirmed by the staff itself. On the basis of those considerations, Mr. Lovato continued, he was led in principle to conclude that the requirement for a purchase under the buffer stock financing facility had not been met. He was however prepared to recognize that there was no clear-cut definition of balance of payments need, and that that circumstance created at least some doubt as to how to proceed with the request. It was significant that even the staff had said that it was unclear whether the test of balance of payments need had or had not been met. It therefore seemed reasonable to him to express reservations, to give the benefit of the doubt to the member country, and to approve the proposed decision if the majority wished to do so, but, as Mr. de Vries had suggested, with the understanding that Australia would repurchase the amount should it become clear within two months or so that the balance of payments had really improved. In any event, balance of payments need should be the subject of a general discussion in the future.

Mr. Laske remarked that he considered the request by the Australian authorities to be rather surprising. After reading EBS/82/183, and hearing the observations of the staff, he still felt that the Australian request was a borderline case that required careful judgment. The staff had obviously had difficulties in making up its mind, and so had he. Like other Executive Directors, he had referred to the discussion that had taken place in 1976 on the requirement of need, and it was evident that the opinion at the time had been that the Executive Board should approach

the question on a case-by-case basis. During the 1976 discussion, his chair had expressed the view that the three separate criteria of a balance of payments position--the level of reserves, developments in reserves, and balance of payments--should be taken in combination. He found no reason to depart from that view. Moreover, so far as the balance of payments itself was concerned, he attached higher priority to changes in the overall balance of payments than to changes in the current account.

Referring specifically to the Australian request, Mr. Laske said that he was satisfied, as all other speakers had been, that the request fully met the requirements of the decision on the buffer stock financing facility. It was important to form a judgment on the level of reserves and developments in the reserves. The statistical picture was not clear. That there had been relatively large swings in reserves in recent years, a point that should be taken into account, but the decline in reserves during July and August 1982 had been more than offset by the increase in reserves during September 1982. Consequently, he still doubted whether Australia had a balance of payments need. He would of course take into account the fact that the authorities had financed their current account deficit by substantial official borrowing. However, during the past three months, official borrowing had been several times the overall deficit, excluding official borrowing. Hence, Australia's gross reserves, together with its capacity for borrowing abroad, had not been so depleted that the financing of the compulsory sugar stocks could not have been undertaken in some other way.

Commenting on the level of Australia's reserves, Mr. Laske remarked that, looking at the longer period, the present reserves did not seem to be so low in relation to imports as might at first sight appear. It was true that the ratio was lower than in the past, but there were also many cases in which the Fund had granted access to its resources where the ratio had been much lower. Consequently, in the present instance, the relationship between reserves and imports did not provide much help in coming to a decision. He had therefore examined the absolute level of Australia's reserves. According to IFS, at the end of September 1982 Australia's gross reserves were higher than they had been for many years. What was not revealed by the figures in IFS was whether there were strong seasonal swings in Australian reserves. Naturally, if such swings were present, they could have an impact on his decision; he would therefore be grateful if the staff could give some further information on changes in reserves, and perhaps explain why the September figures were so high.

In conclusion, Mr. Laske stated, he wished to reserve his position until he had heard the views of other speakers.

Mr. Supinit stated that he was in general agreement with the thrust of the staff paper. He was able fully to support the request by Australia to draw on the Fund's resources under the buffer stock financing facility in order to finance a compulsory contribution to sugar buffer stocks under the 1977 International Sugar Agreement. The request was justified and met

all the criteria of the facility. Australia had experienced persistently large, and increasing, current account deficits in the recent past. The imbalance in the current account was expected to double between 1980/81 and 1982/83. The overall account had been fluctuating widely because of the changes in capital flows. Although Australia's reserves looked large in absolute amounts, they had been greatly influenced by the recent official borrowing. For a major exporter of primary products, a reserve holding of only 2.5 months' of imports was clearly not comfortable in face of a potentially unstable export market. Australia's balance of payments was fundamentally weak, and the country appeared to have a balance of payments need. The continued depreciation of the Australian dollar was also a manifestation of the underlying weakness in the balance of payments.

