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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 94/54

10:00 a.m., June 17, 1994

Contents

Executive Board Attendance

M. Camdessus, Chairman
R. D. Erb, Deputy Managing Director

Executive Directors	Alternate Executive Directors
M. Al-Jasser	A. A. Al-Tuwaijri
	M. Sirat
J. Bergo	E. Srejber
H. Evans	J. Dorrington
	T. Fukuyama
K. P. Geethakrishnan	
	K.-T. Hetrakul
D. Kaeser	
A. Kafka	A. Calderón
K. G. Kagalovsky	
W. Kiekens	
G. Lanciotti	N. Coumbis
K. Lissakers	B. S. Newman
	G. Torres
	M. Daïri
L. J. Mwananshiku	
G. A. Posthumus	
C. V. Santos	Y.-M. T. Koissy
S. Schoenberg	E. Wagenhoefer
A. S. Shaalan	Y. Y. Mohammed
	K. B. Langdon, Temporary
E. L. Waterman	
Zhang M.	Wei B.
A. G. Zoccali	A. F. Jiménez de Lucio

L. Van Houtven, Secretary and Counsellor
C. P. Clarke, Assistant

Also Present

IBRD: R. Hirschler, Policy Research Department. African Department: M. Touré, Counsellor and Director. Central Asia Department: S. N'guiamba. European I Department: M. C. Deppler, Deputy Director; G. Bélanger. European II Department: J. Odling-Smee, Director; E. Brau, Deputy Director; L. Hansen, P. C. Hole, M. Shadman-Valavi, T. A. Wolf. External Relations Department: S. J. Anjaria, Director; P. J. Bradley, H. P. Puentes. Fiscal Affairs Department: E. F. Offerdal. Legal Department: W. E. Holder, Deputy General Counsel; J. L. Hagan, Jr. Middle Eastern Department: P. Chabrier, Director. Policy Development and Review Department: J. T. Boorman, Director; T. Leddy, Deputy Director; D. Andrews, B. V. Christensen, S. B. Creane, L. D. Everaert, A. K. McGuirk, K. M. Meesook, E. Sidgwick, N. Tsaveas. Research Department: M. Goldstein, Deputy Director; P. Wickham. Secretary's Department: A. Leipold. Southeast Asia and Pacific Department: C. M. Browne. Treasurer's Department: G. Wittich, Deputy Treasurer; E. Decarli, R. H. Floyd, D. Gupta, K. M. Kenney, O. Roncesvalles, M. Wattleworth. Western Hemisphere Department: S. T. Beza, Counsellor and Director. Advisors to Executive Directors: M. A. Ahmed, T. K. Gaspard, J. Jonáš, M. F. Melhem, P. A. Merino, T. Oya, J. W. van der Kaiij. Assistants to Executive Directors: S. E. Al-Huseini, D. A. Barr, D. Desruelle, G. Z. El-Masry, S. S. Farid, R. Ferrillo, A. Galicia, G. H. Huisman, G. J. Matthews, J. A. K. Munthali, C. F. Pillath, V. Rigász, S. Rouai, M. W. Ryan, A. Sighvatsson, V. Y. Verjbitski, R. von Kleist, Wu H.

1. REPORT BY MANAGING DIRECTOR

The Managing Director said that he had visited Dublin on June 10, 1994 to address a seminar sponsored by the Debt and Development Coalition, a group of 70, largely Irish, nongovernmental organizations (NGOs). While in Dublin, he had met with the Prime Minister and the Minister of Finance.

The Debt and Development Coalition had been established in response to the perception among NGOs that the external debt burden continued to present insurmountable obstacles to the alleviation of poverty in developing countries, the Managing Director noted. The seminar organized by that coalition had offered a good opportunity to meet directly with a large group of NGOs and to explain the Fund's activities. In doing so, he had stressed that the Fund shared the concerns of the NGO community about the alleviation of poverty in developing countries. Indeed, poverty alleviation was closely related to a high-quality growth strategy based on the implementation of appropriate macroeconomic and structural policies. In that respect, he had discussed the evidence of successful performers under the enhanced structural adjustment facility--to which Ireland had contributed--and the benefits of official debt reduction.

It was not clear whether his explanations were entirely convincing to his rather skeptical audience, the Managing Director remarked, but he had certainly cleared up some misperceptions about the Fund. In any event, the External Relations Department would follow up on the seminar and would keep NGOs informed about the Fund in the runup to the Madrid meetings. That was likely to be an uphill struggle, however, as the coalition of NGOs that he had met with was driven more by ideology and a bureaucratic approach to adopting positions than by a desire to listen to the Fund's point of view.

Following the seminar, the Managing Director continued, he had held meetings with the Irish authorities, during which he had drawn on the views expressed by the Executive Board the previous week. The Irish economy had performed well in recent years, with a rate of growth among the highest in the industrial world, and a rate of inflation among the lowest. At the same time, if Ireland was to gain maximum benefit from exchange rate stability, the capacity of the real economy to respond to external shocks needed to be strengthened, which required increased liberalization and flexibility across a range of sectors. His discussions had been useful, and there was agreement on the way forward.

2. ROLE OF FUND IN FINANCING ECONOMIES IN TRANSITION - ACCESS AND COFINANCING TRUST ACCOUNTS

The Executive Directors considered a staff paper (EBS/94/121, 6/3/94) and the following statement by the Managing Director (BUFF/94/57, 6/3/94) on the role of the Fund in financing the economies in transition through increased access to Fund resources and cofinancing trust accounts:

The Interim Committee has invited us to consider how best the Fund can continue to play its central role in supporting the efforts of a large number of our members in making the transition to market economies. As we have discussed earlier, we must approach this question with an eye to maintaining evenhandedness in the Fund's treatment of all its members. This is all the more important, given that a range of countries outside those typically regarded as "in transition" may face large financing requirements in the period ahead, including for building reserves to safeguard their programs; many of them face challenges no less profound. I remain convinced that an SDR allocation has a role to play in meeting the demand for reserves, but we will be discussing the SDR issue separately. In this statement, I will focus particularly on the question of access to the Fund's resources.

In its companion paper on this subject (EBS/94/121), the staff has reviewed recent experience under the access limits and prospective financing requirements for countries within and outside the transition group. In very summary terms, the paper suggests two steps for the Board's consideration.

First, a temporary increase in the annual access limit applying to stand-by and extended arrangements, from 68 percent to 85 percent of quota, intended to help provide confidence to all members that the Fund will be in a position to respond to their needs quickly and on an appropriate scale in support of strong measures.

Second, an extension and enlargement of the structural transformation facility (STF), from up to 50 percent of quota to up to 85 percent of quota, together with modifications intended to retain the "paving" character of the STF. For eligible countries that can move quickly to upper credit tranche arrangements, the enlargement of resources under the STF would permit a better mixing of the maturities of resources provided in the context of those arrangements. But we now understand better the difficulties some of the eligible countries face. We also understand better the determination of many of them to overcome these difficulties, even though there are setbacks and delays. Thus, we could also modify the STF to enable it to provide continuing support for some time where progress is encouraging but still not sufficient to qualify for an upper credit tranche arrangement. The idea here is to continue to allow for a first purchase of 25 percent of quota on the basis of appropriate initial conditions but provide for four successive purchases, of up to 15 percent of quota each, with timing depending on movement to a Fund arrangement, or on continuing progress toward that objective and satisfactory financing for the program.

The staff's suggestions are intended to respond to the Interim Committee's call in a way that is responsive both to those problems and also to the potential needs of the membership at large in the period ahead. But particularly with respect to the economies in transition, it has been stressed in our past discussions that an expansion of access will entail risks for the institution, and we must bear this clearly in mind as we consider how to proceed.

As the Interim Committee said, the task before us is one of historic proportions, deserving the full and concerted support of the international community; in leading this effort, the Fund's monetary character and catalytic role must be safeguarded; and this requires the support of all potential bilateral and multilateral creditors in providing adequate and timely assistance in conjunction with the Fund. I am prepared to endorse the increase in access limits under arrangements and the modifications to the STF the staff has suggested for consideration, but only if this commands the broadest support among the membership and in plain view of the potential risks involved. It would have to be understood that the membership would stand ready to increase Fund quotas if the Fund's financial involvement with transition economies and other members brought the Fund's liquidity position close to the traditional threshold for action to raise the Fund's capital. It is also essential that we have clearer understandings than has proven to be the case in the past that the Fund's financing role, while perhaps larger, will still be catalytic--including in particular under programs supported by the STF. 1/ Finally, before proceeding in this way, I will ask the membership, through you, to reaffirm its assurances regarding the Fund's preferred creditor status and readiness to provide financing in the future, in the terms provided when the STF was established (see EBM/93/61, 4/23/93).

Mr. Waterman made the following statement:

By the nature of the mandate given to us by the Interim Committee, the focus of this discussion will be on the role of the Fund in providing balance of payments support to the countries in transition. That is understandable, but it is important to recognize that any change to access policy or the creation of additional financing vehicles would apply equally to all members of the Fund. The reform efforts being undertaken in most of the

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1/ The idea of cofinancing trust accounts has a potential role to play in this. I do not believe we need to have a substantive discussion now, but I would invite Directors' comments on the main possible features of such accounts as set out in EBS/94/121, or on other points, for the staff's guidance in preparing further documentation.

countries in transition and their large balance of payments needs are matters of particular relevance to the Fund at present, but we do need to ensure that the broader issues are also given full consideration. I would like to pick up on some of these broader issues in relation to the proposals on access. On the proposals for the creation of cofinancing trust accounts, I can go along with the preparation of a detailed Board paper, but a number of issues will need to be canvassed. Among other things, it remains to be seen what level of financial support might be forthcoming.

For some time now we have argued in the context of SDR discussions that, if the ability of the Fund to provide financial resources in support of members' reform efforts was being hampered by current access limits, we would be prepared to consider changing those limits. The Board last examined access limits in October 1993, and it was widely believed then that the current limits were not overly constraining the Fund. I believe it is still the case that access limits, per se, are not proving to be a limiting factor. Rather, it is arguably the way in which access is determined within those limits that appears to be the constraint. In that regard, the staff paper is quite enlightening. Since the new access limits were put in place, average access has been well within those limits; only one stand-by arrangement or extended arrangement has had access above 75 percent of the annual limit, and gross Fund financing as a proportion of total gross financing requirements has been lower than in 1990-92.

This suggests either that reform programs have not been strong enough to justify higher access or that a glass ceiling--which has been referred to in previous discussions--is in place. My guess is that a combination of both of these factors is in play. We could, therefore, support a moderate increase in annual access limits for stand-by and extended arrangements insofar as that would help adjust upwards the yardstick by which average access could be judged. That the Fund's liquidity ratio is now quite high is a comforting factor, but as the Managing Director quite rightly points out, that situation could change quickly. We should, therefore, keep the liquidity situation under close review.

In agreeing to a moderate increase in annual access limits, we attach particular importance to the Fund's maintaining its catalytic role. The Fund was never intended to fill the financing gaps of its members, and we do not think that should change now.

It will be vital to ensure that in cases where higher access is granted, the reform effort is sufficiently strong to warrant that access. It has been said many times, but it is worth repeating, that policy conditionality is the most effective way in which the Fund can protect its resources. Conditionality may be painful, but it also brings benefits to the borrowing countries, in terms of both the reforms it assists and the more general investor interest it can stimulate in an economy; such capital flows can be particularly beneficial where they take the form of private direct investment. If access is not matched by conditionality, the Fund's portfolio would become riskier, which could lead to the need for a higher level of precautionary balances, and hence, a higher rate of charge. Access not matched by conditionality, therefore, has a very real direct cost to borrowing members. The indirect costs would accrue to all members and to the institution itself.

It is because we do not believe that conditionality would be sufficiently strong--ultimately working against the interests of both the Fund and the country concerned--that we cannot support an increase in the access limits for the STF. When we joined the strong consensus to establish the STF, we indicated that we thought 50 percent of quota was on the high side because of the limited conditionality attached to STF programs. It would be possible, theoretically, to agree to higher access now, if that conditionality were to be much stronger, but to do so would make little sense, because then we would be at or around the level of conditionality that applies to stand-by and extended arrangements. The STF is meant to pave the way to the Fund's normal facilities; it should do so in terms of both access and conditionality. We are also somewhat uneasy with what would be an important increase in the scale of what was always seen as a temporary facility.

