

EXECUTIVE BOARD MEETING 54/38

1818 H Street, N. W.

11:00 a. m., July 9, 1954

13 SEP 54

Present:

I. Rooth, Chairman; Executive Directors: D. Crena de Iongh, E. Delgado, A.K. Eriksen, A.Z. Saad, F.A. Southard, B. Tann, T. Yumoto; Alternate Executive Directors: J. C. Godeaux, B. B. Callaghan, G. Grosse (Temporary), S. T. G. Akermalm, C. P. Caranicas, A. de Lattre, J. C. Gouvea, V.G. Pendharkar, J.H. Warren, F.J. Portsmore, A. Mansour, K. H. Yu, W. Tennekoon; R. L. Horne, Acting Secretary; F. Hodel, Assistant.

Present for Item:

2--G. L. L. de Moubray, Technical Assistant; H. L. Dey, Director, Asian Department; F. C. Dirks, Western Hemisphere Department; J. G. Evans, Legal Department; G. Ferras, Deputy Director, Exchange Restrictions Department; L. S. Friedman, Director, Exchange Restrictions Department; E. P. Hexner, Legal Department; E. Jones, Exchange Restrictions Department; Y. C. Koo, Treasurer; C. L. Merwin, European Department; A. Pfeifer, European Department; H. Ponsen, European Department; J. Reid, Office of the Managing Director; J. P. Salle, European Office; J. M. Stevens, Director, European Department; J. O. van der Mensbrugghe, European Department.

1. Approval of Minutes

The draft minutes of Meeting 54/34 were approved.

2. Free Exchange Market for Certain Transactions - Netherlands and Belgium-Luxembourg Proposals

The Executive Board took up the request of the Netherlands, Belgium and Luxembourg for approval of exchange measures designed to liberalize the movement of capital and channel certain current payments between their monetary areas (EBS/54/17, 7/7/54) and the request of Belgium and Luxembourg for the approval of exchange measures which would set up machinery in the Belgium-Luxembourg Economic Union for facilitating capital movements between the BLEU and other members of EPU (EBS/54/17, Sup. 1, 7/7/54). The staff analysis and recommendations were also considered (EBS/54/17, Sup. 2, 7/8/54). The proposed Benelux measures envisaged the establishment of a free market through which all capital movements within Benelux must be carried out and through which the payor, at his option, could effect certain invisible current payments. The BLEU proposal made similar facilities available to other EPU countries if they wished to participate. The staff recommended that the Fund not object to the multiple currency practices that might arise in the territories of the Netherlands, Belgium and Luxembourg as a consequence of the exchange measures proposed.

Mr. Crena de Iongh expressed his general agreement with the staff analysis of the Benelux proposal. He noticed, however, that particular attention had been given to the question of the deviating rates which might develop in the free markets to be established. The fundamental purpose of the proposed measures was the liberalization of capital transactions between the areas and the rate question was merely a by-product of this primary objective. He felt the Board could only welcome the measures as representing further progress by the Benelux countries towards convertibility. Mr. Godeaux associated himself with these remarks. It was understandable that the staff analysis concentrated on the aspects within the Fund's jurisdiction, but this should not detract from the Board's judging the proposals in the light of their main purpose. The Benelux measures were primarily designed to attain greater freedom of transactions between the Netherlands and Belgium and Luxembourg. The BLEU proposal was submitted as a supplement to the Benelux measures and also constituted another step toward greater freedom and eventual convertibility. The techniques to be used, which might result in the development of multiple rates, were far less important than the over-all objectives.

In the discussion, Mr. Southard said he had no objection to the proposed measures. He agreed that they should be considered in the light of their real objective as transitional steps toward wider convertibility, and, as such, were worth a try. Although it was possible that multiple rates might develop in the free markets, it was not at all evident that the deviations would be very great. In any event, he did not believe the rate discrepancies would be important or harmful to movements between Benelux and the dollar area. In this connection, he noted that the legal arrangements presently governing capital movements between these areas would not be affected. In respect to the BLEU proposal, he asked whether the measures could be regarded as a complete legalization of transactions that might now be taking place in the so-called free market in Belgium for EPU currencies. Mr. Godeaux pointed out that the existing arrangements, which had been reviewed in the 1952 and 1953 consultations, applied only to Belgian and Luxembourg residents. The proposed measures would make it possible for certain specified current transactions to take place in the contemplated free market and residents of other EPU countries could participate if their countries permitted it.