The staff had indicated, Mr. Supinit noted, that Australia had become the third largest sugar exporter in the world in 1981. He would be interested to know what had caused such rapid expansion. For instance, were the authorities providing an element of subsidy?

Mr. Anson stated that he would concentrate on the main point at issue, namely, Australia's balance of payments need. As others had said, the concept of balance of payments need was fundamental to the operations of the Fund and should be interpreted consistently. He had found it difficult to form a judgment in the present instance. As Mr. Prowse had explained, there were three heads under which balance of payments need could be assessed: the balance of payments position itself, the reserve position, and developments in reserves. Any one of the three elements could qualify a country for drawing on the Fund; it was not clear from the staff paper which of the criteria had been thought most relevant in the present case. The latest figures put forward by the staff were open to more than one interpretation, depending on the treatment of overseas borrowing, and did not give any clear lead. He could however agree both with the Director of the European Department and with Mr. Prowse that it could not be conclusive to assess the reserve position of a country for the purpose of a drawing under the buffer stock facility on the basis of a single month's experience. In the circumstances, he had been grateful for the opening remarks by the Director of the European Department. He agreed that it was difficult to lay down precise guidelines when, after considerable discussion in 1976, the Executive Directors had decided not to codify the rules. It would be proper for Executive Directors to continue applying the case-by-case approach.

He could agree with the Director of the European Department, Mr. Anson said, that the high current account deficit, the depreciation of the exchange rate, and the substantial official borrowing all provided some evidence that there was a weak balance of payments and that reserves were low, at least in the minds of the authorities. Nevertheless, he was perturbed by one or two aspects of the request. First, the larger part of the buffer stock contribution had been made in February 1982. On the matter of timing, the authors of SM/76/197 had written "it is for consideration whether a degree of flexibility should be introduced by allowing drawings, even if they occur up to, say, a year after the contribution is

made, to be classified under the buffer stock facility if and to the extent that the payments difficulties experienced at the time of the drawing could reasonably be attributed to a freezing of the part of the member's reserves in the Buffer Stock Account." The outcome of the discussion had been some support for a more flexible interpretation, as suggested by the staff. He assumed that the same criterion was being applied in the present instance; but he found it somewhat difficult to see how the payments difficulties being experienced in November 1982 could reasonably be attributed to the freezing of SDR 32 million in the Buffer Stock Account in February 1982. Mr. Casey's point about the size of the figures was certainly relevant.

Taking up the question of Australia's reserves, Mr. Anson remarked that he was prepared to give Australia the benefit of the doubt and support the request on the basis of the recommendation made during the meeting by the staff, which had clearly given the matter a great deal of thought. But he hoped that the staff would take note of the hesitations experienced by Executive Directors on the present occasion, especially when they were considering future cases that appeared to be at or near the borderline. Moreover, in future cases the staff could help Executive Directors, not only by recirculating SM/76/197 and Supplement 1, together with the summary of the Board discussion on that occasion, but by preparing a note on the way in which the requirement of need had been interpreted in connection with drawings under the compensatory financing facility and the buffer stock facility in the intervening period. He left it to the staff's judgment how best to present the necessary information; but it should be available so that Executive Directors would not have to find their way through a maze of papers dating from nearly a decade previously. He was not proposing a new codification of policy, but it would be helpful to know whether the decisions being taken on current cases were broadly consistent with those of the past.

Mr. Suraisry commented that the main issue in connection with Australia's request was whether it would satisfy the requirement of balance of payments need. In his view, although the request was not absolutely clear cut, it satisfied that requirement on several grounds. First, the ratio of the current account deficit to gross domestic product in Australia, estimated at 6 per cent in 1982/83, was relatively high. Second, even after the sharp rise in reserves in September, the general level could be considered relatively low for a country that was primarily a commodity exporter and therefore subject to large fluctuations in its terms of trade. Third, the Australian Government had been borrowing overseas to support the balance of payments. If the overseas borrowings were excluded, the increase in reserves since September 1982 would be less than the decline in July and August. Fourth, the exchange rate and interest rate policies followed by the Australian authorities certainly showed their concern about the balance of payments position. Together with the requirement of balance of payments need, the request clearly met all the other requirements for a purchase under the buffer stock financing facility. He therefore had no problem in supporting the request.