Nevertheless, we recognize the important role that the STF has played in assisting several countries in transition. We could therefore support an extension of the deadline for the STF. But if some countries face large financing needs, the Fund's regular facilities are the appropriate modes of assistance. If higher annual limits for those facilities still prove to be insufficient to match the strength of reform efforts, we will have the opportunity to review progress after some time and to consider, say, increasing the cumulative limits.

Mr. Calderón made the following statement:

Today we are asked to explore alternatives that best fulfill the Interim Committee's desire to have the Fund continue to play a central role in the transitional economies, including through increased access, if needed, but, at the same time, retaining the catalytic role of the Fund.

In the statement by the Managing Director of April 8, 1994, on external financing requirements of transition economies and possible sources of financing, the financing requirements of the countries of the former soviet union (FSU), for the period 1994-96, were estimated at $186 billion. Of this amount, the Fund was assumed to provide $19 billion, and an unidentified gap of $49 billion remained. This scenario is called the baseline case.

In the current paper, the staff explores two other alternatives. In the first scenario, the resources are increased to the maximum combined access available under stand-by, extended, or enhanced structural adjustment facility arrangements and the STF. In the second, for countries that are not ESAF-eligible, annual access under stand-by and extended arrangements was raised to 85 percent of quota for three years and, for all countries, access under the STF was increased from 50 percent to 85 percent of quota. We will call these the maximum access and increased access scenarios.

We are firmly convinced that we must do all that is possible to carry out the Interim Committee's mandate, but with due regard to preserving the Fund's credibility and financial soundness. This consideration obliges us to ask a number of questions. The first question that comes to mind is, why do we need to increase access limits? Or, in other words, for what countries does the staff foresee that current access limits will become binding? This question is particularly relevant because, as the staff paper points out, with today's current access ratios stretched to the limit, the Fund would be lending countries of the former Soviet Union (FSU) $28 billion. Consequently, does the staff think that the FSU countries, on average, are going to borrow from the Fund more than the $28 billion mentioned?

If the case is made that a general increase in access is needed, this does not imply that an increase in STF access is also warranted. As a general rule, it is desirable that the Fund should, at all times, appear to treat its members evenhandedly. Would we not break that rule if we increased access to a specific, low conditionality facility? Would we not be seen as discriminating in favor of a particular group of countries? Moreover, if necessary, access limits could be raised more under stand-by and extended arrangements. Finally, even if we only raise access limits under stand-by and extended arrangements, we must make sure that effective access does not rise in a fashion which may--or even appear to--discriminate between members.

The next question is, what happens to the Fund if access limits are, in fact, increased because they become generally binding for FSU countries? In order to have a rough answer, we calculated three indicators: the liquidity ratio, which is defined as the quotient of adjusted and uncommitted ordinary resources to total liabilities; a regional concentration ratio or risk indicator, which we define as the quotient of outstanding Fund drawings to a particular region over total outstanding drawings; and a catalytic ratio, which shows the share of total financing requirements to FSU countries provided by the Fund. In Table 1 (see Annex), we present these indicators, at the end of the three-year period, 1994-96, for each of the scenarios outlined by the staff paper: the baseline case, the maximum access scenario, and the increased access case.

The liquidity ratio, which today is 167 percent, would fall in the baseline case to 80 percent. This would be close to what the Managing Director tells us in his statement is the traditional threshold for action in raising the Fund's quotas. If we want to go further than the baseline scenario, would we not be making a strong case for an increase in quotas? The regional concentration ratio increases to unprecedented levels. For example, during the worst year of the Latin America debt crisis and the year of the Fund's highest level of credit and loans--1985 1/--this region accounted for 35 percent of the Fund's total outstanding drawings. Even if the regional concentration ratio increases, on average, only to the baseline scenario level--around 50 percent--would this not be a signal that we should increase the Fund's precautionary balances? And, does this not imply that we have to change the system of burden sharing? At the same time, in the past, this chair has said that it will not shy away from new risks; however, we have also insisted that, after a certain point, the Fund should start thinking about requesting collateral.

Some could argue that Table 1 is an extreme case, which will most likely not happen. Consequently, let us assume that access is increased and that FSU countries, on average, only use half of the maximum feasible credit. The liquidity ratio, in the case of increased access, would still drop to 54 percent, and, therefore, the main conclusions stated in the last paragraph still apply.

The only way that increased access would not lead to the scenario described in Table 1 is if the unidentified financing gap of the FSU countries is substantially reduced. And, at least until today, the only credible way we can substantially decrease the financing gap is by a general, new SDR allocation. In other words, approving increased access and delaying decisions on a new SDR allocation and/or an increase in quotas, will most probably lead the Fund, by default, to the unthinkable scenarios presented in Table 1.

1/ We take the year of the Fund's highest level of credit and loans.

Mr. Shaalan made the following statement:

The main conclusion of the paper before us is that a temporary increase in both the annual access limit under stand-by and extended arrangements and access under the STF could provide sufficient scope for the Fund to meet the possible needs of the membership in the period ahead. I agree with this conclusion; I am not sure, however, whether such an approach to meeting the possible needs of the membership, or to be more precise, a segment of it, is absolutely necessary. Moreover, I do not think that one could say with any reasonable degree of confidence that expanding the Fund's financing role through the STF would not increase the riskiness of its portfolio to unacceptably high levels.

In coming to this view, and insofar as increasing the access limit under stand-by and extended arrangements is concerned, I was particularly impressed by the following observations, which the staff has made in the paper.

As in the establishment of the STF, access under stand-by and extended arrangements has been below the annual access limit for all countries.

In contrast to initial arrangements, access under subsequent arrangements for economies in transition was only moderately above the Fund-wide average.

Within existing access limits, and taking into account resource availability under the STF, the Fund has planned to assume a share in the financing requirements of transition countries, and other countries, that is well in excess of the share it had typically tended to assume.

One could hardly see, on the basis of the above considerations, a compelling case for increasing the access limits. It could, of course, be well argued that the case for raising the limits is suggested by the prospective financing needs of the economies in transition. But, here again, the picture that emerges when one considers some of the staff's observations regarding the prospective financing needs, is also less than clear-cut, to say the least. In particular, the staff's conclusion that "the current limits are not expected to impose constraints on the ability of the Fund to assist most members" is certainly reason enough to question the need for raising the limits. To be sure, this conclusion by the staff is promptly followed by some qualifications that may be seen as lending support to the proposal to increase those limits. Specifically, the staff refers to three cases in which higher access to Fund resources may be justified. These are cases in which potential financing needs are large in relation to quotas; cases in which conditions are conducive to undertaking economic liberalization at an ambitious pace; and cases in which, despite the progress achieved in stabilization and liberalization, there is a high degree of vulnerability to abrupt changes in market perceptions.

If there is justification for higher access to Fund resources in cases such as those described by the staff, and I believe that with the appropriate safeguards there is, that does not necessarily mean that there is a need for increasing access limits. Because in most cases access tends to be well below the limit, there is considerable scope for increasing access without raising the limits. And in those cases in which access beyond the limits is deemed necessary, the exceptional circumstances clause may be invoked.

This said, there is a sense in which the limits themselves may suppress, or may be seen as suppressing, the actual access to levels below what might otherwise be permissible under the policy on access. To the extent that is the case--and this is a point made by Mr. Waterman--I can support an increase in the access limits under stand-by and extended arrangements. Specifically, I can go along with the proposal to increase the annual limit under stand-by and extended arrangements to 85 percent of quota. Let me, however, add the following points.

First, the principle of uniformity of treatment should be adhered to scrupulously, and I agree with the Managing Director that the task at hand must be approached with an eye to maintaining evenhandedness in the Fund's treatment of all its members. I do not think in this connection, however, that the professed general applicability of the approach outlined by the staff would be promoted by the proposed retention of the cumulative limits, because "those members with very large financing needs generally have little or no exposure to the Fund."

Second, I think that we should keep well in view the full context in which the Interim Committee encouraged the Fund to continue playing a central role in supporting the economies in transition. To be sure, the Committee made reference to the possibility of increased access to Fund resources. But the Committee also underscored the importance of safeguarding the monetary character and catalytic role of the Fund. In this connection, I would stress that conditionality is the ultimate safeguard of the revolving nature of the Fund's resources, and of the effectiveness of its catalytic role. It should, therefore, be clear that higher access may be contemplated only where adjustment programs are sufficiently strong. Otherwise, the Fund would not only be risking its resources, but its credibility as well.

Third, I agree that higher access limits have the virtue of signaling to members the Fund's readiness to respond to their financing needs promptly, and on an appropriate scale. I think this should apply not only prior to the member's entering into an arrangement, but equally while under an arrangement. Members' circumstances do, at times, take a turn to the worse while under Fund arrangements, and when that happens, an assessment of the continued appropriateness of policies would obviously be called for. Such developments also call for the Fund to stand ready to augment access, as may be appropriate, on a case-by-case basis.

The proposal to extend the availability of the STF and to increase access under it presents us with a set of questions that go well beyond those raised by the possibility of increasing access under the Fund's regular facilities. These questions and issues were highlighted on a number of previous occasions, and there is no need to repeat them now. But, let me say that when the STF was introduced, its temporary or paving-the-way character was emphasized. In my view, this underlies the broad-based willingness to accept extending Fund credit under conditions that are less rigorous than those under the regular facilities.

Under the approach outlined by the staff, the same type of broad-based support would be needed to accept living with increased risk for a longer period of time. Whether such support will be forthcoming would depend critically on a package being presented in which the Fund does not shoulder an inordinately high degree of financing and risk. The proposal to establish cofinancing trust accounts could be an important element of such a package, and we would welcome the preparation of a detailed paper on this subject that incorporates the key features outlined by the staff. Existing and newly allocated SDRs could be an important source of funding under the cofinancing trust accounts. In this connection, we attach great importance to any proposals for increased Fund financing being presented in a well-integrated package that has, as a key element, a new general SDR allocation. Such an allocation, as we have long argued, is well justified on its own merits. But at this juncture, when the Fund is being called upon to devote increased attention to the special needs of a segment of the membership, an allocation, which has for some time been considered of vital importance by the vast majority of Fund members, would go a long way toward reconfirming this institution's commitment to the universality of its mission and responsiveness to the needs of the membership at large.

Mr. Zoccali made the following statement:

We remain convinced that the Fund can and should play a critical role in mobilizing financial support from the international community which is commensurate with the historic efforts of the large number of members making the transition to a market economy. Yet to do so effectively, its credibility must be preserved. Thus, the emphasis on maintaining evenhandedness in the Fund's treatment of all its members, particularly with regard to conditionality, and while safeguarding its catalytic role, cannot be overemphasized. The appropriate mix and timely availability of financial resources in support of strong adjustment and reform policies, calls for an integrated approach, including a general allocation of SDRs to rapidly meet part of the demand for international reserves to hold.

More specifically, on the question of access limits and prospective financing requirements for countries within and outside the transition group, the staff has provided strong arguments in support of the view that "the current limits are not expected to impose constraints on the ability of the Fund to assist most members." In addition, data for the period under review confirms that average effective access was much lower than the current limits. Consequently, we share the view expressed by Mr. Waterman that the way in which access is determined within those limits appears to be the constraint.

Although a combination of factors seems responsible for this outcome, a case also exists for higher effective access to Fund resources, by adjusting upward either the glass ceiling, or the annual access limits, in order to avoid routinely resorting to the exceptional circumstances clause, and more important, to provide confidence to members that their corrective and reform policies would not lack the necessary financing. Notwithstanding the potential impact on the Fund's liquidity and on the risk-concentration, highlighted by Mr. Calderón, we could, on balance, agree with a temporary increase in the annual and combined access limits of stand-by and extended arrangements.

The second part of the Managing Director's proposal, however, related to the STF, could actually undermine its important role. Although its extension would admittedly permit a better mixing of maturities, it could also be perceived as a departure by the Fund from its traditional incentive structure to accommodate the adjustment path of the slower performers in the group. A further expansion of STF access would send the wrong signal in terms of the established conditionality, and potentially pave the way for an unprecedented concentration of risk, conflicting both with the Fund's monetary character and its catalytic role.

