0404

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

Committee of the Whole on Review of Quotas

Meeting 89/5

10:00 a.m., February 10, 1989

M. Camdessus, Chairman

Executive Directors	Alternate Executive Directors
	C. Enoch
Dai Q.	
	D. C. Templeman, Temporary
	J. Prader
E. T. El Kogali	
E. V. Feldman	
L. Filardo	M. A. Fernández Ordóñez
R. Filosa	S. Appetiti, Temporary
M. Finaish	A. M. Othman
M. R. Ghasimi	O. Kabbaj
G. Grosche	
	E. Kiriwat
B. Jalan	L. E. N. Fernando
	J. Hospedales
	D. McCormack
	C. V. Santos
	I. A. Al-Assaf
	M. Pétursson, Temporary
	D. Marcel
G. A. Posthumus	G. P. J. Hogeweg
C. R. Rye	
	N. Adachi, Temporary

C. Brachet, Acting Secretary
S. B. Woolls, Assistant

<u>Also Present</u>

Exchange and Trade Relations Department: L. A. Whittome, Counsellor and Director. External Relations Department: D. D. Driscoll, R. A. O'Neill. Fiscal Affairs Department: O. B. Makalou. Legal Department: W. E. Holder, Deputy General Counsel; R. H. Munzberg, Deputy General Counsel. Research Department: I. Zaidi. Treasurer's Department: F. G. Laske, Treasurer; T. Leddy, Deputy Treasurer; D. Williams, Deputy Treasurer; P. B. Clark, S. I. Fawzi, A. J. Tweedie. Western Hemisphere Department: S. T. Beza, Director; C. M. Loser. Personal Assistant to the Managing Director: H. G. O. Simpson. Advisors to Executive Directors: M. Al-Jasser, M. B. Chatah, W. N. Engert, J. M. Jones, P. D. Péroz, P. Péterfalvy, G. Pineau, M. A. Tareen, A. Vasudevan, R. Wenzel, J. E. Zeas. Assistants to Executive Directors: J. Heywood, S. K. Fayyad, J. Gold, P. Gorjestani, S. Guribye, M. Hepp, C. Y. Legg, V. K. Malhotra, R. Marino, G. Montiel, D. Saha, J.-P. Schoder, C. C. A. van den Berg, Yang J.

1. NINTH GENERAL REVIEW OF QUOTAS - PAYMENT FOR INCREASED SUBSCRIPTION; SHARE OF DEVELOPING COUNTRIES; AND POSITION OF COUNTRIES WITH VERY SMALL QUOTAS

The Executive Directors, meeting as a Committee of the Whole, considered a staff paper on payment for an increase in quotas (EB/CQuota/89/2, 1/25/89), staff papers on the share of developing countries in the Fund (EB/CQuota/89/4, 1/25/89) and the position of countries with very small quotas (EB/CQuota/89/3, 1/25/89).

The Committee first considered the staff paper on payment for an increase in quotas (EB/CQuota/89/2).

Mr. Prader made the following statement:

> My authorities consider that 25 percent of the subscription payment for the increase in quotas should be made in SDRs, as stipulated in the Fund's Articles of Agreement. During Committee of the Whole on Review of Quotas Meeting 88/8 (9/1/88), Mr. de Groote suggested that the Committee should contemplate an allocation of SDRs as a means of financing the required reserve component of the quota increase. The staff has convincingly shown that, from the standpoint of their effects on the Fund's liquidity position, there is a clear ranking of the various payment methods, and payment of the reserve asset requirement in SDRs is most appropriate. To have payments made in usable currencies would be only a second-best alternative, and many countries might encounter difficulty acquiring the needed reserve assets. Payments in local currency would be the least appropriate option.
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> Because the issue of an SDR allocation has to be judged on its own merits and criteria, it should be seen separately from the decision on the means of payment for the quota increase. Nevertheless, we note that the difficulties associated with the payment of quota increases are indicative of the existence of a global liquidity need, and thus indicate that the basic criterion for an SDR allocation--namely, the existence of a long-term global need--could be met.
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> The larger the quota increase, the stronger the case for a new allocation of SDRs, because a large increase would make the strains on members, stemming from the present insufficient supply of SDRs, more evident and more urgent. As the staff paper noted, "There is no assurance that the arrangements followed under the Eighth Review could fully accommodate a reserve asset payment in SDRs which would be large in relation to the outstanding total of SDRs."

Given the present uneven distribution and inadequate supply of SDRs, it would only be logical to adopt the approach taken in 1978 for the Seventh General Review of Quotas and allocate new SDRs to help finance the quota increase. If the case for an SDR allocation could be accepted under the less serious conditions prevailing in the world economy and with the reserve positions of Fund members at the time of the Seventh Review, the need for a new allocation should be all the more evident in light of the present world economic outlook and the lingering debt crisis, which has depleted developing country reserves, and hindered private lending to the heavily indebted countries.

Although the staff has demonstrated that, from a purely technical point of view, any quota payment can be handled smoothly--even in the absence of a new SDR allocation--technical feasibility is only a secondary criterion in considering the most appropriate method of payment. The principal criterion for choosing a particular method of payment has to be its effect on the Fund's liquidity position.

Among the techniques to facilitate the transfer of SDRs suggested by the staff are a number of trilateral transactions that would enable Fund members to acquire on the same day the amount of SDRs or other reserve assets required to make their respective quota payments. Such techniques, however imaginative they may be, are acceptable only if used to a marginal extent. This argument applies to any technical operations to transfer SDRs through special bilateral arrangements or through the standing arrangements to buy and sell SDRs that have been adopted by a number of Fund members and that could be used to ease members' difficulties in making the quota payment.

The scope of the existing voluntary arrangements for buying and selling SDRs is limited with respect to facilitating the payment of the SDR component of this quota increase. For example, assuming an increase in the size of the Fund to SDR 150 billion, apportioned 60/40 between the equiproportional and the selective elements, one member of my constituency, that currently participates in SDR buying and selling arrangements, would need to use about 70 percent of its present total SDR holdings to pay its own quota subscription.

Of course, in extreme situations, technical solutions could be devised that would permit all members to make their SDR payments by utilizing the SDR holdings of a single Fund member. However, this practice could not seriously be considered compatible with the principles generally associated with an increase in the Fund's capital base. We reject the use of such technical arrangements, and, instead, favor an outright SDR allocation, primarily because if the Fund resorts to techniques of this kind to provide SDRs to its members in the face of an extremely unevenly distributed and inadequate supply of SDRs, it would not only reduce the liquidity effect of payments made in SDRs to that of payments made in local currencies, but it would also amount to official acceptance of the mere pro forma execution of the requirements of an important Fund decision. Such relativistic approaches to Fund policies should be rejected, inter alia, because they make no economic sense from the standpoint of meeting the objectives of a quota increase.

For the sake of honesty, and the reputation of this institution, it seems unwise to indulge in imaginative trilateral technical arrangements to provide SDRs and usable currencies to many Fund members. Therefore, if, regrettably, there should be no consensus in favor of an SDR allocation, it would be better--as a second-best solution--to permit Fund members that do not possess sufficient SDRs or other reserve assets to make their respective payments in local currencies.

The authors of the Articles have imposed on the membership a clear obligation with respect to the reserve asset portion of their quota increases. It is the Fund's responsibility to make sure that appropriate instruments are available to enable its members to discharge their legal obligations.

Mr. Grosche stated that the reserve asset requirement, amounting to 25 percent of the increase in quotas, should be paid in SDRs or in currencies of other members, as specified by the Fund. That procedure was followed under the Eighth Review, it served the Fund's purposes well at that time, and its advantages were clearly explained in the staff paper under discussion.

He had nothing to add to the staff's comments on the financing of the local currency portion of Fund subscriptions, Mr. Grosche remarked. However, he would not support any approach that would give members the option of making the 25 percent reserve asset payment in their own currencies. The issue of an SDR allocation was not of high priority in connection with the Ninth Quota Review. In deciding to make an allocation of SDRs, a finding of a long-term global need to supplement existing reserve assets was required.

Contrary to Mr. Prader's comments, he was not convinced that the actual amount of existing global reserves indicated a shortage, Mr. Grosche continued. Although the heavy concentration of SDR holdings in only a dozen countries posed a problem of a more general nature for the SDR, it should not prevent the payment of the reserve asset requirement in SDRs. It seemed possible to put in place a sufficiently large number of arrangements among Fund members to enable those with insufficient SDRs to acquire them in transactions by agreement. In that connection, he did not share the staff's skepticism about the possible difficulties involved with establishing such arrangements, since the borrowed SDRs would be repaid to the lenders on the same day they were borrowed. In that connection, it was conceivable that certain members' SDR holdings could be used several times and by several needy countries on the same day.

Mr. Rye noted that the various aspects of the quota review were interrelated, and it was very difficult to reach firm conclusions about any of them in isolation. For example, until the size of the overall increase was known, it would not be possible to reach any final judgment about the arrangements that might be necessary to accommodate the required reserve asset payment in SDRs. However, his authorities would prefer--if at all possible--to stick with the arrangements followed under the Eighth Review.

His authorities would have difficulty with the suggestion to link the quota review with an SDR allocation, Mr. Rye commented. The issue of a further SDR allocation was based on a number of much broader considerations and should not be driven by the logistics of quota subscription arrangements. He agreed with the main technical conclusions contained in the staff paper under discussion.

Mr. Enoch made the following statement:

> During Committee of the Whole on Review of Quotas Meeting 88/5 (3/18/88), there seemed to be broad agreement among Directors that 25 percent of the increase in quotas under the Ninth Review should be paid in SDRs, or in currencies acceptable to the Fund. We continue to favor this approach, which closely follows that agreed for the Eighth Review, when, in the event, nearly 90 percent of total reserve asset payments were made in SDRs. During that previous discussion, some Directors considered that there should be a preference in principle for payments made in SDRs, but we have no strong views on this.
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> The main issue addressed in the staff paper under discussion is the question of how reserve asset payments in SDRs can be effected, given that some members will almost certainly not have sufficient SDRs at their disposal to pay the reserve asset portion of their subscription at the time it becomes due. The view taken by Directors in March 1988 (Committee of the Whole on Review of Quotas Meeting 88/3) was that the staff should work out appropriate procedures to arrange for the sale of SDRs to members with insufficient SDR holdings and for members with low reserves in general. This would closely follow the procedures put in place for the Eighth Review, which worked smoothly.
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> However, the staff paper for the current discussion suggests that a more efficient solution might be to have an allocation of SDRs in association with the increase in quotas. The

position of my authorities on this issue is well known--they do not see any case for making an SDR allocation at the present time. Moreover, it is by no means clear that, under the Articles, the need to pay reserve asset subscriptions should be a relevant factor in considering a need to allocate SDRs.

Of course, we recognize that--depending on the overall size of the quota increase--the current pattern of SDR holdings may create some distributional problems. However, as the staff paper notes and as Directors agreed at our previous meeting on this issue (Committee of the Whole on Review of Quotas Meeting 88/3, 3/14/88), these problems can be overcome in a number of ways. First, in the period before the quota increase becomes effective, the Fund could--in executing the operational budget--make transfers in SDRs to members making purchases from the Fund and advise them to make repurchases in currency other than SDRs. Second, as Directors have already suggested, members will retain the right to pay their reserve asset subscriptions in currencies acceptable to the Fund. Third, and most significantly, it is a relatively straightforward task for the staff to put in place arrangements enabling members experiencing difficulties in making their reserve asset payments to acquire SDRs from other members either through transactions by agreement or through borrowing.