Mr. de Groote commented that a large number of requests for drawings under the buffer stock facility had already been submitted to the Executive Board, and that they would continue to be submitted in the period ahead was a clear indication of the usefulness of the facility, particularly during the present period of low commodity prices. The use of the facility by members should be encouraged in the present circumstances. The request before the Executive Board fully satisfied the specific requirements of the buffer stock facility with respect to the International Sugar Agreement.

While he did have some difficulties with Australia's use of Fund resources in relation to the balance of payments need, Mr. de Groote remarked, he had been struck by an increasing tendency on the part of some colleagues to impose a stricter interpretation of the requirement of need when higher-income countries were involved. He saw no justification for such an attitude. Executive Directors often complained that only developing countries were making use of Fund resources, while adopting a more critical attitude when higher-income countries approached the Fund. It would of course be useful if the countries that made use of the unconditional resources of the Fund could also rely on its conditional resources when a need for adjustment was clearly involved. Mr. Prowse had convincingly argued that Australia was facing certain adjustment problems. He also noted that the most recent Article IV consultation with Australia dated back to March 1981. The Executive Board could therefore usefully schedule a discussion of Australia's economy in the not-too-distant future.

He would find it difficult to argue that the requirement of need was not satisfied, Mr. de Groote went on. The requirement of need was to be judged not only at the moment of Board consideration, but over a reasonable period of time. Moreover, the balance of payments was to be evaluated on the basis of autonomous transactions, excluding official borrowing. The fact that more market borrowing would be available did not mean that there was no balance of payments need. As Mr. Prowse had indicated, capital inflows had been induced by actions of the Government, but the interest rate mechanism could be regarded largely as nonautonomous. Australia had been accumulating an increasing balance of payments deficit on current account, and its reserves were relatively low, even if the borrowed amounts were brought into account. Would Executive Directors have been more easily convinced that there was a balance of payments need if Australia had not been borrowing abroad and had thus had a lower level of reserves? The Fund should give Australia the full benefit of the doubt. In the circumstances, he could fully support the staff view and the proposed decision, as all the factual information provided by the Director of the European Department indicated that Australia was indeed in balance of payments need.

The resources to be drawn on by Australia should be readily available once Executive Directors gave the country the benefit of the doubt, Mr. de Groote observed. The reserves were cheap, and they would benefit Australian farmers. He was glad that a high-income country like Australia felt sufficiently at home in the Fund to ask for a small amount of financing when it was available. Australia had set an example of approaching the Fund that industrial countries could follow with benefit.

Nevertheless, Mr. de Groote went on, he had to take issue with something that Mr. Prowse had said, namely, that participants in the European Common Margins Arrangement, some of them with high reserves, routinely drew on the Fund and used SDRs for the settlement of deficits in connection with intervention. There must be a real misunderstanding. The Common Market countries had agreed to settle their obligations among themselves as a result of intervention within the EMS in reserves according to the distribution of their reserves, and they only used the reserve positions available to them in the Fund for that purpose. They did not use the Fund's buffer stock facility or draw their reserve tranche to settle obligations.

Mr. Kafka stated that he agreed with Mr. de Groote.

Mr. Vidvei said that his chair supported the view that the proposed purchase was justified, and that it was in accordance with the rules as the Fund had written them. He did however believe that an assessment of a country's balance of payments in connection with buffer stock financing should be based on developments in the current balance of payments over several months, not on developments in the very short run.

Mr. Salehkhou stated that he, too, after hearing Mr. Prowse's statement and the remarks by the Director of the European Department, felt that the requirement of need had been met. Furthermore, considering the relatively modest amount of the request, there was every indication that the other requirements had been met as well. His chair would therefore support the request.