Setbacks and delays can, nevertheless, be justified when serious efforts are being made to sustain the overall adjustment momentum. In that context, continuation of support within the present cumulative STF access level, for some time, even though the conditions are still not met for an upper credit tranche arrangement, merits further consideration. Triggering an actual increase in STF access by substituting it for other forms of financing raises other important issues, such as the Fund's preferred creditor status, and the financing of future provisioning requirements, which to date continue to be borne disproportionately by performing users of Fund resources.

A consensus in favor of a more quota-based distribution of the administrative, capital and provisioning costs associated with operating this institution is urgently required, particularly when the further accumulation of precautionary balances is being advocated by some chairs as the means of addressing the foreseen increase in the Fund's exposure, and its consequent concentration of risk. In this regard, specific guarantees for ensuring preferred creditor status should also be studied. An assessment by the staff on the impact of the World Bank's decision in 1993 to waive the negative pledge clause on a case-by-case basis might, in fact, provide useful insight as to whether its past and prospective use by FSU countries for securing new financing, should not trigger some form of specific collateral to be held by the Fund, particularly in light of the evolving nature of STF conditionality.

With respect to the concept of cofinancing trust accounts, our position remains essentially as expressed in the Board discussion on an allocation of SDRs and related issues (EBM/94/36, 4/18/95). Among the features of cofinancing trust accounts outlined in the staff paper, the definition of a member's official reserves continues to pose difficulty. A further paper on the issues involved, including the liquidity and budgetary implications of potential contributions and the assurances regarding repayment, would be deemed useful for making cofinancing trust accounts more attractive as a channel of additional resources, before discussing the modalities and prototype instruments needed to establish and operate them. A new general SDR allocation could considerably enhance the potential benefits to be derived from such a scheme.

In conclusion, the scenario that confronts the Fund today calls for a well-integrated financing package that can be broadly supported, so as to maintain an appropriate balance between members' needs and the universality of the Fund's mission.

Mr. Bergo made the following statement:

As a number of countries--in transition or others--embark with hope upon appropriately strong reform programs, there might very well be a need to increase their average access to stand-by and extended arrangements from the levels that have recently been the norm. I have no objections to fully utilizing the existing limits when in support of strong programs. I can also, although without much enthusiasm, endorse the proposal to increase the annual access limits.

I recognize that, so far, access limits have not been a limiting factor and that a recourse to the exceptional circumstances clause might be sufficient for handling cases that come up in the future. However, the argument that there is a need to strengthen confidence among the members--and in markets--in the Fund's ability to respond to large financing needs is valid. My support is based on the following qualifications.

First, it has to be understood that the decision to increase access limits would be temporary in character. Of course, all decisions on access limits are in a way temporary, but in this case, it should be explicitly understood that a decision to increase access implies an opening of a window of opportunity that will close within a specific time period. It should serve as an incentive for potential fast-track reformers to proceed with their reforms in order to take advantage of this opportunity.

Second, the need for an increase in access depends on the decision we take concerning allocations of SDRs. I hope the outcome of our long-standing deliberations will be known before we have to make final decisions on access limits.

Third, at this stage, my acceptance of an increase in the annual limit for stand-by and extended arrangements does not imply my support for an increase in the cumulative limits. It is not clear that there will be a need for an increase at this stage. The Executive Board should delay a review of the cumulative limits until some experience has been gained from an increase in the annual limits.

Fourth, an increase in access limits should not imply that the Fund, in general, takes on a larger share of financing than previously. The enlarged access should be applied to exceptional problems, but also the strength of the program must be exceptional; that is, conditionality for high access programs should be markedly stronger than what is now the norm.

The discussion thus far has been linked to the transition economies, but enlarged access would be open to the whole membership, provided that they meet the criteria. Here, we have to think about preserving the Fund's catalytic role; however, what is catalytic depends very much on the circumstances. In situations where the financing need is large, and uncertainty among other potential sources of finance is extreme, a larger share of Fund financing, provided that this is matched by a stronger program, may, indeed, increase the catalytic power of

Fund financing. If international lenders see a larger financing gap than can realistically be closed, they may see that as a risk factor in itself, and thus be less willing to provide any financing at all. In other cases, a large share of Fund assistance where the need is less pronounced and the programs not so strong, may weaken the incentives for potential providers of assistance to come forward. It should be our aim to increase the Fund's share only in those cases in which a larger share will strengthen the Fund's catalytic role.

Fifth, as calculations in the staff paper suggest, the liquidity ratio could fall sharply if a number of transition and other problem economies with large financing needs become successful in establishing strong programs worthy of enlarged access. Hence, the Fund must stand ready to increase quotas at an early stage, as it would be too late to do so when the ratio has already fallen to unacceptable levels. The possibility of "success," leading to rapidly increasing Fund financing, also underscores the need to review the Fund's income system and its protection against risk.

As far as the proposal to raise access limits on the STF is concerned, I am more hesitant. But, as this chair has stated earlier, I can agree to a prolongation of the STF for another year. I am also in favor of gradually strengthening conditionality as purchases are made; the present phasing modalities may be too lumpy. We should be reminded that the whole idea behind the STF is to pave the way for ordinary programs. I would welcome changes that could facilitate rapid progress toward a stand-by arrangement, but remain skeptical to increasing access limits, at least for stand-alone STFs. When purchases exceed 50 percent of quota, conditionality should be of approximate stand-by arrangement strength, anyway. With regard to stand-alone STFs, I could envisage perhaps three drawings: an initial tranche of 25 percent, plus two additional drawings of 12.5 percent each, with increasing conditionality and reviews. However, if a country proceeds to a stand-by arrangement, I would be willing to consider the possibility of one or two more STF tranches, provided conditions for STF drawings are still met and the program has the appropriate strength. In general, however, my authorities are skeptical about increasing access limits for the STF.

Finally, like Mr. Waterman, I can go along with the preparation of a detailed Board paper on the cofinancing trust accounts, but have not taken a position on whether to establish such accounts, or on the modalities of such arrangements.

Ms. Lissakers made the following statement:

Over the years, one of the Fund's greatest strengths has been the ability to respond quickly and effectively to the changing needs of its members and the world economy. Time and again, the Fund has played the leading role in addressing urgent financing problems. In the past ten years, examples include the initial response to the collapse of the former Soviet Union and the emergence of the new democracies; the meeting of emergency financing needs arising from events in the Persian Gulf; and the resolution of the debt crisis in Latin America.

The Fund is now confronted with a challenge that the Interim Committee has rightly characterized as an opportunity of historic proportions. The success of this effort may have consequences for the world economy as great as those that confronted the Fund's creators fifty years ago. We need to approach this issue with the same spirit of cooperation that launched the Fund at Bretton Woods, and has been a hallmark of its activities over the years.

The need for the Fund to assume a leadership role is especially critical at this time. The traditional creditor countries are now pursuing with increasing vigor the fiscal consolidation long advocated by the Fund. Consequently, they are confronted with unprecedented budget constraints at a time when pressures to address pressing domestic needs are mounting. At the same time, our experience with transforming economies indicates that the transition from command to market-based systems will entail longer adjustment periods and larger financing needs than were anticipated initially. In these circumstances, there is no real alternative but to rely increasingly on the resources and talents of the international financial institutions.

The Fund's central role will mean that it must do more to meet the financing needs of the transforming countries. This does not mean that the Fund should aim to achieve a specific target share of the financing. The circumstances in individual countries vary greatly in terms of their ability to implement the types of policies that the Fund could support, the size of their financing needs, and their ability to attract external resources from other sources. Moreover, I agree that the Fund must safeguard its financial integrity and monetary character. However, as the Managing Director noted recently, the monetary character of the Fund depends primarily on the purposes of Fund financing and less on whom it lends to, and the financial terms on which it lends. The best protection for the Fund's resources, and its most effective means of serving as a catalyst for other lending is the quality of its policy advice and the strength of the programs it supports. Consequently, providing greater assurance that the Fund is ready and able to support sound policies, and serious reform efforts with sufficient resources will remain its most effective safeguard.

With these general remarks, let me turn now to the staff's suggestions on access under the STF and stand-by/extended arrangements. At the outset, I want to make clear that I agree with the direction the staff is indicating, although we would follow a slightly different path.

The STF has proved to be a useful vehicle in enabling countries to initiate the reform process in a manner consistent with their needs and capabilities. There is growing recognition, however, that the path it provides toward the Fund's regular program is longer, bumpier, and will take more time to traverse than was anticipated when the STF was created. Farther east, the problems apparently grow greater, reflecting the extent and duration of reliance on central control of production and distribution.

The Executive Board's recent discussions on reform in the transforming economies highlighted several factors that affect the process: the amount of investment needed to restructure production and distribution systems and the domestic resource base available to meet this need at a time when economic activity may have collapsed; the magnitude of the trade shock because traditional channels for trade, investment, and finance have been disrupted; the capacity of government to mobilize domestic savings in the face of a deteriorating revenue base and new expenditure requirements to meet social needs; and the ability of political institutions to build domestic consensus on reforms and the adequacy of administrative machinery to implement reform.

I share the staff's view that, in these circumstances, there is a need to consider extending, augmenting, and adapting the STF. In particular, a good case can be made to increase access to the STF and strengthen the linkages to regular Fund programs.

I am concerned, however, that the staff's proposal of five STF tranches is unnecessarily complex and risks dissipating the effects of the increased access. The purpose of the increased access is to provide additional assurance that needed financing will be available to support the reform effort. However, disbursing the resources in small dollops over an extended period would bring too little resources to bear, and could delay movement to a regular Fund program. Under the staff's proposal, for example, the period from the initial STF drawing to a stand-by arrangement could be up to four years, during which time the Fund would provide up to 60 percent of quota. Such an approach could create the perception that the Fund lacks confidence that the adjustment effort can be sustained, either because the borrower is unable to implement the necessary reforms or because sufficient financing is not available. It would send the wrong message to both the borrower and other lenders.

I would suggest a simpler approach that would provide greater confidence to the borrower and donors, and meet the Fund's interest in moving the country toward a regular Fund program as quickly as possible. Thus, STF access could be increased by adding a third tranche that would be available when a stand-by or extended arrangement is approved by the Executive Board. The linkage to a regular Fund program would respond to concerns that increased STF access would weaken conditionality, as the borrower would, in effect, be required to meet the Fund's standards for upper credit tranche programs. At the same time, however, it would provide a means of front-loading the regular program, as occurs with compensatory and contingency financing facilities (CCFFs) and stand-by arrangements, and effectively extend maturities on Fund financing at a time when the financial position of the borrower is under the greatest strain. The linkage of additional STF financing to regular Fund programs would also provide a useful incentive for the borrower to implement stronger policies.

The access issues are somewhat different with regard to stand-by and extended arrangements, compared with those related to the STF. As the staff paper notes, the annual access limit of 68 percent of quota has been reached in only a few cases, and only a small number of countries are near the 300 percent of quota cumulative limit. This reflects the fact that the staff has applied the guidelines on access in individual cases in a cautious manner, so that the average size of programs has been well below the permitted maximum, about 34 percent of quota for stand-by arrangements and 22 percent for extended arrangements since 1992. However, the size of Fund programs will need to increase, on average, in order to permit the Fund to undertake a larger share of the financing responsibility.

This could, of course, be accomplished by modifying the guidelines on access to give the staff a more explicit mandate for increasing program size under the current limits. This approach would be akin to the first option in the staff paper. However, such an approach would entail the loss of useful flexibility in considering the situation of individual countries, including their financing needs and adjustment efforts. Therefore, I would prefer to rely on the more traditional approach of increasing the annual limit to raise the glass ceiling and to provide the staff more headroom in implementing the guidelines.

The size of the increase in the annual limit is, of course, a matter of judgment, but should be large enough to provide sufficient flexibility and a clear signal of the Fund's intentions. My preference would also be to have the increase in the annual limit for stand-by and extended arrangements roughly the same as the increase in access permitted under the STF. Based on the recent relationship between the size of programs and the annual access limits, the expectation of the Board might be that programs, on average, would be about half the annual access limit. However, care would have to be taken to ensure that the combination of the third STF tranche and a regular Fund program did not result in excessive front-loading of the program. This could be accomplished by phasing the disbursements under the regular program to take account of the STF purchase, as is now done with CCFFs and stand-by arrangements. The Board would, of course, want to continue the practice of regularly reviewing Fund programs to assess the effects of increased limits on program size and performance, and the impact on Fund liquidity.

