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INTERNATIONAL MONETARY FUND

SEMINAR 72/7

12:15 p.m., March 10, 1972

F. A. Southard, Acting Chairman

Executive Directors	Alternate Executive Directors
	R. van S. Smit
E. Brofoss	
R. Bryce	
	C. R. Harley
	M. Al-Atrash
	N. H. Hanh
	B. Martins
B. Kharmawan	C. P. Caranicas
P. Lieftinck	
	S. S. Marathe
	R. H. Arriazu
	R. H. Gilchrist
	S. B. Nicol-Cole
F. Palamenghi-Crispi	
G. Schleiminger	L. Fuenfgelt
H. Suzuki	K. Satow
L. Ugueto	
	H. G. Schneider
	C. Beaurain
	L. M. Rajaobelina

R. V. Anderson, Acting Secretary
P. F. Gourley, Assistant

Also Present
Administration Department: H. H. P. King. African Department: M. Touré, Director; C. L. Merwin, Deputy Director; U Tun Wai. Asian Department: A. A. Mattera. Central Banking Service: G. Dorrance. European Department: B. Rose. Exchange and Trade Relations Department: E. Sturc, Director; C. D. Finch, Deputy Director; S. Mookerjee. Legal Department: A. S. Gerstein, Deputy General Counsel; G. P. Nicoletopoulos, Deputy General Counsel; P. R. Lachman. Middle Eastern Department: M. M. Hassanein. Research Department: J. J. Polak, Economic Counsellor and Director; J. M. Fleming, Deputy Director; C. F. Schwartz, Deputy Director; F. Hirsch, D. Ridler, T. G. Underwood. Treasurer's Department: W. O. Habermeier, Treasurer; F. C. Dirks, D. Williams. Western Hemisphere Department: S. T. Beza, C. E. Sansón. Personal Assistant to the Managing Director: L. F. T. Smith. Advisors to Executive Directors: F. K. Hussein, J. B. Zulu. Technical Assistants to Executive Directors: V. Barattieri, B. Brock, A. M. Dierick, A. Doizé, B. P. Eap, F. García-Palacios, L. Halfmann, P. C. Hayward, K. Kjaer, R. W. Ley, H. Oyarzábal, C. C. Ozumba, A. Pipino, E. W. Shann, N. Tsukagoshi, J. R. Vallet.

1. REFORM OF THE INTERNATIONAL MONETARY SYSTEM - A SKETCH OF ITS SCOPE AND CONTENT

The Executive Directors resumed from Seminar 72/6 their discussion of a sketch of the reform of the international monetary system prepared by the Economic Counsellor (SM/72/56, 3/7/72).

The Acting Chairman said that he understood that there was still some Executive Directors who had questions to ask of the staff about SM/72/56.

Mr. Palamenghi-Crispi said that he had two questions to ask about the Economic Counsellor's lucid and extremely useful paper. First, he very much agreed with the Economic Counsellor that the process of reform should not be overloaded with changes which were neither essential nor urgent. Such were the difficulties that were being encountered in agreeing to even a minimum set of measures, that to go beyond them could well be impossible. Having said that, however, he still wondered whether it would not be useful to think in terms of amendments to the Articles of Agreement which were drafted in such a way that additional reforms could be introduced as the need for them arose without necessarily having to resort in all cases to further amendments. Second, his chair, like those of Mr. Dale and Mr. Schleiminger, had always supported the view that an effective adjustment process was essential to any reform of the international monetary system. The Economic Counsellor, it would seem, also concurred in that view. He wondered, however, whether the Economic Counsellor had discarded the concept of an emerging or incipient fundamental disequilibrium which the Executive Directors had usefully introduced into their 1970 Report. In that connection, he was not sure that he fully understood exactly what was meant by the last sentence of the second paragraph on page 5 of SM/72/56 which stated, "It is primarily a matter of judgment whether the adjective 'fundamental' should continue to be used to describe disequilibria for the correction of which par value changes are judged to be appropriate within the framework of a more flexible parity system." Finally, he agreed with Mr. Mitchell's view that progress on reform would be linked with the establishment of an advisory committee of the Board of Governors. He wondered, therefore, whether the parallel approach suggested by the Acting Chairman at Seminar 72/6, if he had understood him correctly, would not perhaps assist to some extent Executive Directors' progress toward effective discussions of the issues involved in the reform of the international monetary system.