Mr. Jayawardena recalled that the purpose of the buffer stock financing facility had been to ensure reasonable stability in commodity prices, which were known to be volatile. Beneficiaries of stable prices were not only producers of the commodities, but also consumers and the whole international economic system. In general, only the producers and the consumers of the commodity in question expected to finance buffer stocks. True to its international responsibilities, the Fund stepped in to provide such financing, when a country required to make a contribution to a commodity buffer stock, found itself in balance of payments difficulties. From that standpoint, the traditional position of his chair would be that more affluent countries should not resort to the buffer stock financing facility, because by so doing they would reduce the volume of resources available for disadvantaged countries. Of course, he would not deny any Fund member's right to approach the Fund for a drawing under the facility, and each request should be examined on its merit. In the present circumstances, he had been convinced by the arguments put forward by Mr. Prowse to the effect that there was a balance of payments need. A balance of payments need could not be assessed simply by examining the developments in the past three months; it had to be assessed over a longer period. Similarly, he agreed with the observations made by the Director of the European Department at the beginning of the meeting; he could therefore support the request.

Mr. Munthali stated that he could support the proposed decision set out on page 9 of EBS/82/183. The information provided by the Director of the European Department in his second statement indicated the emergence of an overall surplus not only in September 1982 but for the third quarter of 1982 as a whole, reflecting the inflow of capital, including external borrowing by the Australian authorities. He had however been rather persuaded by Mr. Prowse's line of argument. He had demonstrated the underlying economic weakness in Australia's balance of payments position. The outturn in the third quarter of 1982 could have resulted in an overall deficit to the extent of SDR 66 million if official borrowing were excluded. He also sympathized with Mr. Prowse's conceptual approach in establishing the balance of payments need. His reference to SM/76/197 was particularly relevant. It was important to approach the question of balance of payments need with flexibility. He thus found it logical to lend his support to the request by Australia.

Mr. Erb stated that he had some doubts whether Australia did have a balance of payments need. Nevertheless, after hearing the remarks by his colleagues and examining SM/76/197, he was prepared to give Australia the benefit of the doubt. He would however support Mr. de Vries' third suggestion to the effect that, in view of Australia's balance of payments position, the country was a good candidate for an early repurchase. He also agreed with Directors who had suggested that the Executive Board should re-examine the 1976 paper and related discussions on the question of balance of payments need. It was a topic that he had raised in a number of discussions on specific requests. In the light of the changes in the international financial system that had taken place since the previous major review, it would be desirable to have a full-scale discussion. Moreover, the request by Australia had added to the questions in the minds of his own authorities about the desirability of maintaining charges at such a highly subsidized level. That too was an issue that he would wish to take up again at a later date.

The Director of the European Department, replying to questions, noted that as a means of safeguarding the Fund's resources, apart from requiring early repurchase by Australia, the Fund could use the operational budget to the same effect. It might be worth recalling that in dealing with the question of need, the Articles did not define precisely which definition of the balance of payments, (e.g., the most recent current balance, the overall balance, etc.) was most relevant. In 1976 the staff had put great emphasis on the overall balance; but Executive Directors had refused to endorse the staff's suggestion on that point. Similarly, the Articles were not very specific in their reference to the reserve position: it was unclear whether the Articles referred to the level of reserves or the evolution of reserves. In the present instance, the staff had based its opinion on the level of reserves.

Taking up the points raised by Miss Le Lorier, the Director noted that while Australia's gross reserves were equivalent to roughly 2.5 months' imports, the reserves of other countries that had drawn on the buffer stock facility had been: Malaysia, 3.8 months; Thailand, 3.2 months; Bolivia,

2.2 months; and Philippines, 4.6 months. Other more developed primary producing countries were Spain with 5 months of reserves and New Zealand with 1.25 months of reserves, with other countries in between. In reply to another question by Miss Le Lorier, Australia's current account position had varied little in the past three quarters, showing a deficit of about $2.2 billion per quarter. Consistent figures on the overall balance, after allowing for compensatory borrowing, were unavailable, however, as the authorities did not always find it possible to distinguish between borrowing undertaken for balance of payments reasons and other borrowing. He could agree with Mr. Anson's comment that the staff paper could have been made more extensive.