An increase in access and the Fund's role in meeting members' financing needs will have important consequences for the institution's liquidity and risk profile. However, the Fund is well placed to undertake this responsibility. The Fund has about SDR 70 billion in loanable resources, and the current liquidity ratio is at an historic high of about 168 percent. The staff estimates that raising access to 85 percent of quota under stand-by arrangements and the STF would double outstanding Fund obligations over three years to about SDR 38 billion compared with the base case. As a result, the liquidity ratio would fall sharply over the period to levels that are well below those that existed at the times of past quota increases. However, these estimates should be treated with considerable caution. They are based on the mechanistic assumption that the full amount of the increased access would be utilized, which in practice rarely occurs. Moreover, forecasts of Fund liquidity have traditionally been subject to wide margins of error in view of the inevitable uncertainties regarding the pace of Fund lending, the balance of payments, and the reserve positions of potential creditor countries, and the Fund's ability to borrow.

My authorities have always supported an increase in Fund resources when there is a clear need. I have no doubt that they will continue to do so in the future. However, an effort to seek a prior commitment to cross the quota bridge before the river is even in sight could be counterproductive. It would create the same kind of problem as occurred with the child who cried wolf too often. When the wolf is actually at the door, no one believes him.

Similarly, the Fund is well positioned to undertake increased risks, although I am not so sure that what is being proposed will actually result in much greater risks than the Fund has faced in the past. The Fund's reserves and precautionary balances are at historic levels, and we will be having a discussion next month on the appropriate size of such balances and their financing. The strengthened arrears strategy is in place and functioning, as intended, to encourage members in arrears to meet their Fund obligations and to discourage future arrears cases. An increase in Fund lending to transforming economies may produce some concentration in Fund claims on a few countries. However, the Fund traditionally has had a large concentration of lending to a few countries. In 1984, for example, when Fund lending was at an all-time high, the five largest borrowers accounted for more than 40 percent of outstanding obligations under the General Resources Account (GRA). In 1990, as Fund lending fell off following the debt crisis, the ratio rose to more than half of where it stands today. Moreover, the problem of arrears has not been related to the largest borrowers, but rather to smaller countries.

Nevertheless, I agree that prudence requires that the Fund proceed with due diligence, both in terms of the amounts it provides and the conditionality of the programs it supports. In this regard, it is important that the World Bank also do its part by substantially expanding lending to transforming economies. The scope to do so clearly exists with current World Bank lending activity well below the sustainable level. I would encourage management, as well as those Fund Directors who sit on the Bank's Board, to urge the World Bank to step forward in an expanded cooperative effort with the Fund.

I would like to say only a brief word about the staff's suggestions regarding the security and liquidity of creditor claims on the cofinancing trust accounts, in light of the Chairman's suggestion that we defer substantive discussion on this issue. There seems to be an inherent conflict between the goal of reducing the risk to the Fund from increased lending to transforming economies, and the creditors' ability to treat claims on the cofinancing trust accounts as nonbudgetary monetary transactions. In the case of the United States, for example, our ability to treat quota transactions and loans to the Fund as monetary operations that do not result in net budget outlays is based on the fact that the U.S. reserve position in the Fund is fully secured by the Fund's assets, and can be mobilized automatically in case of need. However, the staff's goal of having cofinancing trust accounts creditors bear some of the risk of lending to transforming economies must mean that cofinancing trust accounts claims would not have the same liquidity, and security, as Fund reserve positions. In these circumstances, any U.S. loans to the cofinancing trust accounts would be treated as budget outlays and be subject to pay-as-you-go requirements. We do not see a way out of this conundrum that would make U.S. participation in the cofinancing trust accounts a live possibility.

Mr. Kiekens made the following statement:

There is no doubt that the STF is serving a useful purpose: for several countries it is paving the way to a subsequent, more traditional Fund arrangement, and for others it is also providing increased access to Fund resources, in conjunction with a stand-by arrangement. I agree with the staff that some countries have had difficulty changing from an STF to a stand-by or extended arrangement, and that others clearly need more time to prepare themselves for a stand-by or extended arrangement. I, therefore, fully agree that there is a need to extend, modify, and augment the STF.

I support extending the life of the STF by one year. This would enable the Fund to continue playing a central supporting role for countries that have thus far been unable to make much headway on the difficult road to a market economy. I also support modifying the STF by replacing the 12-month rule for the second purchase of 25 percent of quota. And, I favor augmenting access under the STF in order to better reflect the tremendous challenges involved in the transition process, especially for countries that are disadvantaged in terms of quota size. Creditors' concerns about such increased access can be allayed by a matching reinforcement of STF conditionality.

During last year's discussions leading up to the creation of the STF, this chair spoke in favor of larger access, to be accompanied by stronger conditionality and a more back-loaded pattern of purchases. The staff now proposes, for the revised STF, an initial purchase and four subsequent purchases, all of which would be subject to Board review. This would not only add heavily to the Board's work load, but even more important, could convey the impression that the STF is to be viewed as an independent facility, only incidentally linked to a subsequent traditional Fund arrangement. I would prefer a pattern of three rather than five purchases under the STF, in order to avoid such an impression. The sequencing for such a pattern would then be the present two tranches of 25 percent of quota each, followed by a third tranche of 35 percent of quota, which would become available on approval of a traditional upper credit tranche arrangement. The resulting back-loading of purchases would encourage members to conclude a stand-by or other arrangement as soon as possible after the second STF purchase has taken place. This pattern would also embed the additional access more firmly in the conditionality framework of a stand-by arrangement. If a single disbursement of 35 percent of quota is deemed too large, an alternative would be to split the 35 percent purchase into two purchases of 17.5 percent each, linked to the first and second purchases under the stand-by arrangement. Further tranching of the STF disbursements would risk creating a complicated situation requiring repeated escalations of conditionality for each additional tranche, in order to gradually match the standards of a regular stand-by arrangement.

Singling out a subset of the membership, namely, the transition countries, and granting them privileged access to Fund resources does not, at first sight, seem to respect the principle of equal treatment. But if we examine the issue from a broader perspective, we realize that the Fund has always had a policy of assisting particular groups of member countries--and assisting them promptly--in case of new types of problems. The ESAF is a case in point, as was the oil import window of the CCFF, to name but two. The STF is the most recent example. What has to be ensured is equal treatment for all members under comparable circumstances--in other words, evenhandedness.

As the staff notes, there are other member countries besides the transition countries, whose potential needs are large in relation to their quotas; equal treatment means we have to provide adequate access to those members as well. I, therefore, deem appropriate the proposal to raise, temporarily, the access limits for stand-by and extended arrangements from 68 percent to 85 percent of quota. As in the case of increased access under the STF, conditionality is the key issue. The Fund must not be perceived as lowering its conditionality standards in order to provide adequate financing to a subset of the membership. One can certainly not expect that increasing maximum access by 17 percent will automatically result in raising average access, and the Fund's financial commitments, by anything close to that amount.

Ultimately, only one yardstick exists for measuring whether it is appropriate to increase access: will the increase contribute decisively to meeting the perceived balance of payments needs of member countries? If we decide to increase access limits, it is not primarily because the Fund now possesses greater liquidity, but because the needs of the membership at large are now seen to be greater than before. Increasing access temporarily does not imply that the problems that the additional financing is intended to address are necessarily temporary. If the adjustment problems of a sizable number of countries turn out to be protracted, continuation of enlarged access would be warranted. And if this threatens the Fund's liquidity position, a quota increase or additional financial resources for the Fund, of bilateral or multilateral origin, is the only logical response.

This chair continues to believe that an SDR allocation can play a useful role in supporting the adjustment efforts of a sizable number of countries; directly, by serving these countries' reserve needs; and indirectly, by providing monetary resources to countries in a position to rechannel them to those in need. In this connection, an SDR allocation of 36 billion would, in effect, permanently increase Fund-related resources by some 25 percent of quotas, compared with the temporarily increased access of 17 percent of quotas that would result from the current proposals.

On the subject of rechanneling, and the role of cofinancing trust accounts in this process, I have already submitted my initial comments at our April 18 meeting. I will reserve further comments until we discuss the next staff paper on this topic.

Mr. Torres made the following statement:

When the Interim Committee defined the task of supporting a large number of our members in their transition to market economies as one of historic proportions, it was calling for special action. One does not qualify a situation as historic just to conclude that what is needed is to do business as usual. I agree with the Interim Committee in their definition of the present task as one of historic proportions, but I believe that to act solely or unilaterally on the issue of access limits to Fund resources would be equivalent to doing business as usual.

To measure up to the task we are facing, we need a comprehensive package that should include at least four elements: first, a new general SDR allocation; second, an increase of access limits to Fund resources; third, a better-defined link between the STF arrangement and other Fund arrangements; and fourth, a clear commitment by other bilateral and multilateral creditors to act in conjunction with the Fund. The fact that we have to consider all these factors, one by one, does not mean that they should not be part of a global and comprehensive arrangement. Moreover, this is a good opportunity to reach an agreement between all members, about the difficult issues that we have been discussing for a long period.

On the specific issue of access limits to Fund resources, let me begin by reiterating the principle that the institution should ensure that there is adequate financial support for countries where there are assurances of strong policies. There are several ways of doing this but, certainly, if we are to maintain uniform treatment for all Fund members, the best way is to increase annual access limits. For many years we have argued that until Fund quotas are commensurate with the size of the payment imbalances of member countries, the Fund has to rely on a policy of enlarged access. Therefore, we support the proposal to increase the annual access limits applying to stand-by and extended arrangements, from 68 percent to 85 percent of quota.

> This shift would recognize that payment imbalances in many member countries are severe, and that a large majority of developing countries and transition economies are likely to require substantial external inflows to finance their current account deficits and meet principal payments on external debt; that only a few developing countries have regained limited access to the voluntary capital markets; that strong adjustment programs need to be supplemented with official financing to ensure an orderly transition; and that structural reforms require adequate amounts of financial support to ensure perseverance with the adjustment effort.
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> With regard to the STF, we might agree with a moderate extension and enlargement of this facility if its character of paving the way is better defined and assured--the conditionality that applies to the STF should come closer to the one that applies to the other regular facilities of the Fund. Otherwise, we may risk the credibility of the institution, which no doubt is its best asset.
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> The fourth element of the comprehensive package I mentioned is the commitment of other bilateral and multilateral creditors to act in a coordinated manner with the Fund. Among other initiatives, the idea of cofinancing trust accounts may have a great role to play here. Although the cofinancing trust accounts should be implemented on a voluntary basis, I foresee substantial progress if concrete commitments to these accounts by particular countries are made simultaneously with the definition of the new SDR allocation, the increase in the access limits to Fund resources, and the conceptual refining of the STF.

The Director of the Policy Development and Review Department said that the interpretation of the staff's proposal by Ms. Lissakers, that as much as four years could elapse between the first purchase under the STF and an agreement on an upper credit tranche stand-by arrangement, was not the intent or the spirit of the proposal. The intent in entering into any STF operation was to establish a policy framework and provide the technical and other assistance to enable the country to move as rapidly as possible to a stand-by arrangement. That was clearly the underlying intention of the STF in its original formulation, and that was how the staff envisaged the STF would operate following the proposed modifications.

The alternative process described in the staff paper was intended for cases in which, for whatever reason, a rapid conversion to an upper credit tranche arrangement did not prove possible, the Director remarked. The first STF purchase would continue to be made on the basis of an expectation of agreement on such an arrangement, but experience had shown that in some cases--owing, for example, to slippages or inadequate institutional capacity--such an agreement might take longer to realize. It was in that context that the staff was proposing the establishment of a mechanism through which the Fund could stay involved financially while the country, in close cooperation with the Fund, established the necessary program and prior actions to move as rapidly as possible to an upper credit tranche arrangement. It was not the intention that the proposed additional STF purchases be made at six- or twelve-month intervals; the mechanism was very much intended to retain the paving nature of the STF. With that in mind, Directors might wish to consider whether some modification of the staff's proposal would be useful; for example, the period within which the four additional purchases would be made could be reduced.

Mr. Waterman said that the staff paper and the Managing Director's statement set out the issues very clearly and were helpful in focusing the debate. He agreed very much that the Fund had an important, if not central, role in helping the countries in transition, and he could agree with much of the staff's proposal, including extending the STF and in respect of the proposals to increase annual access limits for stand-by and extended arrangements.