The Economic Counsellor thought that the question of how broadly amendments could be drafted and what powers of future change could be bestowed on the Executive Directors or the Board of Governors could best be determined when the time came to draft the amendments. It was unlikely that much progress could be made by discussing it in the abstract at the present stage of the proceedings.

Turning to Mr. Palamenghi-Crispi's second question, the Economic Counsellor thought that it might be useful to indicate the sort of conflicting opinions that might be involved in a judgment of whether the adjective "fundamental" could usefully be retained in the context to which Mr. Palamenghi-Crispi referred. Two kinds of considerations had to be taken account of. On the one hand, the general operation of the exchange rate regime under the aegis of the term "fundamental" during the past 10-15 years had not been characterized by the type of flexibility that would be desirable in the future. That being the case, he would expect public opinion in general to have the impression that "fundamental" disequilibrium was a more absolute kind of disequilibrium than the Fund would want it to believe would guide the flexibility of the parity system in the future. On the other hand, the 1970 Report of the Executive Directors had gone a great distance in saying that that was not the case, and that the Fund could be very forthcoming in defining a situation of "fundamental" disequilibrium. Clearly, when the time came to draft the new provisions, a decision would have to be reached as to whether the old wording could be retained, on the understanding that its connotation had changed, or whether it should be changed in order to demonstrate more clearly that a new system had been adopted. As to the somewhat separate question of the expression "emerging or incipient fundamental disequilibrium," his personal view was that its use would not prove very helpful. However, that expression together with other combinations of words could be discussed most fruitfully at the drafting stage.

The Acting Chairman, in response to Mr. Palamenghi-Crispi's final remark, said that he would have thought that, for the time being at least, Executive Directors would find it more convenient to discuss the matter of an advisory committee of the Board of Governors on the basis of a separate paper. At some point in the future it might, of course, prove desirable to consider that question together with that of the reform of the system. At the present stage, however, Executive Directors were merely determining what the next meeting should be rather than anything beyond that.

Mr. Bryce complimented the Economic Counsellor on his excellent paper and expressed his admiration for the elegant paper on symmetrical intervention systems which supplemented it. The Economic Counsellor's paper was so clear and comprehensive that he did not have as many questions about its meaning and intent as he had expected, but he nevertheless had several points to raise. His major concern was that, although the question of capital movements and their financing had been dealt with in paragraph 6 on page 11 of the paper, it had been referred to as a "special" problem and appeared to be regarded as a peripheral feature of the reform of the international monetary system. He wondered whether that view took adequate account of the great magnitude of capital movements to be financed, in view of the size and world-wide nature of the multilateral corporations that were based, or at least partly based, in the United States, and given the behavior of those corporations during the past half dozen years. It seemed to him that it was becoming increasingly difficult to distinguish short-term capital movements from commercial and other transactions, and that the international community was confronted with people of great technical capacity and heavy bureaucratic corporate responsibilities, who considered themselves to have a mission in a field in which the amounts involved and the speed at which they could be moved were very great indeed. Taking that consideration into account, together with the fact that there would inevitably be some nervousness during the next few years about the strength of the U.S. dollar and the nature of the United States economic policies under a regime which provided it with a greater freedom to devalue, he felt that the problem of financing capital movements was of major importance and that the way in which it was dealt with would be central to the working of the reformed international monetary system. In his view, therefore, the problem of capital movements ought to be brought into focus at an early stage of the design of the new system and, to that end, he wondered whether the matter could be explored at a little greater length, in terms of its place in the reform of the system.

The first contingency relating to gold, which was described in the second paragraph on page 14 of the paper, seemed to sidestep an important issue, Mr. Bryce remarked. With that in mind, he wondered whether the Economic Counsellor would be prepared to supplement that paragraph with a short note on the desirability of removing Article V, Section 6, from the Articles of Agreement or, at least, modifying it to provide the Fund with the right to purchase gold but not with the obligation to do so. He made that suggestion because he felt that there should be a clear decision as to whether or not the Fund should be in a position in which it was obligated, in effect, to underwrite the monetary use of gold on a vast scale if the first contingency described by the Economic Counsellor came to pass.