Referring to Mr. Supinit's suggestion that the sharp increase in Australia's relative share of the world sugar market could perhaps be attributable to the use of subsidies, the Director of the European Department recalled that it was intended to hold an Article IV consultation with Australia in the spring of 1983. The staff would certainly respond to Mr. Supinit's question at that time.

The Director of the Legal Department commented on the requirement of need as it applied under the Articles to purchases from the Fund. The requirement of need could be met if a member qualified under one of three criteria. It was however not a condition that could be waived. Nevertheless, perhaps just because the condition could not be waived, the Fund had applied the criterion flexibly. When the provision had been inserted in such specific terms in the Articles, it had been explained that the intention was to reflect, under the Amendment, the prior practice followed by the Fund in relation to the requirement of need with respect to both purchases from the General Department and the use of SDRs. It had been agreed that the Fund would continue to apply the requirement of need in a flexible manner; and, when attempts had been made to bring about some codification, the Executive Directors had shown reluctance to follow the suggestion because they had felt that codification might in some way restrict the flexibility with which it was intended to apply the concept. The intention remained to apply the requirement of need on a case-by-case basis, in the light of past practice and with a view to ensuring uniform application.

Taking up the specific suggestions made by Mr. de Vries, the Director mentioned first that if the Executive Board found that they had serious doubts whether the requirement of need was met, they could either delay or reject the request. On the other hand, it had been the common practice in connection both with the purchases of currencies from the Fund and with the use of special drawing rights to give the member the benefit of the doubt. The second suggestion by Mr. de Vries had been that, instead of approving the request outright, the Executive Board should aprove what amounted to a stand-by arrangement under which it would agree that the member could make a purchase if and when management felt that the requirement of need had been met. Such a technique was of course possible. But in each instance when a purchase was made under a stand-by arrangement, the balance of payments need had to be present at the time that the purchase was made.

He would however not recommend that practice to the Executive Board, the Director of the Legal Department concluded. The Fund had not applied that technique in connection with the buffer stock facility or the compensatory financing facility. It had been used only in connection with purchases subject to the type of conditionality attaching to the higher credit tranches. In any event, the Fund would have to adopt some general policy rather than to apply the technique to one particular member. The third suggestion by Mr. de Vries, namely, that Australia should be asked to make an early repurchase in accordance with Article V, Section 7(b) of the Articles, was already a policy that applied to all purchases, including purchases under special facilities. In accordance with Article V, Section 7(b) and the decision on early repurchase, under the buffer stock facility the Australian authorities would have to make a repurchase before they would otherwise have to. It would also be possible for the Fund to use the operational budget as a means of insuring a reduction in the Fund's holdings of Australian dollars resulting from the proposed purchase.

Mr. de Vries mentioned that Mr. Polak had come to the conclusion that the papers available to Executive Directors did not allow him to conclude that the requirement of need had been met. He had, however, noted that most speakers had not shared that opinion, and he had been struck by Mr. Anson's observations in which, while giving the Australian authorities the benefit of the doubt, he had noted that many Executive Directors would have preferred the staff to be more reticent in such borderline cases. He hoped that Mr. Anson's comment would be one element in any conclusion that might be reached, and he had been encouraged by the remarks of the Director of the European Department and the Director of the Legal Department about the possibility of using the currency budget to reduce the Fund's holdings of Australian currency, and about the early repurchase policy. In those circumstances, he would not oppose the request. In taking that position, like Mr. de Groote, he welcomed the use of the Fund's resources by higher-income countries.

Mr. Laske stated that, so many Executive Directors having supported the request by the Australian authorities, he would also go along with it. He would however echo what Mr. Erb had said regarding the possibility of early repurchase, and he was sure that his authorities would appreciate it if the Australian authorities would see fit to use the funds at their disposal for an early repurchase if the country's reserves improved in the near future. He would also agree with Mr. Casey's proposal that consideration should be given to incorporating into the provisions for the buffer stock facility an arrangement that would require a member to request a minimum drawing related to its overall export earnings.