In this respect, my authorities are ready in principle to participate significantly in arrangements to buy and sell SDRs. At the time of the Eighth Review, the United Kingdom agreed to make roughly 25 percent of its SDR holdings available for same-day loans and repayments and up to SDR 200 million for outright purchases. We envisage being able to participate in such arrangements on a broadly similar scale in the Ninth Review. I hope that other large member countries will be able to join the United Kingdom in offering these facilities to members facing difficulties in making their reserve asset payments. Contrary to Mr. Prader's statement, but fully in accord with the views expressed by Mr. Grosche, we think that such arrangements are a feasible, and, indeed, relatively straightforward way to effect a quota increase.

Mr. Prader remarked that his argument was that, given the liquidity effect associated with arrangements to buy and sell SDRs and their impact on maintaining the Fund's integrity with respect to capital increases, such arrangements were not desirable--not that they would not be technically feasible.

Mr. Hospedales noted that the Articles of Agreement made it clear that 25 percent of the increased subscription should normally be paid in SDRs. That stipulation was consistent with other key provisions of the

Articles, which were aimed at making the SDR the principal reserve asset in the international monetary system and preserving the Fund's liquidity position. The case for an allocation of SDRs had been made repeatedly by his chair and, in fact, by a majority of Directors on previous occasions. He continued to believe that an allocation of SDRs would facilitate the financing of an increase in quotas, which would be extremely important for a large number of members that did not have sufficient SDRs or reserve holdings. In that respect, he associated himself with the statement made by Mr. Prader. Certainly, an allocation would obviate the need for many countries to access capital markets to make the required subscription payment, and in reality, such access might not be possible. His authorities recognized that arrangements could be put in place to reduce the difficulties that members holding insufficient SDRs--or whose reserve holdings in general were insufficient to pay in SDRs--encountered in trying to make the required reserve asset payments. Nevertheless, they agreed with the staff that, while such arrangements were technically possible, as shown in the appendix to EB/CQuota/89/2, there was no assurance that those arrangements could work as well under the Ninth Review as they had under the Eighth Review, because the amount of SDRs needed for the reserve asset payment in connection with the Ninth General Review might be considerably larger in relation to the total number of SDRs outstanding in 1982. Hence, the approach taken during the Seventh General Review, when an SDR allocation had been made, would be consistent with the Fund's obligations under the Articles of Agreement and should, therefore, be followed in the Ninth General Review.

Mr. Templeman made the following statement:

While we agree that it is useful for the Committee to discuss the three issues currently before it, I must note for the record that my authorities have not yet concluded that any increase in quotas is justified, and my comments on these topics should be understood with that caveat clearly in mind.

Concerning the question of payments for increased quotas, there is a good prima facie case for accepting the normal rule of the Fund, which requires that 25 percent of the quota subscription be paid in SDRs. The fact that SDR payments would tend to strengthen the Fund's liquidity position is important in this connection.

The payment of a quota subscription constitutes an exchange of assets and does not reduce a country's reserves. While it does not usually result in a budgetary outlay--and would not for the United States, which would however require from the U.S. Congress a budget authorization and an appropriation for the full amount of any increase in the U.S. quota subscription--some of these financial distinctions are not easy to explain to legislators. My authorities know from past experience that obtaining Congressional authorizations and appropriations is not easy; this would probably be particularly true at the present stage, given that the U.S. budget deficit is a serious and sensitive economic and political issue.

We recognize that payment of 25 percent of the quota increase in SDRs would lead to a major redistribution of SDRs and some change in the composition of existing official reserves. Although the staff paper highlights the considerable extent to which current holdings of SDRs have become heavily concentrated in the hands of the industrial countries, the Executive Board has discussed this phenomenon in the past, and it would not be appropriate to re-examine the matter in depth for the current discussion. However, the resulting scarcity of SDR holdings among the large majority of member countries can be seen as an unfortunate impediment to payment for any possible quota increase.

Therefore, some arrangements would clearly be needed to make SDRs available to many members--if a quota increase were agreed and if 25 percent of the payments were to be made in SDRs. In this connection, a variety of possible arrangements to facilitate the transfer of SDRs are outlined in the staff paper, and a combination of those arrangements could be used. Assuming that a quota increase were agreed, my authorities would be willing--as in connection with previous quota reviews--to consider ways in which some U.S. holdings of SDRs might be made available to other members for quota payments, either through voluntary transfer arrangements or through same-day borrowing and repayment agreements. However, at this stage we are not in a position to make any commitment as to the types or amounts of such transactions that might be possible. Whether or not special arrangements would result in a sufficient reallocation of SDRs to permit payment of 25 percent of the quota increase in reserve assets would, of course, depend partly on the size of the overall quota increase. In this connection, a modest quota increase would present less of a problem.

Finally, we are not sympathetic to the idea of making a special SDR allocation to facilitate SDR payments for any quota increase. An SDR allocation must conform to the criteria set out in the Articles, and the Executive Board has discussed the need for an SDR allocation repeatedly without reaching a consensus.

The Chairman noted that Directors were familiar with the difficulties the U.S. Administration faced in obtaining appropriations from the U.S. Congress. However, such appropriations had nothing to do with the U.S. budget deficit.

Mr. Templeman said that his point was that Directors should not conclude that, because no budgetary outlay was required in connection with a quota increase, the U.S. Administration would not have difficulty in obtaining the necessary appropriation from Congress. Such distinctions were very subtle, and, from previous experience, the U.S. Administration had found that many of the people involved with legislation in the United States either could not or would not understand the distinction between payment of the U.S. subscription to the Fund and other budgetary matters.

The Chairman remarked that no doubt a similar situation existed with respect to the need to raise taxes owing to the increase in the U.S. budget deficit.

Mr. Jalan stated that his authorities would support arrangements, similar to those agreed under the Eighth Review of Quotas, to facilitate the transfer of SDRs. In addition, they also supported Mr. Prader's suggestion to link the issue of allocating SDRs with the quota increase under the Ninth Review. The arguments put forward by Mr. Prader concerning the technical and practical aspects of transfer arrangements merited further consideration, and they certainly strengthened the case for a new allocation of SDRs.

Mr. Kiriwat said that, like many other Directors, he preferred the use of arrangements similar to those made in connection with the Eighth General Review of Quotas. Payment of 25 percent of the quota increase in SDRs, or other convertible currencies acceptable to the Fund, would be beneficial to the Fund's liquidity position. At the same time, arrangements would have to be made, as for the Eighth General Review, to allow members with inadequate reserves to participate in the quota increase through a simultaneous use of their enlarged reserve tranche positions.

Mr. Marcel stated that his authorities agreed with other Directors that 25 percent of the quota increase should be paid in reserve assets.

With respect to the possible allocation of SDRs in connection with the Ninth General Review, the view indicated by his chair on previous occasions was that there was an overall liquidity shortage in the international monetary system, Mr. Marcel said. However, the payment of quota increases had no bearing on the net liquidity position of member countries. As the staff had emphasized, such payments amounted to a transfer of assets. Moreover, the purpose of any quota increase was not to improve the liquidity position of member countries, but to enhance their access to Fund resources.

Nevertheless, in light of the amount of SDRs that had been allocated in the past, his authorities agreed with the staff that the payment of 25 percent of the quota increase in SDRs would dramatically reduce the amount of SDRs currently held by countries and undermine the role of the

SDR as a significant international asset, Mr. Marcel continued. That fact clearly indicated that the amount of SDRs currently available was not in line with the needs of the international monetary system.

As to the immediate issue of payments for the quota increase, his chair supported the staff's suggestion to adopt the same arrangements to facilitate the transfer of SDRs that were agreed in connection with the Eighth Quota Review, so that countries with insufficient SDR holdings could borrow them and then make repayments by drawing on their new reserve tranche positions, Mr. Marcel concluded. However, it should be kept in mind that such an approach would not avoid a reduction in the amount of SDRs held by member countries. The Committee should certainly examine the issue of SDR holdings at a later stage, since that was an urgent matter.

Mr. Ghasimi said that the payment of 25 percent of the quota increase in reserve assets would be most appropriate. With respect to the media of payment, he agreed with the staff about the consequences of making payments for the reserve asset subscription payment in SDRs. Indeed, as the staff paper clearly showed, reserve asset payments made in SDRs would enhance the Fund's liquidity position, serve as a suitable guide in making future SDR allocations, and assist in the redistribution of the present stock of SDRs.

The proposed modalities for securing the required SDRs for those member countries with insufficient reserve assets, as described in the appendix to EB/CQuota/89/2, seemed both practicable and desirable, Mr. Ghasimi commented. However, as the staff had noted, there was little assurance that the existing stock of SDRs would be sufficient to accommodate the potential demand for SDRs. Furthermore, confining the media of reserve payments to SDRs would reduce the flexibility of reserve asset payments. In the light of those considerations, payment of 25 percent of the quota increase could best be made in any combination of SDRs and other currencies specified by the Fund.

Mr. Adachi remarked that his chair had difficulty in finalizing its position on the payment of increased quotas, because the size and distribution of the quota increase had not yet been agreed. However, it would be useful for the Committee to proceed with its work on the Ninth General Review of Quotas and reach whatever agreements were possible, even if only tentatively. Therefore, he would present the current position of his authorities, although they would reserve their final position until the size and distribution of the quota increase was decided.

The two most important issues under discussion were the appropriate media of reserve asset payments and the question of making an SDR allocation in conjunction with the quota increase, Mr. Adachi noted. With respect to the reserve asset payments, his authorities considered that the practice followed under the Eighth Quota Review should be repeated under the Ninth Review. Under the Eighth Review, reserve asset payments were made not only in SDRs, but also in dollars, pounds sterling, deutsche mark, and yen. While he agreed with the staff that the liquidity effects of reserve asset payments made in SDRs were greater than those resulting from payments made in usable currencies, he did not expect that the liquidity effects of reserve payments made in a combination of SDRs and currencies acceptable to the Fund would fall short of those resulting from payments made only in SDRs.

If the Committee agreed that the reserve asset payment should be made only in SDRs, the Fund would have to make arrangements to enable all members to pay in SDRs, Mr. Adachi considered. However, as the staff had pointed out, the sale of SDRs by the Fund to members with insufficient SDR holdings would be the equivalent of having the reserve asset payment made in usable currencies in the first place. For that reason, he did not consider that much benefit could be gained from a mandatory payment of 25 percent of the quota increase in SDRs.

Nevertheless, there was a possible need to arrange for some members to borrow the amount of SDRs needed to pay the Fund, as was the case in the Eighth Quota Review, Mr. Adachi continued. At the present stage, he would say that, if necessary, his authorities would be ready to consider joining in transactions that would help members holding insufficient foreign assets to pay the Fund.

As to making an SDR allocation in association with a quota increase, on previous occasions, his chair had expressed the view that a further study of the concept and measurement of international liquidity, an assessment of the long-term global need, and an examination of feasible measures to improve the SDR's role would be needed as an essential basis on which to consider an SDR allocation, Mr. Adachi recalled. The issue of an SDR allocation should be considered within the overall context of the role of the SDR in the international monetary system, and the Board was scheduled to discuss that issue in the near future.

Mr. Finaish said that he could go along with the staff's suggestion that 25 percent of the quota increase should be paid in reserve assets, as in the past two quota reviews. Nevertheless, he would have liked the staff to give a more explicit explanation of the liquidity effects and other implications of paying a lower portion of the subscription payment in reserve assets. The 25 percent reserve asset requirement was set in the Articles not only as a normal rule, but also as a ceiling, and the requirement that the balance of the quota increase, amounting to 75 percent, had to be paid in local currency was set as a floor. Since it was left to the Board of Governors to decide whether a lower reserve asset portion of the increase would be appropriate, it would have been useful for the staff paper to indicate more clearly the merits of maintaining that ceiling, although the point was mainly one of presentation.