Mr. Portsmore accepted the staff analysis as a reasonable statement of what the proposals were intended to accomplish and he indicated that he would not object to them as temporary measures pending further progress towards convertibility. It was to be regretted, however, that the Governments concerned found it necessary to accomplish their objective by establishing arrangements which might result in multiple currency practices. He enquired whether it was expected that these arrangements would necessarily terminate when the Belgian franc and the Netherlands guilder became convertible. Mr. Crena de Iongh replied that the Benelux authorities were unable to foresee what the position would be at that time. In regard to the BLEU proposals, Mr. Portsmore said that he would have found them more acceptable if they had not included certain current transactions and had related entirely to capital transactions. Mr. Godeaux explained that the inclusion of some current invisibles was to provide a balancing element which would help to keep the possible rate fluctuations within narrow margins.

Mr. Eriksen regretted that there had not been time for him to get the reaction of the countries that elected him. Speaking personally, however, he thought it went without saying that the multiple currency aspects of the schemes were not very welcome. Nevertheless, he was prepared to go along with Fund approval of the Benelux proposal on a temporary basis and on the understanding that the proposed measures were not regarded as part of the long-run exchange policy of the Benelux countries. He had more doubt regarding the BLEU measures, but would also agree to their approval on a temporary basis with the understanding that the creation of the "L" accounts would only be possible to the extent that the authorities in EPU countries permitted their residents to avail themselves of the facilities created by the BLEU. He understood that, without such permission, payments to residents of his countries would continue to be made in accordance with the respective payments agreements and, further, that the BLEU authorities would not permit the currencies of his countries to be quoted on the free market if those countries objected. In this connection, Mr. de Lattre inquired whether the BLEU authorities would require evidence from a prospective "L" account holder that his Government permitted him to hold such an account. Mr. Godeaux replied that the regulations did not require Belgian banks to have documentary evidence of such permission. The enforcement of other countries' exchange regulations rested with those other countries. However, the Belgian authorities had, in the past, demonstrated their spirit of co-operation and in the same spirit, they would certainly be ready to discuss with other countries their particular problems in this connection.

Mr. Warren thought the Fund should not object to the proposals as temporary measures pending fuller convertibility. He was not convinced that the special arrangements being considered were necessary, but he recognized that the Governments concerned were in the best position to decide. Mr. Caranicas said he also would support approval because of the objectives of the proposals, notwithstanding the fact that they contained multiple rate elements.

The draft decision was considered. Mr. Godeaux put forward several revisions. Some Directors asked whether the Fund had to limit its approval explicitly to the multiple currency aspects which might emerge from the proposed measures. There seemed to be no reason why the Fund's action could not relate to the proposed system as a whole, as had been suggested by Mr. Godeaux. Other Directors agreed. The staff representative also saw no objection, provided it was understood that the Fund would only be expressing no objection to matters within its jurisdiction. Mr. Southard asked whether Fund approval under Article VIII, Section 3 would be required if the free markets were limited to capital transactions. Mr. Saad thought that the Fund should consider the legal aspects of the question whether multiple currency practices so limited required Fund approval. He asked if the staff regarded Article VI, Section 3 as providing an exception. The Legal Department representative replied that this question had never been specifically discussed by the Board. The staff had been guided in its approach to this question by the consideration that the obligation of members to maintain the rates for exchange transactions within the prescribed margins applies to all exchange transactions. No distinction between current and capital transactions is contained in Article IV, Section 3, nor is such a distinction made in Article IV, Section 4(b) under which members undertake to insure that exchange transactions would take place in their territories at rates within the prescribed limits. Nor does the first sentence of Article VIII, Section 3 which requires members not to apply multiple currency practices without approval of the Fund differentiate between current and capital transactions. The significance of the absence of a specific differentiation between current and capital transactions is emphasized in Article VIII, Section 3 when compared with the text of Article VIII, Section 2(a). The text of this latter provision specifically limits its applicability to current payments. In view of this situation it would be difficult to construe Article VI, Section 3 which leaves members free to exercise controls necessary to regulate international capital payments as an exception to the provisions of Article IV, Section 3 and 4(b), and the first sentence of Article VIII, Section 3. While the first sentence of