Mr. Prowse, replying to comments by Executive Directors, remarked that a passage in Fund Pamphlet No. 34 was relevant regarding the level of reserves. It had there been written that "It is not possible to define a level below which reserves should be considered as inadequate, because the adequate level of reserves may vary considerably from country to country. On the one hand, some countries belonging to a common currency union may operate with very low reserves of their own because they have easy access

to a pool of reserves within the union. On the other hand, some countries subject to wider fluctuations in their export earnings may consider that their reserves are inadequate if they do not exceed the equivalent of half a year's imports." As that was a statement in a Fund document, countries were surely entitled to take it as guidance in formulating their own policies. He had drawn attention to the level of Australia's reserves, and the observation was particularly apposite in the case of Australia.

Commenting on Mr. de Groote's remarks about a more flexible interpretation of the requirement of need in connection with the buffer stock facility, Mr. Prowse recalled that the Executive Directors, in their report to the Interim Committee on May 29, 1975, had written: "As regards the requirement of need in the application of the existing buffer stock facility, most Directors felt that the requirement as such should be maintained; some others favored more flexibility in its interpretation."

Taking up the question about developments in reserves, Mr. Prowse remarked that the argument seemed to be that balance of payments need based on developments in reserves was restricted to the reserve countries, or countries that had substantial commitments of a financial kind on their reserves. That was of course not the case in Australia. However, in SM/76/197, Supplement 1, the staff had written: "One important consequence of the aspect of need is that the requirement does not bar a member with adequate or even high reserves from using either the Fund's resources or SDRs." Continuing, the staff had said that "this principle was established long ago in connection with Fund resources, but a clear-cut instance which also involves SDRs, is that countries with high reserves routinely draw on the SDRs in the settlement of their claims in connection with the snake intervention." He was using the quotation as an example of the interpretation of balance of payments need in particular circumstances.

On the question of capital inflows, Mr. Prowse explained that his proposition had been that if borrowing by the Commonwealth of Australia Government--which was general-purpose borrowing to support reserves--were eliminated, the deficit in the first two months of the third quarter of 1982 would not be offset by the outcome for the third month. His further argument had been that there was at least some conceptual support for keeping government borrowing "below the line." The private capital inflows that had occurred in September 1982 were quite extraordinary, in that September was normally an adverse period for the balance of payments owing to seasonal factors. While the cause of the inflows had not yet been traced, it seemed likely that they had occurred in response to financial factors, and that therefore they might well be reversed in the coming period. His authorities had examined the available information and had concluded that the inflows had been caused to a significant extent by Japanese investment in the form of purchases of existing government and semigovernment fixed-interest securities to the extent of some $A 800 million in July and August 1982, and September 1982. At that time, Australian interest rates had been higher than the rates available in the Japanese market; Japanese investors had become rather disenchanted with certain other financial markets; there had been some doubt about the future value

of the yen; and there had perhaps been a view that interest rates were reaching their peak in Australia. Basically, however, the inflows had taken place in response to high interest rates maintained as a matter of policy by the Australian authorities; they were liable to be reversed when the interest rate differential was narrowed.

The Australian authorities would of course accept the legal position regarding early repurchase, Mr. Prowse stated. Executive Directors had however been interested to know whether the authorities would go beyond the legal position. The authorities had said that they would consider early repurchase if there was a strong improvement in reserves, quite apart from any obligations that they might have entered into in that connection. Moreover, an Article IV consultation with Australia had been scheduled for March 1983; it would be a good opportunity for reviewing the fundamental issues that some Directors had raised during the discussion.

It seemed to him important, Mr. Prowse asserted, that countries like Australia, meaning advanced countries with relatively high incomes, should use the Fund's resources as circumstances permitted. In general terms, the Fund ought surely to encourage rather than to discourage that practice.