As to the media in which the reserve asset payment should be made, it was clear from the staff paper that the use of SDRs would be advantageous to the Fund from the standpoint of preserving its liquidity position, Mr. Finaish remarked. It was also clear that, if payments were to be made in SDRs, arrangements similar to those made in connection with the Eighth Quota Review would have to be made in order to enable members to acquire needed SDRs. However, to the extent that even such arrangements might not be sufficient, two obvious options would be either to agree on a modest SDR allocation or to allow payments to be made in other currencies. The preference of his authorities was clearly the former, given their position on SDR allocations in general. However, if an agreement on an SDR allocation proved impossible, his authorities would be open to the possibility of allowing members to make the reserve asset payment, in whole or in part, in the currencies of other members as specified by the Fund.

Mr. Hogeweg remarked that his authorities supported the staff's preference for a payment in SDRs amounting to 25 percent of the quota increase. That was the normal rule of the Fund as stated in its Articles of Agreement, and it was the optimal payment method for the Fund's liquidity position.

The staff paper under discussion described the mechanisms that were used in the Eighth Review to accomplish the redistribution of SDRs that was necessary to permit all members to make the reserve asset payment, Mr. Hogeweg noted. However, it was important to note the staff's warning that there was no guarantee that those mechanisms would be sufficient in connection with the Ninth General Review of Quotas. The amount of SDRs needed for reserve asset payments under the Ninth Review was likely to be larger, relative to the existing stock of SDRs, than was the case at the time of the Eighth Review. However, the Fund should try to use those mechanisms to their fullest extent. As a precaution, the Fund could open the possibility--in line with the decision made during the Eighth Review--for payments to be made in the currencies of other members, specified by the Fund, with those members' concurrence.

Although his chair supported in principle moderate annual allocations of SDRs as a means of contributing to the maintenance of the allocation mechanism and avoiding possible future problems in reserve supply, his authorities did not consider that the need of members to make payments for quota increases should be an argument for a special SDR allocation, Mr. Hogeweg commented. The payment for a quota increase was a one-time event, and it did not increase the long-term global need for reserves. As he had noted on previous occasions, it should be possible to overcome the technical problems associated with making quota payments in SDRs without making an allocation at the present time.

Mr. Santos said that a reserve asset payment in SDRs, amounting to 25 percent of the increase in quotas, would clearly result in a greater improvement of the Fund's liquidity position than would a payment in usable currencies. Arrangements for the settlement of the reserve asset requirement in SDRs, along the lines followed in the Eighth General Review, would be needed. However, given the relatively small stock of

SDRs in relation to the size of the quota increases expected by many member countries, including those in his own constituencies, such arrangements would prove insufficient, because the amount of SDRs needed could not be fully accommodated by the stock presently available. While he agreed with the staff that no direct link necessarily existed between an increase in quotas and an SDR allocation, he considered that a package that would combine both an SDR allocation and arrangements to facilitate the transfer of SDRs should be considered as a means to ease the difficulties associated with the payment of the reserve asset portion of the quota increase in SDRs. Such an approach would help to address the liquidity needs experienced by a large portion of the membership, and it would serve the interests of the Fund.

Mr. Filosa noted that the staff had stated that the payment of the quota increase in SDRs would have a clear advantage in terms of the effects it would have on the Fund's liquidity position. In principle, he agreed that such a payments requirement should be pursued, in line with the normal rule stated in the Articles of Agreement. Therefore, his Italian authorities favored a payment of 25 percent of the quota increase in SDRs.

However, if the Fund decided to follow the normal rule, it would encounter, as a side effect, a very abnormal redistribution of SDRs among members, given the present low level of SDR holdings and their extreme concentration in a limited number of countries, Mr. Filosa considered. The greater the increase in the size of the Fund, the more pronounced the shift in the distribution of SDRs would be. Even though such a redistribution of SDRs could be corrected, it was important to note that exchange rate risks and interest rate costs could not be avoided under arrangements between the Fund--or members holding a sufficient amount of SDRs--and members that needed to borrow SDRs. The staff paper stressed the need for cooperation between the Fund and its members to smooth the arrangements needed to enable countries facing difficulties to make their reserve asset payments. In that respect, his Italian authorities were ready to cooperate in the process of transferring SDRs as smoothly as possible.

However, as the staff had indicated, there was no assurance that such arrangements would work as well under the Ninth Review as they had under the Eighth Review, Mr. Filosa noted. Therefore, it was appropriate to raise the question of allocating SDRs in connection with the Ninth Review. Although an increase in quotas did not depend on an allocation of SDRs, he favored such an allocation for the reasons that were clearly spelled out in the staff paper. An appropriate amount of SDR allocations would help to reduce the risk of mismatching that could arise in meeting quota payments, and it would produce positive effects on the Fund's liquidity position, which was the most important consideration. In that connection, he agreed with Mr. Hogeweg that SDR allocations should be made annually in small amounts, and that large allocations should be made only under unique circumstances.

Mr. Al-Assaf said that, as his chair had indicated on previous occasions, his authorities had not yet taken a firm position with respect to the media of payment for the reserve asset requirement, amounting to 25 percent of the quota increase. However, for the reasons outlined in the staff paper, especially those concerning the liquidity impact of various modes of payment, he tended to go along with the proposition that that payment should be made in SDRs. Surely the staff would be able to work out arrangements, similar to the one illustrated in the appendix to EB/CQuota/89/2, to enable members with insufficient SDRs to acquire them to pay the Fund.

His chair did not have a strong position on the issue of allocating SDRs in association with an increase in quotas, and it could go along with the majority view, Mr. Al-Assaf stated. Obviously, the need for an SDR allocation to facilitate the reserve asset payment would greatly decrease if a moderate quota increase--which was the well-known preference of his chair--was agreed.

Mr. Pétursson commented that the Nordic countries considered that it would be appropriate to have 25 percent of the quota increase paid in SDRs, or other currencies specified by the Fund. His authorities understood, however, that the quota increase--particularly if it was large--might impose payment constraints on some members, owing to the current concentration of SDR holdings. Therefore, they could support an arrangement that would provide flexible utilization of usable currencies, facilitate the borrowing of SDRs from other members, and the sale of the Fund's SDR holdings, if required. Moreover, if necessary, the Nordic countries would be prepared to support a moderate new allocation of SDRs to accommodate payment of the quota increase.

Mr. Feldman stated that his chair supported the staff proposal on the size of the reserve asset payment, amounting to 25 percent of the increase in quotas, as that percentage was specified in the Articles of Agreement.

Furthermore, his authorities could go along with the proposal that the reserve asset payment should be made in SDRs, since that choice maximized the liquidity effects of the quota increase, Mr. Feldman continued. However, he considered that the proposal to have payments made in SDRs should not be considered in isolation from the arrangements that would be necessary to facilitate such payments, not only for those members with insufficient SDR holdings, but also for members with insufficient reserves in general.

In that connection, the small amount of SDRs in existence and the high concentration of SDR holdings in only a few countries clearly reinforced the arguments that had been presented in several previous discussions on the need for an allocation of SDRs, Mr. Feldman concluded. The quota increase was an additional justification for an allocation of SDRs, which would facilitate the reserve asset payment of the quota increase and help to promote the SDR as an important international reserve asset.

Mr. El Kogali commented that he could understand the preference of Directors for using SDRs to make the reserve asset payment, amounting to 25 percent of the increase in quotas. However, he considered that such payments should be facilitated by an allocation of SDRs as in the Seventh Review of Quotas.

Mr. Dai said that he agreed that as a normal rule, 25 percent of the increased quota subscription should be paid in SDRs. For members with insufficient SDR holdings or insufficient reserves in general, the same arrangements that were made on the occasion of the Eighth General Review of Quotas could be made in connection with the present review. However, as the staff had pointed out, the total amount of SDRs in existence might be small in relation to the amount that would be needed to make reserve asset payments, particularly as many members were experiencing shortages of reserves in general. Therefore, an allocation of SDRs should be considered in association with an increase in quotas. Since the Board planned to discuss the role of the SDR in the international monetary system at a future date, he would not elaborate on the allocation issue at the present stage. However, he supported the initiative to make an allocation of SDRs in connection with the Ninth Review of Quotas.

Mr. McCormack remarked that his authorities had not yet taken a definite position on the payment for increased quotas. However, at the present stage, their preference was to follow the same procedures that were used in association with the Eighth Review, which permitted payment of the increase in quotas to be made in SDRs, currencies acceptable to the Fund, or in a combination of SDRs and acceptable currencies. Admittedly, the Fund's liquidity position could best be preserved if payments for 25 percent of the quota increase were made in SDRs. However, it was clear from the staff paper that such a method of payment could greatly disrupt the management of individual members' reserves, indicating a need for agreement on a new SDR allocation. However, his authorities did not consider that such an allocation was warranted at the present time.

He agreed with the staff and other Directors that, if the reserve asset payment in SDRs was agreed, arrangements to enable members with insufficient SDRs to acquire them in order to pay the Fund would be needed, and could be put in place, Mr. McCormack commented. The Fund could also assist members with insufficient reserves in general by helping them to borrow SDRs from other members. The loans could be repaid on the same day with proceeds derived from drawings on the reserve tranche positions created as a result of the payments for increased quotas.

Mrs. Filardo said that her chair still did not have a position on the payment of increased quotas, because it would depend on the future size of the Fund that was agreed. However, her authorities' preference was to follow the methodology applied during the Eighth Review of Quotas. Like Mr. Feldman, she considered that the increase in quotas was an additional reason for an allocation of SDRs.

The Deputy Treasurer remarked that, with respect to Mr. Prader's question about whether the Fund could allow members with very low reserves to make payments for the reserve asset requirement in local currency, the Articles of Agreement made no provision for distinctions to be made between members, but made it quite clear that payments should be made on the same basis by all members. Therefore, any distinction between members was not permissible. Of course, the arrangements that had been followed in the Eighth Review, which were outlined with very few modifications in the staff paper under discussion, had provided for 100 percent mitigation of the reserve asset payment, because, as soon as the payment for the increased quota was made, members--regardless of whether or not they had paid the reserve asset requirement through borrowing--could, based on balance of payments need, make an immediate drawing on their new reserve tranche positions.

A number of Directors had noted the staff's indication that some difficulties could arise in following the same arrangements that were made for the Eighth Review, the Deputy Treasurer continued. Although the offer in principle made by some large holders of SDRs to participate again in arrangements to facilitate the transfer of SDRs was welcome, it could be difficult to accommodate the large number of members that had insufficient SDR holdings who wished to make payments in a short period. Therefore, a problem could arise in accommodating transfer arrangements in a given short period. The period of payment for the increased quota subscription, following the date of a member's consent, had traditionally been 30 days. Given the number of members that were faced with low SDR holdings or low reserves in general, it might be necessary to consider the length of time they might require to complete such transfer arrangements in order to pay the Fund. In that connection, consideration could be given to extending the period for payment, after the date of consent for the Ninth Review, even though such an extension would be unfortunate in that it would delay the coming into effect of members' new quotas, and it would deprive the Fund of additional quota assets during the extended payment period.

The Committee then considered staff papers on the share of developing countries in the Fund (EB/CQuota/89/4, 1/25/89), together with a staff paper on the position of countries with very small quotas (EB/CQuota/89/3, 1/25/89).

Mr. Grosche recalled that, with respect to the share of developing countries in the Fund, on previous occasions his chair had indicated its view that the distribution of quota increases should be based on uniform methods. Thus, an increase in quotas should not be constrained by the objective of maintaining the shares in voting power or in quotas of particular groups of members. For the present discussion, the staff had not put forward any compelling arguments that would lead to the conclusion that the present distribution of voting power should be cast in cement. The actual quota and voting shares of the developing countries, and in particular, of the countries with very small quotas, were already higher than was called for by their relative economic sizes, as measured by the quota formulas. Therefore, his authorities were reluctant to support special treatment of the shares of either the developing countries in general or the members with very small quotas.

As the staff had pointed out, a special policy for countries with very small quotas would likely lead to new distortions not only within the group of countries concerned, but also in relation to other members, Mr. Grosche noted. A policy of individual quota adjustments should be avoided, unless it was based on members' relative economic positions. Also, the modifications made in 1963 to the Bretton Woods quota formula and the introduction of the multiformula method of calculating quotas went a long way toward mitigating the problems of smaller members with relatively open economies.