As he had indicated in his statement, Mr. Waterman commented, the main concern was the basis for an expansion of the STF. The complexity of the staff's proposal and the implicit delay in moving countries to normal Fund conditionality were somewhat surprising. While he took the points made by the Director of the Policy Development and Review Department, he would like to see a faster move to normal Fund conditionality for countries with STF programs. His concerns would largely be met if any expansion of the facility were along the lines that had been detailed by a number of other Directors, namely, one additional tranche firmly linked to a stand-by arrangement or one additional tranche with normal Fund conditionality.

Ms. Lissakers noted that several speakers had raised questions about the appearance of special treatment and excessive regional concentration of Fund resources. In her view, those sentiments were somewhat ironic given the history of the Fund's extraordinary efforts on Latin America's behalf in the 1980s, including the Brady Plan, and the resulting high concentration of resources. With regard to the issue of special treatment, she agreed with Mr. Kiekens that the Fund had in the past rightly tried to adapt its resources to the specific needs and situations of its members in order to serve the membership; the enhanced structural adjustment facility and the compensatory and contingency financing facility were only two examples. Clearly, adaptability was a strength, not a weakness. On the regional concentration issue, it was not clear to her that geography played a role in the Fund's financial position; the strength of the Fund's portfolio depended on the strength of conditionality and of specific programs.

Several statements had mentioned the possibility of seeking collateral from members drawing resources from the Fund, Ms. Lissakers recalled. Such an approach was not unprecedented, of course. The lesson of history in that respect was that if adequate collateral, sufficiently liquid in nature, were available from sovereign borrowers, they probably would not need to borrow from other sources.

Mr. Calderón said that his chair had not backed away in the past from the risks involved in the Fund's increased involvement in the countries of the former Soviet Union, and would support further Fund involvement in those countries. However, there were some concerns about the Fund's main financial indicators, such as the liquidity ratio. In the Managing Director's statement on the external financing requirements of transition economies at EBM/94/34 (4/18/94), the financing gap of the countries of the former Soviet Union had been estimated at $49 billion, taking into account Fund involvement of $19 billion. The gap had to be filled somehow; if it were not to be filled from bilateral sources of financing, the gap must be filled by either the Fund or through the cofinancing trust accounts that would channel resources following a new SDR allocation.

Mr. Shaalan recalled that, on two separate occasions, a member had drawn from the Fund on the basis of an offer of collateral. The first occasion involved a gold pledge by the member, and the second was based on a weaker guarantee provided by industrial countries.

The Chairman remarked that cofinancing trust accounts were not intended to be the focus of the present discussion, and the Board would have an opportunity to discuss the issue on the basis of a staff paper. Nevertheless, he would note that the Fund was again being invited to make significant efforts to adapt itself, to take more risk, and to increase its share in global financing. Clearly, the world was at a historic juncture, and such a situation called for something more than business as usual. Indeed, the present discussion appeared to reflect the Board's desire to move the Fund in that direction. At the same time, it would not be unreasonable to expect the membership to move at least part way in that same direction. With that cooperative spirit in mind, he had suggested the establishment of cofinancing trust accounts. He recognized the concerns of those who saw drawbacks in his suggestion, such as the concern that cofinancing trust accounts would not be backed directly by Fund resources, and would therefore be less liquid, possibly necessitating parliamentary approval for the participation of some members. Nevertheless, his suggestion contained important elements that should allay those concerns: cofinancing trust accounts resources would be used only for monetary financing; would be backed, in the same way as ESAF resources, with a pledge to make all possible efforts to ensure the liquidity of cofinancing trust accounts claims; and, if needed, the Fund would utilize all of its resources, including, gold, to back those claims. Therefore, he would encourage Directors not to close that particular avenue before first having had a chance to discuss his proposal fully.

Mr. Kagalovsky made the following statement:

> I welcome the Managing Director's statement on the role of the Fund in financing the economies in transition and the staff paper on the subject. My authorities greatly appreciate the efforts of management to find the best way for the Fund to play its leading role in supporting a large number of its members in

making the transition to a market economy. I agree with the Managing Director that we must approach this question with an eye to maintaining evenhandedness in the Fund's treatment of all its members. Evenhandedness and equity in Fund policy is the first priority of my authorities, which is why they welcomed very much the Managing Director's proposal to make a special amendment to the Articles of Agreement, that will offer us the possibility of resolving the so-called equity issue and allocate SDRs to those members that did not participate in previous allocations. We will discuss SDR issues separately, and soon, I hope.

The proposed increase in access is obviously urgent and important. It provides the possibility of meeting, if needed, the financial requirements of every Fund member in a difficult reserve position. This is the appropriate time to make such a change, particularly taking into account the fact that the Fund's liquidity ratio is now very high.

My authorities consider the proposed increase to 85 percent of quota in the access limit for stand-by and extended arrangements and the extension and enlargement of the STF as a step in the right direction, but a moderate one. I agree with those who think that because of insufficient financing from other sources, the Fund should provide a relatively larger share of total financing needs to its members that are trying to implement strong stabilization programs in a difficult financial situation. An increase in the Fund's share of financing will create positive feedback, and will encourage other potential creditors to give more money, eventually enhancing the Fund's catalytic role. Taking into account the prospective financial needs of the transition economies, and some other Fund member such as South Africa, a bigger increase seems more appropriate at this stage. Therefore, my authorities propose to increase the access limit for stand-by arrangement to 100 percent. This increase will be sufficient to provide confidence to all members that the Fund will be able to respond to their needs quickly, and on an appropriate scale, in support of strong measures. This same access limit, 100 percent, must be applied to the STF.

I support the staff's suggestion to extend the expiration of the STF to the end of 1995, but I have found unnecessarily complicated the proposed scheme for the use of the resources. I appreciate the staff's idea to stimulate the countries that have already received two STF tranches, but a final purchase of 5 percent of quota would not seem likely to improve very much the credibility of their stabilization efforts. Similarly, offering other countries the possibility of several small purchases of 15 percent each, after an initial purchase of 25 percent, does not seem useful. I would propose four purchases of 25 percent of quota each, with each purchase made after three months. The same rules should be applied to stand-alone purchases and purchases linked to a stand-by arrangement.

The staff proposal on cofinancing trust accounts is extremely interesting. The advantage of cofinancing trust accounts compared with other forms of bilateral assistance is that they are strictly linked to Fund-supported programs. This is the linkage we need in order to create an appropriate conditionality. Another advantage is voluntary participation--the free choice of every Fund member to contribute or not to a cofinancing trust accounts. Loans under cofinancing trust accounts will be untied and linked directly to balance of payments financing under the program. I want to stress that this is not the case when a country supports its own industry and gives loans to other countries to finance its own exports; rather, it is untied balance of payments support for the program-implementing country. In that case, these credits must have less risk than export support credits, even if they have the apparent disadvantage of being incorrectly labeled foreign assistance. That is why my authorities consider it very important that the Fund provide the necessary assurances regarding payment. There are some ideas on that issue in the staff paper, and I would appreciate it if the staff could elaborate on them.

In referring to the STF, many speakers seemed to equate this facility exclusively with the countries of the former Soviet Union. Of course, more countries--the so-called countries in transition--were eligible for the STF. For operational reasons, I usually use the world economic outlook definition of this concept, which lists 28 such countries; two additional countries, Viet Nam and Cambodia, have received STF purchases. It was important to be cautious, therefore, in speaking about the countries concerned.

My next comment concerns the concentration of the risks in different regions. According to the most recent paper prepared by the staff on the Fund's liquidity position and financing needs, the concentration of Fund lending was somewhat more complicated. Indeed, Fund lending to the countries of the Western Hemisphere represented 38 percent of the total in 1985, 5.6 percent in 1990, and was projected to reach 29 percent in 1995. Seemingly, the Fund has been successful in overcoming this problem when there is an urgent need to help some countries. In fact, that was why the Fund was created 50 years ago--to successfully overcome the challenges that from time to time occur in the world economy.

Mr. Posthumus made the following statement:

Let me say at the outset that I take the Interim Committee's statement that the transition to market economies is a task of historic proportions, deserving the full and concerted support of the international community, as the starting point of my position.

I am concerned, therefore, by the more limited statement of Ms. Lissakers that "the Fund is now confronted with a challenge which the Interim Committee has characterized as an opportunity of historic proportions." It is the international community, not the Fund alone, that was mentioned by the Interim Committee, and rightly so. The U.S. approach seems to substitute monetary resources for budgetary resources, with the argument that "the traditional creditor countries are confronted with unprecedented budget constraints." Fund resources should not substitute, but catalyze, budget resources. I hope that the other Group of Seven countries in this case will not follow the lead of the United States.

I agree with Mr. Bergo, Mr. Kiekens, Mr. Torres, Mr. Zoccali, and Mr. Waterman, in fact, with all the other statements in this respect.

Now that it is clear that the external financing requirements of the countries in transition will be substantial for a long time, it should be obvious that a considerable contribution should come from official creditors and donors. When presenting estimates about the future financing gaps of the countries concerned, the staff should make an effort to show that the envisaged increase in annual access limits would, indeed, help address the financing problems. The Fund should therefore seek enhanced assurances from the donor community, in particular the United States, Japan, and the EU, that their contributions will indeed be committed and disbursed. The Netherlands stand ready to continue balance of payments support within the Group of Twenty-Four/EU framework.

I now come to the specific proposals by the Managing Director. In programs, conditionality is the most important contribution of the Fund, not the Fund's money. I agree that policy conditionality is the most effective way in which the Fund can protect its own resources. At the same time, the guiding principle must remain that strong programs deserve substantial financial support, also from the international community. Mr. Waterman fears that this principle cannot be maintained in the case of the proposed increase in access for the STF. Obviously, there is tension between raising STF access limits and stretching out the program period, on the one hand, and keeping sufficiently strong conditionality for paving the way to the Fund's normal facilities, on the other. I doubt whether an STF in five tranches is the solution. The danger is that the STF would become a facility in its own right inviting countries to take a gradualistic, low-conditionality path. The STF should pave the way to regular arrangements. Therefore, I see merit in only one additional STF purchase, closely linked to the first purchase under the stand-by arrangement.

In earlier discussions on access limits, we underlined the necessity of the Fund preserving its monetary character, a perception shared by the Managing Director in his statement. This has the following implications: First, cumulative access limits should approximately be in line with the self-financing ratio, which the staff has estimated previously at about 250 percent of quota. As the self-financing ratio has probably decreased because most new members are debtor countries, I would consider an increase in the cumulative limit to be inappropriate.

Second, any support to member countries should remain within the Fund's longer-term financial capacity. This implies that membership should stand ready to increase Fund quotas if the liquidity position declines to close to its traditional threshold, and I fully support the Managing Director's appeal in this respect. However, given the fact that long preparation periods precede actual quota increases, initiation of this process should not wait until the traditional threshold is approached. Therefore, we should urge a commitment by the Interim Committee to a timely quota increase. Moreover, the proposed increases in access should be temporary. The STF should only be extended for one year, and enlarged access, under the general facilities, should be restricted to, at most, three years.

On this basis, and taking into account the Interim Committee's conclusions, as well as the evidence in the staff paper--Table 2--documenting that in about half of the transition countries, annual access limits were reached or exceeded during 1990-92, I support the Managing Director's proposal for a temporary increase to 85 percent in the annual access limits for stand-by and extended arrangements, and support an extension, and some enlargement, of the STF, but in the form I suggested.

A greater financing role for the Fund requires protecting its financial health. In particular the proposed substantial increase in access to the low-conditionality STF, implies increased risk-taking by the Fund. This underlines the necessity of the Fund continuing its present policy of building up precautionary balances, within the framework of a better burden-sharing system than the one we have had thus far. This is perhaps a better approach than asking for collateral.

Finally, I am not convinced of the merits of cofinancing trust accounts, but if there is time to prepare a detailed study on this issue, I would not object to such a study.

Ms. Lissakers, responding to Mr. Posthumus' comments about budgetary constraints, said that budgetary constraints in many creditor countries actually limited their ability to substitute budgetary resources for monetary resources. Moreover, many of the countries in transition had foreign exchange reserves equal to between only one week and two and one half weeks of imports; and even that depressed level of imports was neither normal nor adequate for growth. Clearly, those countries needed additional balance of payments financing, which was what the Fund was being asked to provide, in keeping with its traditional role. Her authorities were fully prepared to provide substantial sums of budgetary resources for project financing, export credits, suppliers' credits, technical assistance, and meeting basic human needs where there was a need. The Fund, in turn, was being asked to step in and provide more resources in a form that met the traditional criteria of the Fund and where there was a clear and undeniable need.