He was grateful to all Executive Directors who had spoken, Mr. Prowse said. He would convey their thoughtful comments to the Australian authorities, who, he was certain, would examine them in detail. That the staff, in its care for preserving Fund doctrine and principles, had not put a more clear-cut solution before Executive Directors in EBS/82/183 was rather to its credit than the opposite.

The Chairman remarked that it was clear that the Executive Board had agreed to approve the request by Australia. Two other points might however be made. First, it was understood that if the reserve position of Australia were to improve, the authorities would show a spirit of cooperation with the Fund with regard to the early repurchase policies. Second, as Mr. Anson and other speakers had suggested, the Board could review the 1976 decision on the requirement of need in the light of the present policies on compensatory financing and the buffer stock facility. It would be useful to review cases in which members had been discouraged from making a request from the Fund on the grounds of a particular interpretation of the requirement of need, or in which requests had been submitted to the Executive Board, and the requirement of need had been invoked. He welcomed the observation by Mr. de Groote and other Executive Directors that it was helpful for the working of the Fund when industrialized or advanced developing countries felt at home in using its resources.

The Executive Board then took the following decision:

1. The Fund has received a request by the Government of Australia for a purchase of the equivalent of SDR 32.463 million under the decision on buffer stock financing facility: the problem of stabilization of prices of primary products (Decision No. 2773-(69/47), adopted June 25, 1969, as amended by Decision No. 4913-(75/207), adopted December 24, 1975), and the decision on buffer stock financing facility: 1977 International Sugar Agreement, Decision No. 5597-(77/171), adopted December 16, 1977).

2. The Fund determines that this purchase would be in conformity with the decisions referred to in (1) above, notes the representations of Australia, and approves the purchase in accordance with the request.

Decision No. 7241-(82/143), adopted
November 5, 1982

APPROVED: April 1, 1983

LEO VAN HOUTVEN
Secretary

Table 1. Australia: Official Reserve Assets and Imports

(In millions of Australian dollars; end of period)

	Foreign Exchange	Months of Imports	Total (gold at SDR 35 per ounce)	Months of Imports
1971-72	3,146	10.0	3,382	10.7
1972-73	3,684	11.6	3,904	12.3
1973-74	3,051	6.4	3,260	6.8
1974-75	3,010	4.7	3,251	5.1
1975-76	2,145	3.3	2,384	3.6
1976-77	2,164	2.5	2,444	2.8
1977-78	1,708	1.8	2,003	2.2
1978-79	1,565	1.4	1,885	1.7
1979-80	1,355	1.0	1,672	1.3
1980-81	2,223	1.4	2,501	1.9
1981-82	4,074	2.2	4,370	2.3
1982				
September	4,733	2.5	5,011	2.3

Table 2. Australia: Current Account of the Balance of Payments as a Percentage of GDP

	Current Account Balance (in $A mlns.)	Current Account Balance as Percentage of GDP
1971-72	-338	-0.9
1972-73	711	1.7
1973-74	-842	-1.6
1974-75	-957	-1.6
1975-76	-1,072	-1.5
1976-77	-2,073	-2.5
1977-78	-3,056	-3.4
1978-79	-3,805	-3.7
1979-80	-2,071	-1.8
1980-81	-5,225	-4.0
1981-82	-9,097	-6.2
1982-83 1/	-10,000	-6.0

1/ Forecast.

Table 3. Australia: Australian Dollar Exchange Rates 1/

	TWI of Value of $A (May 1970 = 100)	US$/$A Mid-Rate
1980		
June	85.0	1.1576
1981		
June	92.9	1.1480
July	94.2	1.1356
August	94.4	1.1508
September	93.8	1.1414
October	93.0	1.1350
November	91.2	1.1514
December	90.5	1.1279
1982		
January	90.1	1.0994
February	89.2	1.0740
March	88.8	1.0503
April	88.2	1.0608
May	88.0	1.0482
June	88.2	1.0223
July	86.1	0.9958
August		0.9643
September		0.9493
October 14	83.7	
October		0.9367

1/ End of month (except second last entry).