Mr. Prader said that his authorities recognized the potential negative consequences of a quota increase on the developing countries and the countries with very small quotas, with respect to their share of quotas in the Fund and, in particular, their voting rights. Since voting rights had an important bearing on members' perceptions of the Fund as a cooperative institution, it was appropriate to consider mechanisms that would allow special treatment of the most seriously affected countries, in particular members with very small quotas. At the same time, care should be taken to construct mitigation schemes for those countries in a way that would neither lead to new distortions in the quota structure nor weaken the principle that quotas should reflect members' relative positions in the world economy. Therefore, he could agree to the adoption of rounding techniques similar to those used in the Eighth Quota Review for the countries with the smallest quotas. The resulting additional overall quota increase for those countries would be marginal and within acceptable limits.

With respect to the introduction of various mitigation schemes for the quota shares and the voting power of developing countries, Mr. Prader concluded, his authorities remained open minded, and could agree to any of the proposed schemes.

Mr. Rye made the following statement:

> Like the issue of payments for increased quotas, questions surrounding the share of the developing countries in the Fund and the position of countries with very small quotas cannot be divorced from the size of the quota increase and the nature of its distribution.
>
> The staff paper on the share of developing countries in the Fund represents an earnest attempt by the staff to examine the concerns of developing countries, while avoiding the use of predetermined constraints based on artificial country classifications. My Australian authorities consider that any institutionalization and discriminatory treatment of member groups

should not be countenanced. However, there is a real problem with respect to the countries with very small quotas of under SDR 10 million.

The Fund should distinguish between the two issues of voting rights and access. For the small countries in my constituency, voting is not a significant consideration. However, I recognize the concerns of other Directors, and I would not be opposed to the consideration of some simple, nondiscriminatory device, along the lines advanced in EB/CQuota/88/7, aimed at addressing those concerns. My authorities consider that the present structure of the Executive Board is appropriate, and should not be put at risk. However, the issue of voting shares should be discussed at a later stage of the Ninth Review of Quotas, so that a debate on that subject will not add to the issues already before the Committee, which are delaying the completion of the review.

Turning to access limits, neither of the staff papers before us really addresses the question of whether the access needs of smaller members justify special treatment for them, and it is difficult to see that there is any general problem of access for the vast majority of Fund members, at least in principle. Developments in the access policy and the establishment of special facilities should have mitigated the concerns of most smaller Fund members. For example, the recent establishment of the structural adjustment facility and the enhanced structural adjustment facility has provided heavily subsidized resources to low-income members, many of which are holders of small quotas. Recent developments with respect to the enlarged access policy, which the Committee will discuss at a later date, are relevant to the question of the overall amount of access available to members.

Nevertheless, there still seems to be a real problem with respect to the countries with very small quotas. Certainly, that is the case with the small island countries in my constituency. They see the Fund as a very useful and indispensable source of technical assistance, but as irrelevant when it comes to issues of financing. That point, and a plea for special consideration was put forward during the Annual Meetings by the Governor of the Fund for Kiribati, who was also speaking on behalf of the Solomon Islands, Vanuatu, and Western Samoa, when he said:

> Turning to the Fund, we are the smallest and poorest members, and we have the smallest quotas. We do not object to being the smallest, but our present quotas are so small that they almost might not exist. Our potential access to Fund resources should be big enough to play a significant

> part in our consideration of adjustment policies. To achieve that, when the Ninth Review of Quotas takes place, we need a tripling of the small island quotas, or the addition of a flat sum of, say, SDR 10 million to each quota (whatever happens to the total capitalization of the Fund).

Although that statement was very subjective, it contained some relevant objective considerations, as I hope to show, and it should not be lightly dismissed. If any sector of the membership believes that the Fund's main purpose is essentially irrelevant to them, that ought to be a matter of concern to this Committee. It should at least warrant open-minded consideration.

There are some points that support giving some form of special treatment to the members with very small quotas. First, the small quota policy of the 1950s has left a legacy of discontinuity in the quota structure of the Fund. The group of countries that are somewhat larger than those under consideration is in a substantially better position with respect to the relationship between the size of their quotas and the size of their GNP, trade, and other economic indicators. Therefore, it would certainly be logical to extend some kind of special treatment to the members at the bottom of the quota list. Second, the very small countries with relatively primitive economic structures suffer some disadvantages that are not adequately reflected in their calculated quotas and that probably could not be captured by any objective formula. Such disadvantages include the lack of a diversified export sector, and hence an extreme vulnerability to the vagaries of international demand and natural disasters, which is compounded by scale limitations, inadequate capital and skilled labor, and geographical isolation. In addition, these very small economies are often characterized by large sectors at subsistence standards of living, and they have limited scope to adjust in the face of external shocks. For most of them, access to commercial financing, if it exists at all, is highly constrained.

These considerations have not been adequately addressed in the staff paper. Casual observation suggests that there is indeed an unusual degree of variability in the external accounts of many very small Fund members. I recently examined the annual variations in export proceeds and the current account balances of the Solomon Islands, Seychelles, Vanuatu, and Western Samoa for the period 1982 to 1987. Of the 23 exports for which figures were available, export variability exceeded 20 percent for 16 exports, and 40 percent for 8 exports. The current account balance varied by more than 40 percent from the preceding year on no less than 17 occasions, and by more than

100 percent on 7 occasions. I sincerely doubt whether the quota formulas make adequate allowance for this kind of variability.

I am not satisfied with the staff's suggestion to use rounding schemes for the countries with very small quotas, as adopted in the Eighth Review. Although such schemes would undoubtedly be better than nothing, they do not go far enough, and they create new anomalies, as demonstrated in the case of Seychelles. Seychelles is in a particularly poor quota position, which was made worse by the Eighth Review, and which was noted in the staff paper as foreshadowing a possible application for a special quota adjustment in connection with the Ninth Review to address the issue of countries with very small quotas in general.

It might be helpful to apply a multiplier to all countries with very small quotas to bring them into a better relationship with the group of countries just higher up from them on the quota scale. I have not had time to calculate what the appropriate multiplying factor should be, but, no doubt, the staff could help in formulating it.

If the Committee cannot agree to using such a multiplying factor--or perhaps in any case--the Fund should do something to rectify the structure of very small quotas. Some of the very small members have actual quotas that are far short of their calculated quotas, in contrast with other small members for which the relationship is much more in line. Of course such differences occur throughout the membership, but they seem to be a lot more pronounced and a great deal more significant for the very small member countries. At a later stage in this quota review, after other decisions have been made, the Committee should examine these relativities and consider making special adjustments for the very small members whose actual quotas remain most inadequate in relation to their calculated quotas.

Mr. Hospedales said that his authorities remained deeply concerned that, in the absence of any mitigation scheme, the quota and voting shares of developing countries would continue to be reduced in the Ninth General Review. Those declines would follow the declines that had occurred under the Eighth General Review. Moreover, the decline in quota shares would come at a time when there was an established and unquestionable need for additional liquidity by the Fund's membership to ensure the success of the growth-oriented adjustment programs that were currently being implemented in many countries. The commensurate decline in voting power would be clearly inconsistent with the need to ensure equitable and fair representation in the decision-making process of the Fund, especially in the light of its international cooperative character. Therefore, his authorities considered that the decline in the quota share and voting power of developing countries as envisaged under all mixes of quota calculations should be avoided. In that connection, mitigation schemes could be used to address the needs of countries with very small quotas.

Mr. Templeman made the following statement:

Concerning the shares of developing countries in the Fund, it is our firm position, which is shared by most Directors, that a change in the number of basic votes would not be acceptable and that the distribution of any quota increase should be based on uniform methods and should not be artificially constrained to maintain the shares in quotas or voting power of particular groups of members. Indeed, we do not see any legitimate justification or purpose for deviating from the basic policy of the Fund to make quotas reflect members' relative economic positions. The staff correctly raises this fundamental question in EB/CQuota/89/4, but then it seems to conclude that some form of mitigation of the effects of this policy may, nonetheless, be justified.

If the staff's primary concern is that a reduction in relative quotas would have an adverse effect on access or on the ability of members to present their views within the Fund, there are other ways to deal with such concerns. Such methods could include implementing an appropriate degree of flexibility in applying the access policy and considering ways to ensure the adequate representation of members in the Board.

As the staff points out, the many alternative ways in which it has calculated the distribution of a quota increase would result in a considerable range of effects on the relative size of the developing countries' shares of quotas and votes. These results are one factor that should be considered in reaching any final decision about a quota increase, in particular in connection with the selection of a method of quota distribution. However, it should be noted that the developing countries already have a share of voting power that exceeds their quota share. We would not support distributing any equiproportional component of a quota increase based on voting shares instead of quota shares, and we are inclined to believe that the use of mitigation schemes, which are appropriately constrained to avoid the creation of additional distortions, would not noticeably reduce the downward impact on quotas and voting shares resulting from the use of a uniform formula in quota distributions.

I will make a few preliminary points indicating the initial direction of my authorities' considerations on the position of countries with very small quotas, a subject which will, ultimately, have to be part of any overall quota package, if a decision is made in favor of a quota increase.

In general, we do not support the idea of making special arrangements for groups of member countries. Instead, quotas should accurately reflect the relative economic positions of members--whatever their size. After some experimentation with minimum quotas and a very small quota policy, the Fund has recently adopted an approach of setting quotas for new members based on their individual situations, and the staff paper says that "the combined quota share of very small new members has come to bear a relatively close relationship to their share in calculated quotas."

At the same time, the staff indicates that members with very small quotas now have lower than average ratios of actual quotas to calculated quotas and of actual quotas to external imbalances compared with the non-oil developing countries as a group. On the other hand, their averages are very close to the average for all member countries. The staff concludes that it would be reasonable to consider a special adjustment for these members, as on the occasion of the Eighth General Review. We are not prepared to accept this view, but we would be willing to keep under consideration the possibility of making a special adjustment for these countries in the form of a modest upward rounding of quotas, provided that several caveats are respected. These caveats include assurances that special adjustments for members with very small quotas would not result in actual quotas exceeding their calculated quotas, in an increase of any existing disparities within this group of members, by adding to a current excess of actual quotas over calculated quotas. In addition, such special adjustments should not be allowed to cause distortions in the structure of quotas for members whose actual quotas are already somewhat in excess of the quotas of countries with very small quotas. The impact of special adjustments on any overall increase in quotas should also be very small.

Finally, we concur with the staff that there is no strong case, or even any reasonable case, for reinstituting a small quota policy or for establishing a minimum quota.

Mr. Jalan noted that the issue concerning countries with small quotas raised two problems. The first was that, because small countries had small quotas, they faced special problems, as Mr. Rye had pointed out. The second problem was that the small quotas were expected to get even smaller, because the calculated quota shares of a number of countries would decline by about 30-40 percent under the Ninth General Review of Quotas.

The present quota formulas did not measure what Mr. Templeman had referred to as the relative economic positions of the countries eligible to use the enhanced structural adjustment facility in an appropriate and equitable way, Mr. Jalan considered. He had previously referred to the favorable rates of growth that had been achieved by those countries, but despite their impressive growth rates, a number of those countries would be facing reductions in their quota shares. For example, the rate of growth achieved by Cape Verde over the past four years amounted to about 6.5 percent, but its quota share was expected to decline by 40 percent under the Ninth Review. Thus, the Committee should examine the way in which the formulas used to calculate quotas had worked to reduce the quotas of small or poor countries even though their economic performance had not necessarily declined. He did not want to re-examine the issue concerning the appropriateness of the present quota formulas at the present stage, but the situations of the countries with small quotas should certainly be taken into account in considering different distribution techniques for the increase in quotas.