Several questions had been asked at Seminar 72/6, Mr. Bryce recalled, about private or unofficial holdings of SDRs, which were referred to in the second paragraph on page 2 of the paper. He was inclined to share the general reluctance to permit private holdings of SDRs before they had become established as a universal reserve asset and had been invested with the attributes appropriate to that role. However, the thought had occurred to him that if the multicurrency variant of symmetrical intervention was adopted, the smoothness and impartiality of its operation would be greatly facilitated by permitting licensed brokers or dealers to hold SDRs. As he understood the way in which the system would operate, careful and quick judgment would be required to move SDRs in relation to various currencies available on the market in such a way as to ensure that the relative values of those currencies in terms of SDRs were rapidly equated. The profit incentive of licensed brokers or dealers would be perfectly consistent with and, in fact, would contribute to the smooth working of the system, and the Fund would not have to become embroiled in market operations of a highly detailed and skilled nature.

The Economic Counsellor felt that Mr. Bryce's first two questions could best be answered by one-page supplementary papers. The paper, which after all was no more than a sketch, was necessarily brief on many points because it contained brief summaries of larger papers, some of which had not yet even been written. It would certainly be feasible to write short supplementary papers to clarify certain points raised by Executive Directors. Finally, in stating that "special problems" arose in connection with the issue of short-term capital movements, he had meant to imply that "especially major problems" were involved. He agreed with Mr. Bryce about how crucially important it was to the success of the system to find a solution to those problems. Without such a solution, a viable reform package would simply not emerge.

The Deputy Director of the Research Department, addressing himself to Mr. Bryce's final point, understood him to be suggesting an intermediate system somewhere between a market system in which private holders would transfer primary reserve assets and conduct market intervention in currencies, and the system described by the staff in which the transfer of assets and the market intervention in currencies would be conducted by monetary authorities. The merit of his suggestion lay in the fact that it was rather difficult for the monetary authorities to simulate the operations of the market. Indeed, the staff had been hesitating between the kind of solution discussed in the paper and one in which there would, as there was at the present time, be an equal value principle applied to all sales of SDRs and which would leave the direction of the transfers of SDRs to rules and regulations. Clearly, a considerable amount of study and discussion would have to take place before a conclusion could be reached as to which would be the most effective method. He should, perhaps, add that it was not immediately clear to him why, if private intermediaries were permitted to transfer SDRs between monetary authorities, they should not be allowed to complete the operation and carry out the exchange transaction itself.

The General Counsel observed, in response to Mr. Palamenghi-Crispi's question about broad powers to amend, that there were two possibilities. The first was to confer on some organ of the Fund itself the power to amend without requiring the process of acceptance or ratification by members. There were a few institutions in which the plenary organ corresponding to the Fund's Board of Governors had a power to amend without any requirement of acceptance or ratification by members. Such a power to amend could be of two types: one was a limited power to make amendments which did not involve an increase in members' obligations; the other, like that enjoyed by the Board of Governors of the IFC, was unlimited. If there was a flaw in the process, it was that, in the case of the IFC for example, individual Governors might be unable to approve an amendment until they had received legislative authority from their countries. The limitation existed, therefore, not in the charter of the organization concerned but in individual constitutional requirements. The second possibility was one which had been developed in the Fund and that was the power to vary certain provisions, such as those on designation and reconstitution, without the need for amendment. He was not sure, however, how far that process could be taken before the need for amendment was felt. Clearly, the Economic Counsellor's suggestions would have to be considered closely in order to determine what could properly be proposed in the way of variation without amendment. Whether it would be possible to invest the Board of Governors with the power to amend without the requirement of acceptance was doubtful. The suggestion had been made at Bretton Woods but had been rejected.

Turning to Mr. Bryce's question, the General Counsel said that he was strongly in favor of reviewing Article V, Section 6, whatever the status of gold might be in the new system. That provision had been the subject of an unfortunate difference of opinion as to whether the Fund was obligated to purchase gold and it should, perhaps, be clarified by amendment in any event.

The Executive Directors concluded the question and answer phase of their discussion of a sketch of the reform of the international monetary system and agreed to hold a more formal discussion in seminar on March 22.

ROGER V. ANDERSON
Acting Secretary