Article VIII, Section 3 states that members shall not engage in multiple currency practices "except as authorized under this Agreement," in view of the provisions of Article IV, Sections 3 and 4(b), it would be difficult to imply that such an authorization was intended by Article VI, Section 3. An example of an intended authorization is Article XIV which permits members to maintain multiple currency practices under specified conditions, and this authorization has been recognized by the Board. Moreover, there seemed to be no implication in the letter of December 19, 1947 (EBD 235, Rev. 2) that a member could engage in multiple currency practices for capital transactions without Fund approval. The Board's consideration of multiple rates in December 1947 (EBM 234, Item 4, 12/12/47, EBM 235, Item 4, 12/17/47, and EBM 237, Item 3, 12/18/47) suggested only that members in eliminating multiple currency practices give preference to their removal in respect to current transactions.

Mr. Saad said that he still believed that this matter should be carefully examined in the light of the clear text of Article VIII, Section 3, which does not require approval by the Fund of multiple currency practices if they are authorized under the Agreement. Article IV, Section 3 seemed to give members authority to "exercise such controls as are necessary to regulate international capital movements." Such control on capital transactions could take the form of multiple currency practices. However, he believed the decision in this case should be in the broader form suggested by Mr. Godeaux. The exchange measures involve multiple currency practices applied to current transactions which would require Fund approval. Mr. Southard also agreed that the decision should be in the broader form. He added that he still had some doubts as to the meaning of Article IV, Section 4(b). From the practical standpoint, he thought that there was a limit beyond which a member should not be expected to go in supporting the exchange rates of other members within its territories--i.e., the words "appropriate measures" probably did not need to be interpreted to mean "all necessary measures." Mr. Godeaux added that the draft decision he proposed should be understood in the sense that the Fund would approve whatever part of the system required the Fund's approval. But it was not necessary at this time to enter into a long discussion of a legal nature as to the extent of the Fund's jurisdiction in this matter.

In conclusion, the decision in regard to the Benelux proposal was:

1. The Netherlands and Belgium-Luxembourg have informed the Fund of their decision to grant complete freedom to movements of capital between

their respective territories. However, in order to prevent movements of capital from affecting their respective EPU positions, they have proposed the establishment of a free market for such capital transactions and certain current transactions between their currencies. All payments for the purpose of transferring capital between the respective countries must be carried out through these free markets. At the option of the payor, specified current transactions may also be carried out through these free markets. Payments for current transactions directly connected with foreign trade cannot be carried out through these free markets and must take place at rates governed by the established par values.

2. These exchange practices may give rise in the territories to the monetary area of Belgium-Luxembourg, on the one hand, and of the Netherlands monetary area, on the other hand, to exchange rates in the free markets exceeding the margins prescribed in Article IV, Section 3, and to this extent would constitute a multiple currency practice. The Fund notes that the Central Banks have made an arrangement which provides for the possibility of intervention in the free markets in order to avoid disorderly fluctuations of the rates.

3. The Fund does not object to the proposed system as a temporary measure and intends to remain in contact on this subject with the authorities of the Netherlands and of Belgium-Luxembourg.

The decision with respect to the BLEU proposal was:

1. Belgium-Luxembourg have consulted the Fund respecting their intention to adopt regulations designed to facilitate the movements of capital between the Belgium-Luxembourg Economic Union and other EPU countries. These regulations include the establishment in Belgium and Luxembourg of a free market for certain transactions between their currencies and the currencies of other EPU countries. All payments for the purpose of transferring capital between the respective countries and the purchase and sale of their banknotes as well as payments for specified current transactions could be carried out at the option of the payor through this free market. Payments for other current transactions directly connected with foreign trade could not be carried out through this free market in Belgium and Luxembourg and would have to continue to take place at rates governed by established par values.

2. These exchange practices might give rise in the territories of the monetary area of Belgium-Luxembourg to exchange rates in the free market exceeding the margins prescribed in Article IV, Section 3, and to this extent would constitute a multiple currency practice. The Fund notes the BLEU statement that the proposed system is a temporary measure pending further progress towards convertibility.

3. The Fund does not object to the proposed system as a temporary measure and intends to re-

main in contact on this subject with the authorities of Belgium and Luxembourg.

APPROVED BY THE EXECUTIVE BOARD:

Meeting 54/48, August 18, 1954

H. MERLE COCHRAN
Acting Chairman

ROMAN L. HORNE
Acting Secretary