Earlier in the discussion, he had suggested that the preponderant part of the quota increase should be distributed equiproportionally in order to mitigate the impact of the somewhat odd results of the quota formulas, under which the poorer countries would lose more than other countries, despite their healthy aggregate rate of growth, Mr. Jalan concluded. He supported the staff's proposal to use rounding techniques in connection with the Ninth General Review of Quotas.

Mr. Kiriwat commented that it was difficult to take a definite position on the issues concerning the share of developing countries in the Fund before a decision was reached on the size and distribution of an increase in quotas. However, it was evident that a further decline in the quota shares of developing countries would take place under the Ninth General Review of Quotas unless remedial action was taken. On previous occasions, the Committee had discussed two ways in which the quota shares of non-oil developing countries could be preserved--one was through an increase in basic votes, and the other was by constraining quota calculations. There were practical difficulties associated with the proposal to increase the basic votes, and many Directors maintained the view that quota increases should be based on uniform methods and should not be constrained to maintain the voting or quota shares of particular groups of members. Therefore, the schemes proposed in EB/CQuota/89/4 were most welcome, because they could at least partially mitigate the reduction that would take place in the quotas as a result of the Ninth Review.

As to the position of the countries with very small quotas, it should be noted that the adverse impact of the overall increase in quotas would fall relatively more heavily on the voting power of the countries with very small quotas than on others, given the sharp decline in the relative importance of basic votes in determining voting power, Mr. Kiriwat said. However, as the staff had indicated, the current payments of very small quota countries, which could be considered a useful indication of their potential need for Fund resources, were relatively low, both in terms of the Fund membership as a whole, and particularly in relation to other developing countries, especially those with relatively small quotas. On that basis, he was comfortable with the special rounding procedures that had been used for the countries with very small quotas in connection with the Eighth General Review.

Mr. Marcel stated that his authorities were reluctant to take a definite position on the share of developing countries in the Fund and the position of countries with very small quotas, because the Committee could not reach any conclusions on those matters until an agreement was reached on the size and the method of distribution of the quota increase.

His authorities shared the concern expressed by other Directors about the implications of the current quota formulas for the position of developing countries, Mr. Marcel commented. However, they were reluctant to support the introduction of any differentiation between groups of members, in particular between industrial and developing countries. Such a division of the membership would run counter to the very nature of the Fund as an institution in which each member could alternately be debtor or creditor. Therefore, his chair could not support any use of predetermined constraints on quotas based on country classifications.

In any case, schemes aimed at mitigating the possible reduction in the relative power of developing countries should be calculated on the basis of uniform techniques and should have a very limited impact on the distribution of quotas, Mr. Marcel remarked. Nevertheless, a more precise view of the future size of the Fund and method of distribution for the quota increase was needed before the Committee could reach any decisions concerning individual members or groups of members. In that connection, it would be useful for the staff to prepare further calculations based on different sized increases and various methods of distribution.

The best way to mitigate any unfavorable consequences on the access of developing countries to Fund resources would be, first and foremost, to adequately maintain both access limits and the access policy, Mr. Marcel considered.

His authorities did not have a strong position with respect to the countries with very small quotas, Mr. Marcel stated. The staff paper made it clear that the quota shares of members with very small quotas bore, on average, a closer relationship to their shares in calculated quotas than the shares of most other developing countries. In addition, the current payments of countries with very small quotas, which indicated their possible need for future access to Fund resources, were relatively low, both in relation to the Fund membership as a whole, and, in particular, in relation to other developing countries. In that connection, the basic question was whether or not those countries were expected to have a greater need for access than other members. Therefore, his authorities wondered whether the problems associated with the countries with very small quotas could be addressed simply by implementing a flexible access policy.

Mr. Ghasimi made the following statement:

During our previous discussions on the size and techniques of distribution for an increase in quotas, this chair has stated its position that, if at all possible, the Fund's size should be doubled and that it would be most appropriate to have the larger portion of the increase distributed on a selective basis to a short list of member countries whose present quota shares are most out of line with their relative economic positions. However, given the cooperative character of the Fund and the importance of improving the potential access of the low-income developing countries to its resources, we are equally concerned with the potential decline in the already unfavorable position of these countries resulting from whatever quota increase is agreed.

As Tables 1-A and 1-B of the staff paper show, the decline in the quota share and voting power of smaller member countries would tend to be mitigated if the equiproportional element of the quota increase is greater. The extent of the decline is naturally dependent on the size of the overall increase and the apportionment of the quota increase between equiproportional and selective elements. Therefore, we support the staff's view that it is reasonable to give special treatment to countries with very small quotas, similar to the initiatives undertaken on the occasion of the Eighth General Review of Quotas.

To this end, it would be appropriate to adopt a mechanism that could assist in maintaining, to the extent possible, the existing quota shares and voting power of the group of countries with very small quotas. Furthermore, according to the staff's illustrative calculations, there is a relatively greater potential decline in the combined quota shares and voting power of the non-oil developing countries. Therefore, it seems desirable to use a suitable mechanism to protect the existing level of quota shares and access limits for non-oil developing countries, especially for the important subgroup of those countries eligible to use the enhanced structural adjustment facility.

Given the Fund's experience in the application of rounding procedures, the mitigation schemes proposed by the staff, implemented in an appropriate way, seem in principle to be the most suitable, practical, and agreeable means to minimize the potential erosion of the quota shares of developing countries, and would respond to the concerns expressed by Mr. Rye. It could be argued that the application of any mitigation scheme--including a rounding procedure--would be a departure from the Fund's principle of uniform treatment, a point that has been made by a number of Directors. However, we have some doubts about the validity of that argument within the context of the Fund's operations, which are based on a spirit of cooperation.

The Fund's history has proved that, over the years, the cooperative character of the Fund has been enhanced. The introduction of basic votes; the modification of the Bretton Woods quota formula; the introduction of the multiformula method *of calculating quotas, with a view to addressing the needs of* members; and the adjustment to the quota shares of smaller countries on various occasions are all good examples of the prevailing cooperative spirit. We hope that the membership will continue to adhere to this cooperative spirit in the context of the Ninth General Review of Quotas.

Mr. Enoch made the following statement:

Concern has been expressed that members with very small quotas tend to lose voting power disproportionately whenever quotas are increased. While this tendency clearly exists, its significance must be kept in perspective. Table 1-B of EB/CQuota/89/3 shows that, for the 20 members with quotas below SDR 10 million, in no case would the combined loss of voting power amount to more than one third of one percentage point. Moreover, the extent of the smallest members' loss of voting power would depend significantly on the parameters of the overall quota review. For example, with only a modest increase in quotas, the combined loss of voting power suffered by the smallest 20 members would amount to little more than half of the loss they would face if quotas were to be doubled.

In fact, the staff paper suggests that members with quotas below SDR 10 million have actual-to-calculated quota ratios that are very much in line with the average ratio for the membership as a whole. The smallest 20 members do have ratios that are slightly lower than those of other small members, but this presumably has a great deal to do with the fact that a number of other members have quotas that were initially determined under the minimum quota policy--a policy that was abandoned 20 years ago, largely because it resulted in what was considered to be relatively large quotas for countries with comparatively small economies.

As I have stated on previous occasions, my authorities have a strong preference for uniform methods of distributing quota increases. I have also explained their reservations about according special treatment to particular groups of countries. Nonuniform methods and discriminatory treatment of different categories of members lead to distortions in the quota structure and inequities between members. Nevertheless, we recognize that over successive quota reviews the Board has taken the view that the position of the very smallest members in the Fund needs to be carefully protected. In the spirit of consensus, we could go along with a special rounding scheme, similar in scope to that used in the Eighth Review, for the 20 smallest members.

As to the share of developing countries in the Fund, the staff paper outlines several new techniques designed to mitigate the impact of any quota increase on the voting power of the developing countries. Clearly, as in the case of the smallest members, the extent to which the share of developing countries in the Fund is affected by an increase in quotas depends on the overall size of the quota increase, on the proportion that is allocated equiproportionally, and on the choice of distribution method. For example, under the overall outcome of the quota review favored by my authorities, namely, a moderate increase in quotas distributed along the lines used in the Eighth Review, the fall in the combined quota share of the 118 non-oil developing countries would amount to roughly 1 percent.

In deciding whether further action to protect the position of developing countries in the Fund is warranted at this stage, a number of considerations must be weighed. First, and most generally, a question arises as to whether marginal shifts between review periods in the aggregate voting shares of particular groups have any real impact on the deliberations of the Board. My perception is that Directors are heard with equal weight in the Fund, regardless of their voting power.

Second, there is a question of whether the present formula-based quota distribution methods devised by the staff systematically discriminate against developing countries. This, of course, is a matter the Committee intends to discuss again in the context of the Tenth Quota Review, although my chair has previously noted that these methods have not, over the past few decades, prevented a significant increase in the share of developing countries in the Fund.

Third, the application of the Fund's quota formulas already allows considerable flexibility in determining how quotas should be allocated, while maintaining a degree of simplicity, uniformity, and transparency. Additional flexibility could be achieved by modifying the existing formulas, but the Board has considered and rejected this option for the present quota review.

Fourth, there is a narrower question of whether the schemes under consideration would actually meet the intended objectives. From Table 2 of EB/CQuota/89/4, it is not clear that either of the two proposed mitigation schemes would have much impact on the aggregate voting share of the non-oil developing countries, or on the shares of the countries eligible to use the enhanced structural adjustment facility. Indeed, the illustrations presented in the appendix to that paper show that neither of the proposed mitigation schemes would raise the voting share of any member by more than one hundredth of 1 percentage point.

Having weighed these various considerations, my authorities are not persuaded to support the introduction of either of the mitigation schemes described by the staff. Nevertheless, if strong support is voiced by other Directors, we would not wish to stand in the way of a consensus.

Mr. McCormack made the following statement:

Like other speakers, I note that this discussion seems to be somewhat academic, since we are still not close to reaching an agreement on the approximate magnitude of the quota increase or the method of quota distribution. These two factors have a substantial impact on the quota share of developing countries and their voting strength. Depending on the size of the increase and the method of distribution, there could be only a minor decline in the present quota share of the developing countries, which would not merit the complications associated with trying to make special adjustments for them. Consequently, in light of the continuing uncertainty, my comments with respect to the size of the quota increase should be viewed as tentative.

During the Committee's previous discussion on this issue (Committee of the Whole on Review of Quotas 88/9, 9/2/88), many Directors, including from this chair, reaffirmed their earlier positions that the distribution of the quota increase should not be constrained to artificially maintain the shares in voting or in quotas of particular groups of members. In EB/CQuota/89/4, the staff has described alternative ways to adjust for the declining shares of the countries with relatively small quotas. The basic question that arises from this paper is the purpose of the exercise. If the objective is to protect access to Fund resources, my authorities consider that this could best--and most directly--be done in the context of the discussion on access limits. As we have stated on previous occasions, we would prefer to protect the overall access of developing countries by maintaining access above the suggested level of 250 percent of quota, or by flexibly administering the access policy. In this connection, however, some of my authorities are more supportive than others of using techniques to mitigate any decline in the share of the developing countries in the Fund.

A more difficult problem is to mitigate the reduction in voting strength. Different sizes of quota increase and alternative methods of distribution can result in very small reductions in the shares of members. Consequently, we would prefer not to begin the difficult and time-consuming process of negotiating the details of mitigation schemes until it is clear that the agreed size and method of distribution will lead to declines of a magnitude that would clearly warrant such an effort. In that connection, our position is similar to that of Mr. Rye, namely, that this issue should be addressed at a later stage of the quota review as the Committee approaches the conclusion of the quota review exercise--not at the present stage.