Mr. Posthumus said that the point he had tried to make was that both sources of financing were necessary. In some of the statements for the present discussion, excessive weight had been given to the argument that budgetary constraints prevented some countries from providing the necessary assistance. Moreover, he did not accept the premise that it was the role of the Fund to provide balance of payments assistance while donors provided only projected-related assistance; balance of payments assistance was merely a more efficient way of extending assistance.

Mr. Al-Jasser made the following statement:

When we discussed the issue of access limits last October--less than eight months ago--a substantial majority of speakers were of the view that current access limits were appropriate. Indeed, some speakers felt that the access limits were overly generous. The arguments that were advanced by various speakers, to reach this assessment, went along the following lines:

The Fund was fulfilling well its catalytic role; the access limits were not constraining the provisioning of Fund financing; if the access limits became constraining, then the exceptional circumstances clause could be invoked; the comfortable liquidity ratio provided the Fund with room to maneuver in providing higher actual access when needed; the STF had been created to address the special needs of economies in transition by effectively increasing their access; and an adequate liquidity position needed to be maintained over the next few years.

These were persuasive arguments in October, and they continue to be persuasive today. Granted, an argument could be made that the financing needs of the economies in transition have proved to be higher than expected. It would be a quantum leap to conclude, however, that this calls for changing our access policy. Rather, increasing actual access with appropriate conditionality, within the current access limits, would adequately support the adjustment efforts of our membership, while at the same time preserving the monetary character, as well as the catalytic role of the Fund. Nevertheless, if it is deemed necessary to send a signal of reassurance and confidence in the Fund's commitment to helping our members in transition, then I could agree to a symbolic increase in annual access limits under stand-by and extended arrangements. This signaling effect is akin to the signaling effect of official intervention in the foreign exchange markets; that is, it would not attempt to change the fundamentals.

It is well explained in the Managing Director's statement that as we contemplate the approach of the Fund at this juncture, it is important not to lose sight of two paramount considerations: first, we should stand ready to help members design credible programs of adjustment and to provide the necessary financing to catalyze financing from other sources. I hasten to add that our catalytic role here is not a narrow quantitative concept. The Fund's involvement should, as it usually does, catalyze confidence in the policies adopted by the member, and in its determination to persevere with adjustment.

Second, while performing its catalytic role in its broadest sense, the Fund should "proceed with due diligence both in terms of the amounts it provides and the conditionality of the programs it supports," to quote Ms. Lissakers. This institutional concern is heightened by the possible, unprecedented impact of the proposals before us on the risk profile of the Fund. For example, the sharp decline in the Fund's liquidity ratio, and the high regional concentration that could result from an increase in access limits, as noted by Mr. Calderón, could undermine the monetary character of the Fund. Clearly, the soundness of the Fund's financial portfolio is necessary to catalyze the needed support for the economies in transition and the rest of the membership. Financial markets and Fund members should always be confident of the prudence of Fund financial activities. Otherwise, we would risk undermining confidence in the Fund's judgment of risks, and in its ability to respond to future crises. Moreover, a perception of laxity would hinder the Fund's ability to raise funds in the future, be it through raising quotas or borrowing from members' central banks. It goes without saying that negative perceptions of the Fund would have serious ramifications for the stability of the international monetary system.

Integrating the economies in transition into the world economy is one of the most important challenges facing not only this institution, but the entire world. A successful transition would provide enormous welfare benefits to all. It is in this spirit that the Board approved the STF, and it is also in this spirit that I can be persuaded to support its extension, but not the proposed changes to its "paving" character or its access limits. The arguments presented by Mr. Waterman and Mr. Zoccali in this regard are very pertinent. However, if there is a strong desire for the provision of unconditional, or less conditional resources, then we should not attempt to reinvent the wheel. The SDR is a better vehicle, with many good attributes, and it is in the spirit of cooperation that I hope the Board will support a moderate general allocation of SDRs, which would partly satisfy the liquidity/reserves requirements of the economies in transition, as well as of a significant number of our membership. Such an allocation, followed by an appropriately designed redistribution mechanism, could provide the economies in transition with substantial resources, without undermining the Fund's liquidity, without putting pressure on the fiscal position of the donor countries, and without unduly sacrificing conditionality. In this connection, I can support further work on the cofinancing trust accounts.

Mr. Geethakrishnan made the following statement:

When the proposal for setting up the structural transformation facility was brought before the Board one year ago, this chair had no hesitation in wholeheartedly supporting it. Many of the countries concerned faced the stupendous task of having to move from a totally closed economy, and often without the benefit of adequate institutional infrastructural support, to a market economy. A strategy with front-loaded quick disbursements was clearly called for, and the STF was designed to meet specifically this requirement. The STF has played a useful role in all those countries that have availed themselves of this facility, and I am pleased by the manner in which this facility was operated and utilized.

During the discussions on the Fund's income position, some chairs drew attention to the concentration of lending by the Fund to the countries of the former Soviet Union and Eastern Europe as the single largest group of countries availing themselves of Fund support, as if this were, in itself, a major minus point for the Fund. I would consider this more a geographical accident in the historical setting and nothing more. I refer to the earlier discussion to draw a distinction because I think Ms. Lissakers said some Latin American chairs have expressed this view now, but this view was expressed not by the Latin American chairs on the earlier occasion, but by some of the industrialized countries, including the United Kingdom. There was a time when Latin America had this position, and there was also a time when Asia was the largest user of Fund resources. Such changes, with some part or another of the globe becoming the focus of attention, at some point of time, is in the nature of things and I do not attach any more importance to it than to note it.

Again, during the same discussions some chairs refused to share the optimism of many others on the adequacy of precautionary balances and reserves. They drew attention, inter alia, obliquely to the concentration of lending and high risk involved. I am inferring it because it was not openly stated. Obviously the point they sought to make was that lending under the STF and to the FSU countries carries, perhaps, a higher risk than in other cases, and, as a result, one cannot be too sanguine about the present arrangements for increasing precautionary balances and reserves. This is a very important point, and I would like to have a clear assessment by the staff of whether the lending under the STF and to the FSU countries carries a higher risk than lending in other areas. If the answer is affirmative, then the conditionality package attached to these lendings needs to be re-examined, and made tighter. After all, if the Fund's credibility has not been undermined in the past 50 years, in spite of venturing into those areas where bilateral donors had hesitated, and extending support to countries in dire distress, it is because of the strict conditionalities that have been enforced. This has helped the Fund and the countries concerned.

The present arrangements for the buildup of precautionary balances and reserves, coupled with conditionalities attached to the credit support extended, have today brought us to where a review reveals that reserves are sufficient to meet 100 percent of bad debts, and over 2 percent of other outstanding loans. This position should be zealously safeguarded, and if in the staff's assessment the lending under the STF and to the FSU countries is considered to carry higher risks, then we should tighten conditions to the extent necessary. One option could be to stagger the disbursements as suggested in the Managing Director's statement. If, however, the staff believes that the lending under the STF and to the FSU countries does not carry any higher risk than in other cases, then I would like this point to be noted by all members of the Board to obviate coming back to it in further discussions on level of precautionary balances and reserves, already built up, and on target reductions for net income, contribution to the Special Contingency Account, and so on.

Incidentally, Ms. Lissakers has expressed the view that the Fund is well positioned to undertake increased risks. I quote further: "The Fund's reserves and precautionary balances are at historical levels...The strengthened arrears strategy is in position." I wish the U.S. chair had been equally forthcoming with such generous assessments when we discussed the Fund's income position, and burden sharing last week (EBM/94/52, 6/8/94). If it had, and had also taken the lead in the matter, then the compromise formula endorsed by Mr. Smee and Mr. Sirat for fixing the net income target at a lower level, say, at 3 or 4 percent, might have been approved by the Board.

One proposal in the staff paper relates to the question of increasing access limits. The STF, by definition, is a facility that is front-loaded with disbursement and weak in conditionalities. The facility itself is a transitional one, in that it acts as a bridging support pending the development by the countries concerned of a strong program that would enable them to qualify for a regular program. This being so, increasing the access limits under the STF could be counterproductive in two ways. Securing a larger flow of money on low conditionality will reduce the pressure on the countries concerned to ensure a speedier implementation of the reform process. It also increases the risk element for the Fund and consequently undermines the financial integrity of the Fund itself. This proposal, therefore, merits further examination and discussion. If however, it is considered necessary that these countries, with access to STF, be granted increased access to Fund resources, this can be done by increasing access limits under all other programs. This will benefit not only countries now eligible for the STF, but also all other borrowers as well, thus taking away the likely criticism that the borrowers from one category are the only ones benefiting. Thus, if an increase in access is considered necessary at all, this appears to be a better approach.

On the last occasion--I refer to the crisis of the late 1970s--when answers had to be found for a situation similar to the one faced today, the Fund came up with a novel package of increased access, combined with a fresh SDR allocation. After all, to the extent needy countries get more resources through increased SDR allocations, their borrowing of resources from the Fund under the programs goes down. This package has served well both the Fund and borrowers. Perhaps the time has come to consider such a package--increase in general access coupled with a fresh SDR allocation--once again.

In the discussion on SDR allocations, I made my position clear, namely, that I favor only a substantial traditional allocation. I also pointed out how difficult it would be for many countries to go to their parliaments for approval of an amendment of the Articles, aimed at securing a limited allocation only. And that if such an option were to be considered at all, two things would be needed to make the process easy: to put down as a precondition a substantial traditional allocation, so that every country sees some benefit for itself; to include this particular amendment of the Articles as part of a package of amendments that addresses such questions as equitable burden sharing. I draw attention to this because if it is thought that there should be increased access even though in the process there would be increased risk to the Fund, then the question of securing equitable burden sharing, by amending the Articles, should also be made part of the package.

We also have the Managing Director's novel idea of the cofinancing trust accounts, which opens up several interesting possibilities, including the securing of an increased flow of funds to the needy countries, which, in turn, betters the chances of success for the programs in the concerned countries. And, by doing so, it also ensures timely repayment of borrowed resources to the Fund, thereby ensuring that the Fund's credibility is not eroded. Equally important, this mechanism, coupled with a substantial traditional SDR allocation, obviates the need for undertaking the tortuous exercise of seeking an amendment of the Articles of Agreement to pave the way for a limited allocation of SDRs. I am looking forward to an early discussion on the comprehensive paper promised by the staff.

Mr. Calderón has made a very interesting statement in which, in purely mathematical terms, and taking the extreme position, he has pointed out that if the proposals in the staff paper are approved, it could totally undermine the Fund's liquidity, as well as its credibility. As far as the Fund's liquidity position is concerned, it has been pointed out that from a comfortably healthy current level of 160 percent, it could come down to about 30 percent in record time. If the Fund's liquidity is to be protected, then the Fund itself must initiate action in order to increase the quotas. Usually the trigger point is 80 percent, but considering the speed with which the liquidity could come down to 30 percent, the exercise would have to commence immediately. As far as the Fund's financial integrity and credibility is concerned, the answer lies in our time-tested traditional wisdom--that of tightening the conditionality package.

Mr. Calderón's statement, as well as the staff paper, also draw attention to the fact that if the changes proposed in the staff paper are effected, then the Fund's share of lending could go up to 20-30 percent, or even higher, against the traditional wisdom of 10 percent. In other words, instead of being a catalyst, the Fund could end up as main lender in many countries. This development should be avoided at all costs. There is no merit in emulating Mark Anthony--I refer not to our good friend, the Executive Director from France, but to his historical namesake and to his last sea battle with Octavius Caesar, when he rushed headlong, without waiting for the necessary support, and ended up losing the battle and his life! Whatever we do, we should ensure that the Fund's credibility is not undermined and that the Fund's role as a catalyst is unchanged.

There are a host of interrelated issues that need to be examined together, in depth, and it would be inappropriate to look at any one issue in isolation and attempt to take a decision. We need to consider the whole package, the sooner the better.