As in previous quota reviews, we recognize the special position of the smallest members of the Fund, defined as those with quotas of SDR 10 million or less. While special treatment of very small members could create distortions, the quotas of very small member countries are indeed low relative to their needs. These countries have economic structures that make them especially vulnerable to external factors and other considerations that may not be adequately captured in the formulas used to calculate quotas. However, the aggregate impact of any adjustment is likely to be very small; de minimis considerations therefore apply. In the light of such considerations, we are prepared to consider in detail arguments for a special adjustment of these very small quotas.

Nevertheless, we have not reached any firm conclusions with respect to which technique for making such a special adjustment would be most appropriate, and we would need to further consult with the members of our constituency that would be most directly affected before we could take a firm position. However, we agree with the staff that it would be inappropriate to reintroduce a small quota policy, since such a policy would, in effect, institutionalize distortions for all members with small quotas. In addition, we agree that some ceiling on the extent of special adjustments might be in order. A rounding technique, similar to that used in previous quota reviews, might be practicable, but we are mindful of the disparities that have emerged in association with past rounding exercises. Another approach might be to increase all very small quotas by a proportionate amount. In any event, we see merit in Mr. Rye's suggestion to try to eliminate or reduce existing anomalies within the group of countries with very small quotas. Mr. Rye has given examples of countries in his constituency that are affected by such anomalies; and I would add that Antigua and Barbuda and, to a lesser extent, St. Vincent in my constituency also seem to be anomalous, reflecting, in part, discontinuities in the treatment of small countries over previous years. In the light of these considerations, we support the consideration of special treatment for these countries.

Mr. Adachi said that Mr. Yamazaki had asked him to convey his apologies for being unable to attend the discussion; he hoped Directors would not take that absence as a sign of disinterest. On the contrary, on several previous occasions, his chair had expressed its sympathy with the concerns of developing countries, and his authorities were willing to favorably consider giving exceptional treatment to the countries with very small quotas, as in the Eighth General Review of Quotas.

Although his chair would reserve its final position until the size and distribution of the quota increase were agreed, it supported the application of a special rounding procedure for members with quotas of SDR 10 million or less, Mr. Adachi remarked. At the same time, however, it was important to emphasize the purpose of quota reviews--to rectify the present quota shares of members to reflect their relative economic positions. Therefore, his chair would not support techniques that would have undue implications for restructuring quota shares. In that connection, he endorsed the staff's conclusion that any mitigation scheme for members with very small quotas should not introduce further distortions in the overall quota structure.

Mr. Appetiti made the following statement:

The issue concerning the share of developing countries in the Fund presents two different problems. The first is one of principle, concerning the question of whether or not, in reviewing quotas, we should protect the quota shares and voting power of particular groups of members. The second problem, which is subordinate to the first, is concerned with the technicalities that need to be adopted in order to slow down the decline in the quota shares of given groups of countries.

Like other Directors, I find it difficult to comment on the issues before us without having a decision on the size of the Fund and on the method that will be used to distribute the quota increase; both of those decisions will have an important bearing on the issues currently under discussion.

The reduction in relative terms of the total quota share of developing countries in the Fund, particularly of the non-oil developing countries, is an almost inevitable consequence of the application of any selective method of distribution for the quota increase, because a large number of non-oil developing countries, representing about 94 percent of the total quota share of those countries, have actual quotas that are larger than their calculated quotas. This fact outweighs the positive effects of other factors like the growth of GDP. As we have indicated during previous Committee discussions, the present quotas of these countries overestimate the relative position of the overall group of developing countries in the world economy. Hence, the decline in the quota share of this group represents an adjustment of previous misalignments.

Having said this, however, we are not insensitive toward the problem this group of countries would face in terms of its voting power and quota share, or toward the effect of the decline on the access of individual countries to the Fund's resources. Nevertheless, Directors have recently recognized the need to reduce the discrepancies between actual and calculated quota shares in order to better reflect the relative economic size of each member in the world economy. Although there are differences among Directors concerning the appropriate degree of such an adjustment, the principle of using selective criteria in allocating the quota increase has been broadly agreed.

Therefore, the problem becomes one of striking a balance between minimizing the impact of the quota increase on members' access, and maximizing the realignment of actual and calculated quotas. During the Committee's previous discussions, many Directors clearly recognized the need to make such a trade-off.

The problem of maintaining access, which stems from the declining quotas of developing countries, could be solved by adjusting the margins of flexibility offered by the possible degrees of selectivity that could be introduced in the distribution of quotas and by approving an increase in the size of the Fund that might better reconcile the trade-off between maintaining access and realigning quotas. Obviously, the decision on the size of the Fund has a crucial bearing on this matter.

If a suitable compromise to solve the problem of maintaining access cannot be found within the framework of the agreed distribution method and future Fund size, there are two other possible solutions, although neither of them is satisfactory.

The first option would be to raise access limits either for all members or for specific countries. This solution would raise another set of problems that would probably make the implementation of the access policy difficult. The second option would be to apply some special techniques to mitigate the impact of the quota increase on the access of developing countries.

I will not comment in detail on the mitigation schemes proposed by the staff, since we are not in favor of either of those schemes. However, we see some merit in the application of rounding techniques to mitigate the impact of the quota increase on the position of countries with very small quotas.

The problem of declining quotas for developing countries has resulted from the recognized need to move toward a quota structure that better reflects the relative positions of countries in the world economy. The undesirable effects of the quota increase on access limits should be avoided by endowing the Fund with an appropriate capital base and by using the margin of flexibility presented by alternative methods of distribution to make selective increases. The mitigation schemes proposed by the staff are second-best alternatives. However, I do see some merit to those schemes, but only if they are used to limit the impact of the quota increase on very small countries, and provided that the scheme does not introduce additional distortions and is applied to a very limited number of small countries.

Mr. Dai made the following statement:

Although the share of developing countries in the Fund and the position of countries with very small quotas has been addressed in several previous discussions, no substantive results have been achieved thus far. It is unfortunate that no matter what distribution method is used, the share of quotas and voting power of most developing countries will decline--in some cases drastically. We have always maintained that, as an international cooperative institution, rather than a private, profit-oriented business, the Fund must pay great attention to--and redress--the continued declining trend of the quota share, voting power, and the relative position of the developing countries, especially the low-income and small members. To maintain, or at least minimize the reduction in, the share of developing countries is a matter of principle that most developing countries, which represent the majority of the Fund's membership, are deeply concerned about.

In EB/CQuota/89/4, the staff presents two schemes that are designed to mitigate the decline in the relative voting power of developing members. That paper shows that, to mitigate the adverse effects on developing countries, the equiproportional element of the quota increase must be greater than the selective element, the adjustment coefficient should be small, and the number and amount of selective increases made under Method B should be smaller if a combination of Methods A and B is to be used. These requirements should be used as guiding principles in determining the techniques of distributing quota increases. With respect to the two mitigation schemes illustrated in the staff paper, the first scheme seems to be more acceptable than the second as a compromise device, because it might satisfy the requirement of uniformity while maintaining the relative position of individual members.

As to using techniques to safeguard the position of countries with very small quotas, which was discussed in EB/CQuota/89/3, we should not exclude from the Ninth Review the rounding method that was used under the Eighth General Review. On the issue of a small quota policy or a minimum quota, I am not convinced by the arguments opposing such policies on the grounds that they would introduce distortions in the quota structure, because they are not based on relative economic positions and would result in inappropriately large quotas for very small economies. First, this problem can be addressed by choosing an appropriate scale for the mitigation element. Second, the principle of having a minimum quota policy was introduced at the origination of the Fund. Moreover, the basic voting system specified in the Articles of Agreements is, in itself, a device to safeguard the smaller or poorer members, because their quota shares are relatively low. That is a mitigating element in the Fund's voting system aimed at reducing the imbalances in the relative positions and voices of large and small members.

In addition, I am not convinced by the arguments that have been presented against giving special treatment to exceptional cases, or to the concerns of certain members or groups of members, on the grounds that that would be a breach of the principle of uniform treatment. Under that principle, if the Committee gives consideration to the request for a special or ad hoc increase for a large member like Japan, special requests by small or poor members should also be given equal attention and favorable consideration.

On previous occasions, we have expressed our doubts about the effectiveness and accuracy of the present formulas used to calculate quotas in reflecting the relative economic positions of member countries. Although some low-income developing members, including China, have experienced high growth rates, by international standards, their shares in quotas and voting power are expected to continue to decline, which is discouraging, because it distorts the picture of the economic progress that has been made in the developing countries.

Mr. Santos said that he recognized the significant extent of the calculations and analysis the staff had prepared in order to provide the Committee with a clear picture of the impact an increase in quotas would have on the quota shares and voting power of developing countries and countries with very small quotas. It was unfortunate that the final outcome of the discussion could not match the expectations of those countries, owing to the predetermined constraints that had been recommended by the Committee and that had been translated into more emphasis being placed on the use of uniform methods in quota distribution. For the majority of the membership, the results were disappointing.

The staff had provided two alternative schemes designed to mitigate the erosion of the total voting share of developing countries that would result from a quota increase, Mr. Santos noted. However, those schemes fell far short of addressing the main source of that decline--the decreasing importance of basic votes as quotas increased. That decline was well illustrated in Table 2 of EB/CQuota/89/4, which showed that under either of the proposed mitigation schemes the change in developing countries' voting power would exceed the change in their quota shares.

Therefore, to preserve the voting share of developing countries, a scheme that would restore the importance of basic votes was needed, Mr. Santos considered. Basic votes played a crucial role in establishing a balanced representation in the Fund and reflected the spirit of cooperation that lay behind the Articles of Agreement. Because of the difficulties associated with an adjustment of basic votes, a rule that would have the same practical results was warranted. The staff had developed such a rule, by providing for an additional quota increase of a fixed absolute amount of quota increase for each member. Despite its shortcomings, that rule could be a useful tool, if it was implemented without the constraints that had been introduced in the mitigation schemes described by the staff.

The negative impact of an increase in quotas on the quota and voting shares of developing countries was even more evident with respect to the position of countries with very small quotas in the Fund, Mr. Santos continued. As Table 1 of EB/CQuota/89/3 demonstrated, the aggregate shares of quotas and voting power of small countries--with SDR 10-50 million--declined under all alternative quota distributions. More important, it should be noted that the impact of an overall increase of quotas fell more heavily on the voting power of the smallest countries, reflecting the decline in the relative importance of basic votes. In the case of small countries, the decline in voting power was clearly disproportionate in relation to the decline in quota shares. There was no combination of uniform techniques that would adequately mitigate those declines. Moreover, the staff had shown that the very small countries' current payments were relatively low both in terms of the Fund membership as a whole, and particularly in relation to other developing countries. Mr. Rye and Mr. McCormack had already elaborated in detail on the factors that justified special treatment for that group of countries, and he agreed with most of their comments. Indeed, the special needs of that group of countries made a strong case for a special increase for countries with small quotas. The fact that there were no members at present with quotas between SDR 10 million and SDR 15 million would facilitate the implementation of such a special increase, because the type of distortions introduced by the small quota policy or a minimum quota would be largely avoided. The special adjustment made for the countries with very small quotas should be much wider in scope than a rounding scheme. Apparently, the way in which the rounding approach had been implemented in the past--under the Fifth and Sixth Quota Reviews--added to the erosion of the basic votes in the voting shares of countries with smaller quotas. Mr. Rye's proposal to rearrange the structure of very small quotas to reflect the structure of calculated quotas was worthy of consideration, although it had some shortcomings related to the general problem of avoiding abrupt changes in the structure of quotas.

Mr. El Kogali commented that the position of his chair with respect to the voting share of developing countries in the Fund was only an extension of the remarks he had made during Committee of the Whole on Review of Quotas Meeting 89/4 (2/6/89) on illustrative calculations for the distribution of an increase in quotas. During the Committee's previous discussions on the Ninth General Review of Quotas, a great deal of emphasis had been placed on the cooperative character of the Fund. In connection with the quota increase, that cooperative character involved consideration of the global needs of the membership and the need to safeguard the effective participation of all members in the Fund's decision-making process.

The formulas that were being used to distribute quota increases appeared to be inherently biased toward intensifying the distortion of voting power in the Fund, which was unacceptable, primarily because it would erode confidence in the Fund as a cooperative institution designed to give all its members a fair chance to participate in its decision-making process, Mr. El Kogali commented. Therefore, an explicit attempt must be made to correct that inherent flaw in the formulas.

The approaches that had been suggested by the staff to mitigate the decline in the quota and voting shares of developing countries were aimed in the right direction, but they did not go far enough, Mr. El Kogali considered. According to the staff's calculations, even under the proposed mitigation schemes, the fall in the voting power of developing countries would exceed 2 percent in a Fund of SDR 150 billion. In that connection, it should be noted that, at the current stage, the working assumption of a future Fund size of SDR 150 billion was still uncertain, because the question of the size of the Fund had not yet been decided. Any decision concerning the distribution of quotas and the impact of the quota increase on groups of member countries would clearly depend on the size of the Fund. He wondered whether some other configurations might produce a more favorable result for the developing countries as a group and for the poorer countries in particular. Such configurations might involve a larger equiproportional element in the distribution of quotas, different mitigation coefficients and, perhaps, rounding techniques that included a larger number of countries than those with quotas of SDR 10 million or less. At the same time, due regard should be taken not to materially deviate from adjustments that recognized the relative economic positions of members. The inclusion of only countries with quotas of SDR 10 million or less indicated that their problem could not be solved independently from a decision on the general position of developing countries and countries eligible to use the enhanced structural adjustment facility. Mr. Dai was correct in pointing out that, if the Fund could justify the use of selective methods to increase the quota share of Japan, it should also be able to justify increasing the shares of small and developing countries.

Mr. Feldman stated that on previous occasions his chair had expressed its support for a substantial quota increase with a large equiproportional element combined with Method A, which at the same time would allow for ad hoc increases for those countries with quotas that were clearly out of line. As the staff had mentioned in EB/CQuota/89/3, such a combination, particularly a distribution that included using Method A, would help to mitigate the decline in total quotas and voting power of the members with very small quotas.

He agreed with the staff that the case of the members with very small quotas should be considered in the context of an overall agreement on the size and distribution of the increase in quotas, or in association with arrangements that could be considered to mitigate the decline in total quotas and voting power of the non-oil developing countries as a group, Mr. Feldman commented. Such an approach would clearly help to avoid distortions in the overall structure of quotas, and would be consistent with the application of more general rules and uniform criteria in the distribution of the quota increase.

As to the consideration of the share of developing countries in the Fund, the most important mitigation effect on the decline in the shares of developing countries resulted from the consideration of a maximum equi-proportional element, of higher than 50 percent, in the distribution of the quota increase, Mr. Feldman noted. Furthermore, that would clearly be an application of uniform criteria.

With respect to the mitigation schemes illustrated in the staff paper under discussion, he could go along with Scheme I, which provided for a fixed amount of additional quota increase for each member, subject to an agreed constraint, in order to minimize the distortions between relatively small members, Mr. Feldman concluded. He did not see clear advantages to the application of rounding procedures, since they would run counter to the principle of uniform treatment and might lead to unfair and randomly distributed corrections.

Mr. Pétursson commented that the position of his chair concerning the share of the developing countries in the Fund followed from its general position on the Ninth General Review of Quotas that quotas should be based on objective criteria reflecting members' economic positions. In that connection, the Fund should be cautious not to distort quota calculations to favor a particular country, or a particular group of countries. On that basis, his authorities were reluctant to support the use of mitigation schemes aimed at ensuring a certain quota share for a specific group of countries. It should be noted that the present formulas used to calculate quotas took into account to some extent the specific problems regarding the developing countries, and those countries' access to Fund resources had already been assured through the Fund's various facilities.

He agreed with the staff that the smallest countries had quotas that, on average, bore the closest relationship to their shares in calculated quotas, Mr. Pétursson stated. Therefore, granting special treatment to those countries could not be justified. Moreover, by granting such special treatment, the Fund would distort the relationship between the countries with the smallest quotas and many other relatively small member countries. Nevertheless, his authorities would support the use of a rounding procedure similar to the one applied in connection with the Eighth Quota Review.

Mr. Finaish said that his authorities continued to consider that possible shifts in the developing countries' share in quotas and voting power should be an important consideration in the Committee's final judgment concerning the distribution of an overall increase in quotas. Therefore, the staff's examination of schemes that could mitigate the significant reduction in the quota and voting shares of a large number of developing countries, which would otherwise result from the Ninth Quota Review, was welcome. Of the mitigation schemes presented in the staff paper, he favored the use of Scheme I, although his position on that matter was tentative, given the interdependence of the various elements involved in the quota review.

Although mitigation of the decline in the share of developing countries in the Fund would also help to assure the quota share of the group of countries with very small quotas, the discrepancy between the actual and calculated shares of the smallest members called for additional mechanisms to bring their quota and voting shares more in line with their relative positions in the world economy, Mr. Finaish considered. Therefore, his authorities would support the application of the rounding procedures used in the Eighth Quota Review. However, the Committee should recognize that the benefit to individual members derived from such procedures would be random. Thus, it was possible for members with the largest disparities to benefit the least, as was the case for one member of his constituency, Maldives, during the Eighth Quota Review. In fact, Table 3 of EB/CQuota/89/3 showed that Maldives, which was the smallest member in the Fund, continued to have the largest discrepancy--of all the members with very small quotas--between its actual and calculated quota shares. Looking at the Fund's membership as a whole, it was interesting to note that the ratio of the disparity between the actual and calculated quotas of Maldives was about the same as that of Japan. Therefore, while he agreed with the staff that any special adjustments made for countries with very small quotas should avoid distorting the overall structure of quotas, the need to correct the large disparities in the shares of some small members, such as Maldives, was obvious.

Mr. Adachi remarked that, as his chair had stated on previous occasions, it was important to note the difference between the ratio of disparities between actual and calculated quotas and the absolute size of those disparities. Due attention should be paid to the size of disparities, because quotas were the basis of individual members' rights and obligations within the Fund. In that sense, the position of his chair was very different from that of Mr. Finaish.

Mr. Hogeweg made the following statement:

> As my authorities have indicated on many previous occasions, they value highly the use of uniform formulas in distributing quota increases. In that connection, we are opposed to any division of the membership into separate groups, to which a different distribution technique would apply, and we are pleased to note that, thus far, the conclusions of the Committee seem to go in the same direction.
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> In the light of these conclusions, paying special attention to the share of developing countries in the Fund and the position of the countries with very small quotas is a somewhat delicate issue. Although the way in which the quota shares of such countries move is of obvious interest, paying special attention to the subject may invite the use of mechanisms that would run counter to the earlier conclusion of the Committee not to distinguish between separate groups of countries in the distribution process.
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> The relative decline in the share of developing countries, countries eligible to use the enhanced structural adjustment facility, and countries with very small quotas, as presented by the staff in various tables, reflects two important aspects: the declining importance of basic votes as total quotas increase, and, as far as the increase is distributed in a selective way, the fact that many countries have actual quota shares that are high relative to their calculated shares. It would have been helpful for the staff to illustrate separately the effects of the relative decline in basic votes.
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> During Committee of the Whole on Review of Quotas Meeting 88/9 (9/2/88), this chair expressed its support for the proposal to increase the number of basic votes for all members, and that position is equally valid today. However, as such a proposal would require a change in the Articles, it was not

an option for the current quota review. In light of that consideration, mitigation Scheme I, presented in the staff paper, is of great interest. In essence, this scheme tries to simulate an across-the-board increase in basic votes by distributing a small part of the quota increase, in equal absolute amounts to all members, with an upper limit of a small percentage of present quota shares in order to avoid unduly large effects on members' reserve tranche positions and access limits in general. However, the scheme has a drawback in that it uses quotas--which, by the very nature of the Fund, determine the voting power of members according to economic strength--to preserve the floor in voting power, which should be unrelated to economic power.

Although the staff presents mitigation Scheme II as being similar to Scheme I, there are important differences between the two schemes. For example, Scheme II applies to only part of the membership, which would represent a further step toward distinguishing among country groups, and is therefore undesirable. The inclusion of Scheme II in the staff paper illustrates the fact that mitigation schemes can be used to allow numbers and coefficients to achieve preset outcomes for certain preset groups.

In the light of these considerations, my authorities consider that concerns about large shifts in quota shares, apart from the issue of basic votes, can be alleviated by retaining an important equiproportional element in the distribution of quotas. After agreements have been reached on the fundamental aspects of this quota review, we could consider whether rounding procedures could be utilized to accommodate, to a certain extent, the special concerns of countries with very small quotas.

Mr. Al-Assaf commented that he would not repeat the position of his authorities, which had been presented during Committee of the Whole on Review of Quotas Meeting 89/1 (1/9/89), which was essentially in support of maintaining the share of developing countries in the Fund. However, in that connection, it was important to note that the usable resources of the Fund came mainly from industrial countries, and the concerns that had been expressed by developing countries had been alleviated by the enlarged access policy, the Fund's special facilities, and basic votes.

The members with very small quotas were more concerned about access than about voting power, Mr. Al-Assaf noted. Although the Fund's special facilities, especially the enhanced structural adjustment facility, were designed to address those concerns, he could go along with the use of some rounding techniques, provided those techniques did not alter the position of the smallest members in relation to other members with small quotas.

In addition, due consideration should be given to countries with large disparities between their calculated and actual quotas, as in the case of Maldives mentioned by Mr. Finaish.

Mrs. Filardo said that, like other Directors, she was not ready to take a position on the share of developing countries in the Fund or on the position of countries with very small quotas until the Committee reached a consensus on the future size of the Fund. However, the statement presented by Mr. Jalan concerning the question of whether or not the formulas currently used to calculate quotas accurately reflected the relative economic positions of countries was of interest to her authorities, and that statement should be reviewed in the future. In addition, if the Committee agreed that the position of developing countries and small countries in the Fund should be maintained, efforts to maintain the quota shares of those countries should be implemented at the expense of the larger countries in the Fund.

The Deputy Treasurer recalled that several Directors had raised the question of whether maintaining access limits was really an important consideration in the Ninth Review with respect to the developing countries as a whole, and in particular with respect to some of the smaller countries, or whether the Fund could take some special measures outside of the quota review to ensure access for those countries. As Mr. Rye had noted, the issues concerning members' access to Fund resources would be examined in detail during the Executive Board's discussion on access limits in the light of the outcome of the Ninth Review. However, setting specific access limits for countries with small quotas would run contrary to the Fund's principle of uniform treatment for all members. However, of course, as the Fund's access limits were not targets, the application of those limits could be considered on a case-by-case basis, taking into account the particular circumstances and needs of each member. Therefore, there was flexibility available to the Fund not through the establishment of access limits themselves, but through the application of those uniform limits.

The issue of maintaining the relative importance of basic votes in overall voting shares to protect the configuration of quota shares for the developing countries was examined in detail in EB/CQuota/88/7, which was presented to the Committee in September 1988, the Deputy Treasurer noted. At that time, Directors agreed that possible changes in the Fund's provisions related to basic votes should not be pursued within the context of the Ninth General Review of Quotas, but could be discussed in detail at a later date, as an amendment of the Articles would be required. However, in that connection, it was interesting to note that when the Articles were written, a fixed absolute sum of 250 basic votes for each member was specified--one of the few instances in which a fixed quantity was provided for in the Articles. At the same time, it was apparent that the absolute amount of quotas set in Schedule A of the Articles was not expected to remain fixed, as there were provisions for periodic reviews of quotas. Therefore, the drafters of the Articles must have expected the relative importance of basic votes to decline over time as quotas were adjusted, because they did not include a provision for adjusting the fixed amount of basic votes, while quotas were expected to change. Moreover, at the time of the Second Amendment of the Articles, a large number of Directors took the position that basic votes should decline in relative importance over time, unless specific policy measures were taken to avoid that decline.