Ms. Lissakers commented that, with respect to the discussion of burden sharing at EBM/94/52, her chair had favored returning any surplus in the reserve to debtor countries but had been unwilling to prejudice the more comprehensive discussion that would take place in July 1994 by taking a decision at EBM/94/52 to decrease reserves. Like Mr. Geethakrishnan, she looked forward to a comprehensive solution to that problem.

Mrs. Hetrakul made the following statement:

On the access limits, I can agree with the proposal to moderately increase access limits in the upper tranche arrangements, as it goes along with the Managing Director's statement of June 3, 1994, in regard to "maintaining evenhandedness in the Fund's treatment of all its members." As for the size of such an increase, I agree with Mr. Waterman that "we attach particular importance to the Fund to maintaining its catalytic role. The Fund was never intended to fill the financing gaps of its members and we do not think we should change now." I also agree with Mr. Waterman that access should match with policy conditionality, and that policy conditionality is the most effective way for the Fund to protect its resources.

With respect to the establishment of a cofinancing trust account, I wish to reiterate our support for the scheme suggested by the Managing Director, on the condition that it will not expose the Fund to greater risk. This scheme would enhance global financial support for strong reformers, but would diffuse the risk to the Fund, as well as assist the Fund in preserving its financial integrity. Without such risk sharing, the Fund's exposure to some members may become untenable.

Mr. Evans made the following statement:

This debate is centered on the financing of economies in transition, but the proposals for increasing access under stand-by arrangements relate to all potential borrowers. The reason for the emphasis on economies in periods of adjustment is the scale of that process and the acuteness of the financing needs. The remarks that have already been made about evenhandedness sum up that point well.

This chair has always believed that increasing access to the Fund's conditional resources is the right approach. We think this is much better than, for example, a general allocation of SDRs. In a sense, this is all part of the important debate occurring in this Board, year after year, on adjustment and finance--the balance between them, the instruments, the incentives, and so on. This chair has always put great emphasis on adjustment and conditionality, with the necessary financial support. In this connection, I agree with Mr. Kiekens that the reason for these proposals is not the high liquidity of the Fund, but the needs of its membership. It seems to me perfectly consistent with the catalytic role of the Fund, and maintaining that catalytic role, for the Fund to take on a somewhat higher share of the financing for adjustment; and not only the Fund, but other multilaterals as well.

Therefore, we support the proposal for a substantially higher annual access limit, and we would be prepared to go somewhat beyond the 85 percent limit proposed for stand-by arrangements, in cases in which policies are strong and financing needs are great. By doing so, the Board would give a clear signal that the increase in access limits should be accompanied by a substantial increase in actual access; in the words of some colleagues, "the glass ceiling should also be raised." I do not see any need to change the cumulative limit at the present time, although, undoubtedly, we will need to look at that later on. I am reinforced in my views about raising the access limit by some historical comparisons: maximum access limits in relation to GDP are now clearly below the limits maintained throughout most of the 1970s and 1980s.

Let me make it clear that I want to maintain the conditionality of Fund-supported programs. The intention is not to reduce conditionality; there should be no reduction in the threshold, no watered-down programs. The size of access, in any particular case, must continue to be a function of program strength, balance of payments need, and outstanding use of Fund resources. For the same reason of conditionality, I would agree with Ms. Lissakers about the front-loading of programs. If the STF is available at the same time as a stand-by arrangement, there would need to be an appropriate path of adjustment and financing to avoid too much frontloading.

I have no doubt that we should extend the life of the STF, and I welcome the proposal to increase the amount of access. On the phasing and conditionality, I thought that Mr. Kiekens and Mr. Posthumus put it rather well. There is a risk of weakening conditionality with so many tranches, a risk that the country faced with options would choose a slow-track approach, rather than the fast track. The incentives for countries to move from an STF program to a stand-by arrangement would be stronger if there were three rather than five tranches. In the way described by the staff, slow and hesitant performers could be faced, at some stage, with the option of a stand-by arrangement or nothing, and they would be faced with this option earlier under the Kiekens proposal, than under the staff's proposal. I believe any gains in flexibility from the five tranches would be more than offset by the dangers of encouraging delay. Therefore, conditionality would best be initialled by taking the third tranche, and linking that directly to a stand-by arrangement. This approach would go some way toward meeting Mr. Waterman's concerns.

As we have made clear before, the United Kingdom would not be able to use our reserves to lend to cofinancing trust accounts, nor could we contribute nonreserve assets. More important, we are skeptical about whether there would be any real additionality from cofinancing trust accounts, and whether there would be any extra security for the Fund.

Turning to the question of risks, colleagues are right to raise this issue. Certainly, there are implications for the Fund's precautionary balances, and we ought to look soon, and without too many preconceptions, at the burden-sharing issue, again, from a fundamental point of view. But I am not convinced by the arguments focusing on the regional concentration of Fund lending. It is the Fund's role to operate within its mandate, wherever its members need it. We are not an investment fund, seeking a balanced spread of risk around the world. The overall scale of risk taken by the Fund has actually diminished over the past ten years. As Ms. Lissakers has said, the arrears cases have not been linked historically to concentration and large countries.

My authorities always support quota increases when there is evidence of need. I am sure that we will do so in the future. At the same time, I am not convinced by Mr. Posthumus' argument that these things need to be linked as of now. I think I would have to be more convinced about the need in the short term.

I agree with the Managing Director on the historic role of the Fund in all this. He talked about the Fund "going the extra mile," and suggested that its members, namely, individual countries, should also do so. Many of us have already done so, through both multilateral and bilateral commitments. Whether that response has taken the form of project finance, export credits, technical assistance, or more financial assistance, as noted by Ms. Lissakers, the response should be recognized.

Mr. Shaalan said that he was struck by the willingness of Mr. Evans to go beyond an 85 percent access limit in the presence of strong policies. Presumably, a country pursuing strong policies would also be ready for assistance under the credit tranches, unless Mr. Evans had in mind three levels of conditionality: a level of conditionality for drawings under the STF below 85 percent of quota; another level for credit tranche conditionality; and a level that would apply to drawings above 85 percent of quota under the STF. If that were the case, the access procedures would be highly complex and impractical.

Mr. Evans noted that he had referred to the possibility of going beyond 85 percent of quota for stand-by arrangements, not STF programs.

Mr. Posthumus observed that the Board discussions on the most recent quota increase had been both long and difficult, so much so that he had feared at the time that it would be the last quota increase. The position of the U.K. chair during those discussions had clearly not been as supportive of a quota increase as Mr. Evans' statement at the present discussion, in terms of both timing and size. It was true, of course, that Fund quotas were lower as a proportion of GDP than in the past, but that was precisely because the major countries had not wanted the Fund to expand at the same rate as GDP. If there had been somewhat more foresight in that respect, the Fund would have been able to be more effective in the present circumstances, because it would have had a larger amount of available resources at existing access limits. Another issue to consider was the fact that, owing to the exclusion of interrepublican trade in the quota calculations for the countries of the former Soviet Union, most of those countries had relatively low quotas. He would not necessarily use either of those points to argue in favor of higher access, but it was important to bear in mind the implications for the present discussion of previous decisions of the Fund.

Mr. Evans remarked that it was not unreasonable, in view of the sweeping and unexpected changes that had taken place in recent years, for Directors to take a somewhat different view than in the past of the issues to which Mr. Posthumus had referred. In his view, there was a case for examining the need for an increase in quotas, based on the rather clear change in members' needs since the previous increase.

Ms. Lissakers said that the Fund's current liquidity ratio would still be 70 percent if there had been no quota increase under the Ninth General Review. The broader point was that liquidity developments and the actual need for a quota increase were difficult to predict.

The Chairman commented that it was also the case that in the absence of a quota increase under the Ninth General Review the Fund would not have been in a position to take an open attitude in addressing the problems of the countries in transition. The additional protection afforded by the quota increase had been necessary at a time when the Fund had been confronted by additional risks.

Ms. Lissakers remarked that she agreed with the point made by the Chairman, which tended to argue in favor of higher access limits; the point could also be made, of course, that existing limits had not been fully used.

Mr. Al-Jasser considered that the comments of Ms. Lissakers on the liquidity position of the Fund was a testament to the prudence of the Fund even when it had a high concentration of its lending in Latin America at a most difficult time for that region. Indeed, the raison d'être of the Fund was to act wherever there was a need, and there was certainly no suggestion that the Fund should shy away from that role. However, such a role carried risks, about which the Fund should be fully aware. During the height of the debt problem, for example, the Fund had been criticized for its heavy lending concentration in Latin America, although the extent of involvement had not exceeded 35 percent of total lending in 1985, as noted by Mr. Calderón. Those criticisms, even if not made in the Board, had clearly informed the debate over a quota increase under the Ninth General Review.

When the time came to secure additional resources, Mr. Al-Jasser said, whether through a quota increase or borrowing, the Fund would need to show that it had been prudent in the use of its resources. The Board should be under no illusion that politicians or government officials would be sympathetic to increasing the Fund's resources if the Fund's involvement were to become much more extended than would be prudent. In that sense, the Fund had to act with foresight, because at a later stage others would certainly judge the Fund with the benefit of hindsight.

Mr. Kagalovsky remarked that the concern over the possible need for a quota increase was overdone. There was little evidence to suggest that the Fund's involvement in the transition economies had affected to any great degree the Fund's liquidity position or the adequacy of its precautionary balances. Indeed, the proposed increase in access limits and in the extension of the STF were very much in keeping with the expectations for the Fund at the time of the most recent quota increase.

Mr. Al-Jasser said that it was useful to recall that in the difficult discussions on the quota increase under the Ninth General Review, some members had insisted on the adoption of the Third Amendment of the Articles of Agreement as the price for agreeing on a quota increase. In doing so, they had indicated implicitly or explicitly the view that the Fund had not been prudent in its past lending. It was with that experience in mind that he had suggested that the Board discuss the risks of the current proposals upfront.

Mr. Lanciotti made the following statement:

> Let me state, at the outset, that the mandate given to us by the Interim Committee is unequivocal and leaves little room for imaginative interpretations. It explicitly encourages the Fund to consider possible increases in access to resources in order to provide adequate support to members pursuing strong programs. Therefore, the staff paper points in the right direction in elaborating on how best to meet prospective financing needs.
>
> What is left to our judgment is the amount and the time profile of the additional financing. In determining how much and when funds are to be provided, our reference system has two dimensions to be kept in mind. On the one hand, as Ms. Lissakers points out, there is the experience with transforming economies, which indicates that the transition entails a longer adjustment period and a larger financing need than originally anticipated. On the other hand, we have the constraint of the Fund's liquidity position and the level and concentration of risk.

There are also conditions to be met. These are, in particular, as the Managing Director reminds us, that the Fund's monetary character and its catalytic role be safeguarded and that even-handedness be maintained in the treatment of all members.

This said, let me consider the Managing Director's proposals. It seems reasonable to raise temporarily the annual access limit applied to stand-by and extended arrangements, from 68 percent to 85 percent of the quota. To be effective, this higher maximum should be accompanied by a clear recommendation by the Board that the proportion of the maximum actually used should, in principle, not be reduced.

This provision would be meant to remove, or at least adjust upward, the so-called glass ceiling. I do not find any convincing objection to and, indeed, any convincing position against an increase in the annual limit for stand-by arrangements.

On the contrary, I find, in some of the Director's statements, hesitations and objections concerning the STF.

I am firmly convinced that there is a need to extend and enlarge the STF, probably in the order of magnitude proposed by the Managing Director. I must admit, however, that the modalities of the proposal lend themselves to criticism, which is best expressed in Mr. Waterman's and Mr. Zoccali's statements. The sheer expansion of STF, along with its dilution in small tranches, could send the wrong signal in terms of the established conditionality, and contradict its nature as a temporary facility.

However, the problem can be easily solved: any STF financing--in one or more tranches--exceeding 50 percent of the quota should be granted only when a country has agreed to a stand-by arrangement. In this manner, the advantages of a better mixing of the maturities would be retained while the principles of conditionality would be preserved.

As far as the time profile for the new STF is concerned, my preference, whenever applicable, is for a scheme of two tranches, plus a larger one to be provided together with the first tranche of the stand-by arrangement. This scheme maximizes the incentive for the country to enter into an upper-credit tranche agreement with the Fund. But, I can understand that there might be cases in which a more adaptable approach is appropriate.

Finally, I welcome the preparation of a staff paper on cofinancing trust accounts. At this stage, however, I am not in a position to express a considered view on the newly envisaged facility.