As was mentioned by Mr. Hogeweg, the staff could have illustrated the effects of mitigation Scheme I more clearly and extensively in the paper under discussion, the Deputy Treasurer continued. However, the staff had considered that setting a fixed amount of quota to be given to all countries conveyed the basic principle of that scheme. Scheme II had a certain elegance, which Scheme I lacked, in that it was linked to the current size of members' quotas, rather than being equal for all members irrespective of quota size. Therefore, a more thorough description of Scheme II, than of Scheme I, had been given in the staff paper. However, the staff could provide particular examples of the way in which either of the schemes would apply--with or without the constraints mentioned in the staff paper--if Directors so desired.

The question of whether the formulas currently used to calculate quotas accurately reflect members' relative economic positions had been raised on several previous occasions, and Directors had agreed that those formulas should be examined further in connection with the Tenth Review of Quotas, the Deputy Treasurer noted. However, with respect to the comments made by Mr. Jalan for the current discussion, it should be noted that, although the annual rate of GDP growth for industrial countries during the current review period was 6.9 percent, their share in calculated quotas was expected to decline from 66.6 percent at the conclusion of the Eighth Review to 65.9 percent under the Ninth Review. At the same time, the annual rate of GDP growth for the countries eligible to use the enhanced structural adjustment facility was 4.7 percent over the current review period, and their share in calculated quotas was not expected to change. The aggregate quota share of those countries at the conclusion of the Eighth Review was 4.2 percent, and it was expected to be the same under the Ninth Review. Therefore, there was no antigrowth bias toward small or poor countries in the quota formulas.

Mr. Jalan asked whether the staff meant to indicate that the annual rate of growth for the countries eligible to use the enhanced structural adjustment facility was not 6.7 percent over the period 1980-85. In addition, he wondered whether the figures presented by the staff had included the growth rates achieved by India and China.

The Deputy Treasurer replied that the annual growth rate achieved by that group of countries, including India and China, was 4.7 percent.

Mr. Jalan noted that, during the 1980s, China had an annual growth rate of 9 percent. However, despite that impressive rate of growth, China's quota share was expected to decline by 1 percentage point. He was not arguing that the staff's calculation of the quota formulas was wrong, but rather that there must be some methodological problems associated with the present formulas. Of the 45 countries that had per capita incomes of less than SDR 500 million, 40 were expected to lose quota shares by more than 40 percent.

The quota formulas had resulted in that decline, because the staff had measured GDP growth in SDRs, Mr. Jalan considered. If the staff had, instead, measured rates of real GDP growth based on an index of national currencies, perhaps the decline would not have occurred. In the World Economic Outlook as well as the World Development Report, it was the accepted convention to calculate the growth rates of individual countries in terms of their national currencies at constant prices.

Any formula that had such an adverse and uniform effect on all poor countries could not be defended as equitable, particularly in light of the fact that those countries had achieved satisfactory rates of growth, Mr. Jalan concluded. The fact that there were obviously methodological problems involved in using the present formulas to calculate quotas presented a strong case for distributing the increase in quotas under the Ninth Review largely on an equiproportional basis.

Mr. Al-Assaf asked whether the practice of measuring GDP growth over a number years had implicitly counterbalanced fluctuations that might have taken place with respect to growth or exchange rates.

The Deputy Treasurer replied that the practice of measuring growth over a number of years counterbalanced annual fluctuations to some extent. However, the average annual rate of growth was entered into the formulas for only one year, because in some circumstances that conveyed a more realistic picture of a country's situation. For example, if a country was on an upward growth path, the most recent rate of growth achieved would be most relevant.

Mr. Jalan said that, with respect to the question raised by Mr. Al-Assaf, a problem arose in comparing different national products, owing to the conversion of all national currencies to SDR terms. For example, although a country might have achieved a relatively high real rate of growth, once its currency was converted at the 1986 exchange rate, that rate of growth might not be reflected, or could even appear to be negative. The conversion problem could be solved by measuring national products in terms of local currencies at constant prices, or based on an index of national currencies, rather than using the SDR. Although technical questions such as the use of constant exchange regimes would have to be examined in the context of the Tenth Quota Review, it should be noted that the exchange rate problem was particularly relevant to the current review period.

The Deputy Treasurer remarked that an index of national currencies could be used to measure national products in terms of volume, but the present quota formulas dealt with nominal aggregates of GDP growth in terms of the SDR. It would be difficult to apply a measure based on an index to such nominal aggregates. In fact, during the period in which the Bretton Woods formula was used, the Fund had made measurements based on national currencies, but the considerable overvaluation of exchange rates had artificially inflated GDP figures as undervaluations had underestimated GDP figures. However, under the present system of market-determined exchange rates, the problem of under and overvaluation had essentially been eliminated, and that change had certainly affected the outcomes of the past three quota reviews.

Mr. Jalan noted that the problems involved with comparing official exchange rates were well known, and those problems had a definite impact on the results produced by the quota formulas. For example, between 1980 and 1985, when China had an average annual growth rate of approximately 9 percent, the rate of exchange between the yuan and the dollar had fluctuated considerably. Because the exchange rate had changed considerably, the national product of China might appear to have shown no growth or even negative growth in SDR terms. If the measure of GDP growth was based on the local currency at constant prices, or on an index of currencies, instead of being measured in terms of the SDR, a very different outcome might have been achieved.

Mr. Dai recalled that, according to the staff's estimates, the aggregate growth rate for the countries eligible to use the enhanced structural adjustment facility was 4.7 percent. He wondered whether the staff had the growth rates of the individual countries in that group.

The Deputy Treasurer said that the staff did not have that information available for the current discussion, but could provide it to the Committee at a future date.

Mr. Hogeweg noted that the reference to the staff paper in his statement was not that more attention should have been paid to Scheme I, but rather, that the effect of basic votes on the total voting shares of country groups could have been described in more detail. He had differentiated between the importance of basic votes and the use of the two mitigation schemes proposed by the staff, because he did not support the use of either mitigation scheme.

The Chairman made the following concluding remarks:

> This week we have touched on all the main elements of our work program for the Ninth General Review of Quotas: on Monday, we discussed the role and size of the Fund and the techniques for distributing an increase in quotas; and today we have considered the share of developing countries in the Fund, including the position of countries with very small quotas, and the method of payment for increased subscriptions.

Payment for increased subscription

Most Directors confirmed the positions they had taken during our initial discussion on payment for increased subscriptions to the Fund (Meeting 88/4, 3/14/88). On that occasion, the Committee agreed that 25 percent of the increase in quotas should be paid in reserve assets in order to maximize the liquidity effects of the quota increase. Many Directors expressed a preference for the reserve asset payment to be made in SDRs, but, along with other Directors, they indicated that they could accept giving members an option to make the reserve asset payment in currencies acceptable to the Fund, or in a combination of SDRs and currencies acceptable to the Fund. It was generally agreed that arrangement should be made by the staff for members that needed to acquire SDRs to make the reserve asset payment through entering into transactions by agreement in SDRs, to the extent feasible, and with the cooperation of other members. In addition, most Directors generally agreed that members with insufficient holdings of SDRs, and low reserves in general, should be able to borrow SDRs through arrangements such as those agreed on the occasion of the Eighth General Review and as explained in the Appendix to EB/CQuota/89/2. I welcome, in this respect, the intention of certain large holders of SDRs to facilitate such operations, and especially the agreement in principle of one member to participate in arrangements of this type that could be completed in one working day. The Fund would, of course, need to adopt a policy on sales of SDRs by the General Resources Account in connection with the SDRs received as a result of the increase in quotas.

A relatively large increase in quotas would absorb a considerable proportion of existing SDRs, which amount to only SDR 21.4 billion. Many Directors, therefore, expressed concern about whether a sufficient amount of SDRs would be available for members to acquire the amounts needed to make reserve asset payments in SDRs, even if special arrangements to acquire them were put in place. In this connection, many Directors were attracted to the possibility of making an allocation of SDRs in association with an increase in quotas, as on the occasion of the Seventh General Review. In our consultations on an SDR allocation, the need for SDRs in association with an increase in quotas might be kept in mind. I have noted, however, that in the view of several Directors, the need for a resumption of SDR allocations is not present, and that others, who indicated that they could support a modest allocation of SDRs, did not consider that such an allocation should be linked to the current quota review.

Share of developing countries

With respect to the share of developing countries in the Fund, and in particular the position of countries with very small quotas, Directors noted that the prospective decline in the shares of such members in quotas and in total voting power would be directly affected by the size of the overall increase and its distribution between equiproportional and selective increases. Accordingly, a number of Directors felt that they were not in a position to offer definitive views on the need for mitigation for the countries with relatively small quotas until there was a consensus on the size and distribution of the quota increase. Furthermore, most Directors reiterated their previous positions that the quota increase should be distributed using uniform techniques, which would be applied to all members and should not be constrained on the basis of the shares in total quotas or in total votes of particular groups of members. Indeed, some Directors noted that the prospective decline in the aggregate voting share of the developing countries could be mitigated to a considerable extent through a relatively large equiproportional element in the quota increase, and by distributing the selective increase to all members, as would be the case, for example, under Method A.

Other Directors emphasized that the level of access to the Fund's resources for the smaller countries was also an important consideration.

Accordingly, while not all Directors were convinced of the need for a mitigation scheme in connection with the quota increase under the Ninth Review and others thought that a flexible application of the access policy could appropriately address the needs of developing countries, a number of Directors considered that measures should be taken to protect the share in voting power of the smaller members, along the lines considered by the staff in EB/CQuota/89/3 and EB/CQuota/89/4.

Most Directors were strongly of the view that, if a mitigation scheme were to be used, the amount of mitigation made available in aggregate should be small in relation to the size of the overall increase. Among those who favored mitigation, I noted a preference for Scheme I as described in EB/CQuota/89/4. Directors were of the view that mitigation should not impinge on the principle of adjusting members' quotas in a way that would better reflect their relative economic positions. Furthermore, it was important to avoid introducing further distortions in the quota structure as a result of mitigation. Accordingly, the results of any mitigation technique that might be used would need to be examined carefully to ensure that there would be no widening of existing disparities between individual members' shares in present and calculated quotas.

Position of countries with very small quotas

Most Directors expressed considerable concern about the somewhat special position of members with very small quotas, of less than SDR 10 million. Because of the importance of basic votes to those countries, they would lose voting power as a result of an increase in quotas to a greater extent than other members with relatively small quotas. Furthermore, a number of Directors felt that the very small quotas were out of line in relation to those of other countries with relatively small quotas, of between SDR 75 million and SDR 10 million, as well as in relation to the group of non-oil developing countries. Other Directors noted, however, that, in terms of their shares in calculated quotas, the quotas of the countries with very small quotas were not in general out of line with the membership as a whole.

On balance, many Directors concluded that some mitigation of the decline in the position of countries with very small quotas could be justified, as on the occasion of the Eighth General Review. A number of these Directors concluded that a rounding scheme, such as the one followed under the Eighth Review, would be reasonable. Other Directors, however, noted that the impact of a rounding scheme is to a large extent arbitrary, and may itself lead to new distortions in the quota structure. Their preference was for reducing anomalies in relative positions among small countries. And a few of them referred to the possibility of increasing the quotas of very small countries relative to the quotas of countries in the next highest group and, in so doing, address the special nature and external vulnerability of many of the small countries' economies. Directors generally noted that any adjustments in the very small quotas should be made on a limited scale, and they were concerned that adjustments should not result in distortions in the quota structure or worsen present disparities between actual and calculated quota shares. The Committee will, of course, discuss this issue again when it finalizes its discussion on the Ninth General Review.

The Committee members concluded for the time being their discussion on payment for an increase in quotas, on the share of developing countries in the Fund, and the position of countries with very small quotas.

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