Mr. Sirat made the following statement:

The financing of economies in transition is clearly the starting point of our discussion of today. We have an explicit mandate from the Interim Committee on this issue. But, naturally, higher access should benefit not only economies in transition, but also the whole membership, as we should certainly not use a pure geographical criterion to determine access: equity goes both ways for access as for SDRs.

The whole membership naturally includes the poorest countries benefiting from ESAF arrangements. This chair does not have a definite view on this yet, but I would not be comfortable with the idea of the Fund playing an extended role with all borrowing members, except the poorest ones. At the same time, we recognize the limitation on the existing available resources. We would certainly appreciate further studies by the staff on this issue, in particular, as regards the possibility of higher effective access within the existing limits for strong ESAF-supported programs. The gap between the theoretical maximal access of 190 percent and the effective maximal access of 140 percent is striking.

The staff paper remains relatively ambiguous on the effective meaning of an increase in the access limits. Is the point just to raise the limits, without substantially increasing the average access--as understood perhaps by Mr. Al Jasser--or is it to move both the limits and the average access?

Although we recognize that an increase in the access limits would lead to a higher dispersion of access, we would also favor a substantial increase in the average access so that the Fund remains pertinent in its actions, that is, brings about sufficient balance of payments financing. As I mentioned last April, higher access should certainly not be considered alone as the unique solution, but in conjunction with greater involvement by multilateral development banks, including the World Bank, with the maintenance of bilateral support and--this is a strong wish of this chair--with an SDR allocation. Such a general and broad-based involvement would preserve the role and status of the Fund.

How much should we increase the access limit? This is a very judgmental issue as there is a strong relationship between the assessments of balance of payment needs and the availability of external resources to finance them. Therefore, I am not convinced by the statement in the report that the existing limits have not proved, in the past, to be an explicit constraint. Such a statement hides the iterative process, which takes place in the assessment of needs and available financing. There are two elements here.

The first element is seeing the Fund take a larger share of financing. This share is currently at about 10 percent globally. We would have no objection to raising this limit, while keeping in mind both the catalytic role of the Fund and the need to continue using a case-by-case approach, depending, in particular, upon the strength of the program and the effective availability of other sources of financing.

The second element is allowing higher balance of payment needs--such as those mentioned by the staff regarding economies in transition--to be financed naturally in conjunction with strong reforms, not with weak programs. This chair is certainly not in favor of weakening the Fund's conditionality.

All things considered, we would, like Mr. Waterman, favor higher access limits rather than a higher average within the existing limits. Within this scheme, and in order to obtain an unambiguous higher average access, we would prefer a limit greater than the Managing Director's proposal of 85 percent.

What about the relationship between higher access and risk? A higher access does not necessarily mean higher risk if it occurs in conjunction with substantial and rapid repurchases, that is, if our outstanding credits do not change considerably in volume.

Projections in this field are mechanical by nature and cannot be precise. Mathematics might not be of great help here. More important is a regular review of the developments of our portfolio and liquidity. In any case, this chair, like many others, has indicated its readiness to consider an appropriate relationship between our precautionary balances and the level of our outstanding credit. We will certainly have to discuss the matter further next month, as mentioned by Mr. Geethakrishnan.

The composition of our outstanding credit would also change more rapidly if we made the access limit higher. This adjustment would not necessarily result in a greater concentration of credits, but rather a shift in our portfolio. Such a shift is not worrisome as long as the Fund keeps its usual high standard of conditionality, as it should certainly do. And I am not sure if it is extremely relevant to try to use what Mr. Calderón calls "regional concentration ratio." We did not use it in the past, as mentioned by Ms. Lissakers and others.

As regards the STF, we would be ready to support a one-year extension, but not a substantial change in its basic nature. The STF has proved instrumental in paving the way to stand-by or to

ESAF agreements: Table 4 shows that nearly all countries that have benefitted from the STF have now moved to a full-fledged Fund program.

Because it is important to keep a relative hierarchy of Fund's facilities, we would favor increasing somewhat access under the STF. As there remain only a few countries that could benefit from this facility, the volumes concerned would be relatively small, compared with our total credit outstanding.

In order to respect the hierarchy of conditionality, this increased access to STF should certainly be lower than the increase we would implement regarding stand-by and extended arrangements. The scheme should be kept relatively simple, possibly along the lines mentioned in Mr. Kiekens's statement--three tranches with a strong incentive to move quickly to a full-fledged program. This being said, I understand that the staff and management are very concerned about the possible delays and setbacks in the move to a market economy for the few countries that have clearly not been in a political situation to move forward earlier. We might have to revisit this issue later on, to see if it is possible to introduce some degree of flexibility, without, however, raising the risk of implementing weak programs with low disbursements.

The whole cofinancing trust account exercise makes sense only if it leads to additional financing, and not merely to a shift in existing financing toward a new channel. In view of existing budgetary constraints on most bilateral donors, this would require the monetary character of the instrument to be clearly and fully enforced.

To achieve this might imply further clarifications on two aspects in particular: the origin and use of resources, which should be of an explicit, clearer monetary character; and the Fund's guarantee. The terms put forward in paragraphs (g) and (h) are interesting but may not be sufficient to allow a monetary financing of the cofinancing trust accounts. This regards both liquidity, which would be easier to manage through a pooling of resources in only one global cofinancing trust account, and guarantee of repayment, which might necessitate moving further than the language used for the ESAF trust.

Ms. Lissakers said that she endorsed Mr. Sirat's desire to send an unambiguous signal about the willingness of the Fund to provide greater resources. For the sake of clarity, her chair would favor an increase in access limits under stand-by arrangement somewhat larger than the 85 percent that the staff had proposed.

Mr. Fukuyama made the following statement:

I commend the management and the staff for their intensive work on the Fund's role in financing the economies in transition, and for the useful information provided. I should like to comment briefly on each of the three issues for discussion today.

On access limits to the Fund programs under stand-by and extended arrangements, I understand that the financing requirements of countries, including transition economies, are estimated to be much larger than previously envisaged and that, therefore, the Fund is expected to play a greater role in meeting their financing needs. Under such circumstances, it would be meaningful to issue a message that the Fund intends to expand assistance to those countries that are committed to observing certain conditionalities.

Taking into account also the Fund's current favorable liquidity position, my authorities support an increase in access limits. With regard to the appropriate size of the new access limits, however, it would be more appropriate to examine further various options, including the Managing Director's proposal, than to be strict at this stage.

With regard to the STF, my authorities are, in principle, in favor of increasing the number of tranches, considering that many transition economies will face large and long-lasting financing needs exceeding the current access limit of the STF.

In this respect, I wish to make two remarks. First, increasing the number of tranches of the STF to five, as proposed by the Managing Director, may complicate it. Second, if the number of tranches increases, linking the STF in some way with approvals of stand-by arrangements will be an important issue.

My authorities' position on cofinancing trust accounts has not changed. It has been proposed to establish cofinancing trust accounts as an instrument for financing the needs of developing countries that are committed to observing conditionalities. As this facility would be administered by the Fund, the risks should, because of their nature, be assumed by the Fund. I would also emphasize that my authorities cannot lend their official foreign reserves at their own risk. I, therefore, cannot support the establishment of cofinancing trust accounts designed to shift risks to member lenders.

Mr. Schoenberg made the following statement:

In general, we can support the thrust of the recommendations put forward by the Managing Director, in his statement for this meeting, as substantiated in the accompanying staff paper.

Temporarily raising access limits would enable the Fund to continue to play a central role in supporting a large number of its members in making the transition to market economies, which appears indispensable in the current situation. In this context, evenhandedness--a principle stressed by many Directors--can be defined as the necessity for the Fund to continue responding forcefully to any arising needs; for example, the Fund's role in the Latin American debt crisis, the establishment of the structural adjustment facility (SAF) and the ESAF, and so on.

A period of three years, as proposed by the Managing Director, seems reasonable and adequate for this purpose. Such a fixed period will obviously not keep the Executive Board from closely examining developments, and taking whatever action may be needed.

Let me add, however, that a possible increase in access limits can only be considered as part of a package that would also have to include a satisfactory solution to the SDR equity issue currently under discussion.

Although we agree in principle with the Managing Director's proposal, we are open to compromise concerning the exact percentage of the new annual access limits applying to stand-by and extended arrangements. We could go somewhat higher than proposed by management, so as to match the augmentation of the STF, as proposed in the staff paper. I agree, however, with the points Mr. Waterman has made on this issue, especially the observation that in cases where higher access is granted, the reform effort must be sufficiently strong to warrant that access. The size of actual access by the transformation countries to Fund resources seems to be restricted more by insufficient institutional conditions and insufficiently strong measures to stabilize and liberalize their economies, than by nominal access limits. I agree with those Directors who consider it appropriate for the Fund to declare that it stands ready to assume a stronger role in the financing of the transition countries, but I believe that it would be problematic to assign to the Fund, a priori, a specific share in the overall external financing of those countries, as this could unnecessarily constrain the flexibility of the Fund in dealing with the very different situations in individual countries.

I also share some of Mr. Waterman's concerns regarding the STF. However, as the staff paper states, in a number of the transformation countries, the reform process has been much more protracted than anticipated, inter alia, because of the necessary magnitude of adjustment and rudimentary policy capacity. Therefore, we support an extension and enlargement of the STF, although we would, perhaps, prefer fewer additional tranches than the Managing Director has proposed. Ideally, any additional STF tranche or tranches should be linked to a stand-by arrangement. In this way, we can make sure that the appropriate conditionality is attached to Fund resources. Like Mr. Evans, I think that, in this way, the concerns of Mr. Waterman, which apparently are shared by others, can be addressed.

I want to thank Mr. Calderón for his thoughtful statement, especially the interesting calculations he presents. Perhaps the staff could comment on these figures. We cannot dismiss completely Mr. Calderón's concerns over the regional accumulation of risk--and, incidentally, the concerns of some Directors who have stressed the potentially unfavorable repayment profile arising from an increase in access limits--but a comparison with the Latin American debt crisis is not totally appropriate. Although surely nobody underestimates the severity of the debt crisis of the 1980s, the current developments in transition countries affect more people, and more countries, and fundamentally affect the basic structure of the affected member countries. In other words, and as stressed by other Directors, the challenge resulting from the transition process is unprecedented, and comparisons are, therefore, odious, as the proverb says.

The staff paper contains no additional information on the proposed cofinancing trust accounts. Therefore, we have no reason, at this stage, to add to our earlier comments on the problems involved with such a measure. I would like to point to the inherent conflict, which Ms. Lissakers accurately diagnoses, between the objective of reducing the risk to the Fund from increased lending to the transformation countries, and the ability of creditors--which in many cases are central banks--to treat claims on cofinancing trust accounts as monetary assets. One may believe that member countries, too, should go an additional half mile in shouldering risks. However, I would argue, as Mr. Evans did, that at least some member countries have already gone probably more than half a mile in providing assistance to transformation countries. Moreover, it remains arguable whether central banks should be expected to throw long-standing principles overboard.

Mr. Calderón commented that he had not devised a regional concentration indicator in his statement with a view to limiting the Fund's involvement in certain countries to a fixed share of total lending. If the Fund needed to extend a very large share of its credit portfolio to a particular region, that would be an accident of history that his chair would be willing to support. Another issue that could not be denied, however, was the risk that such a pattern of lending would involve. As noted by Professor James Tobin, the simple fact was that if a portfolio was concentrated on a particular region, the risk would be higher. It was in that context that he had asked in his statement whether the Fund's precautionary balances would need to be examined.

Mr. Sirat noted that the Fund had had a heavy concentration of its portfolio in some regions of the world for some time and, by chance, arrears had emerged in another region.

Mr. Kagalovsky said that he would appreciate some elaboration by the staff on the involvement of the Fund in different regions, particularly during the debt crisis. Another issue to bear in mind was the fact that Russia had inherited the debt of the former Soviet Union at a cost in 1992 of about $17 billion. If not for that decision, many countries of the former Soviet Union would have defaulted on their share of the debt.

Mr. Daïri made the following statement:

In the light of the comprehensive discussion that has already taken place and the issuance of a number of excellent statements, I can be fairly brief.

The paper before us--which seeks to respond to the mandate given to us by the Interim Committee--does not make a compelling case for higher access to Fund resources. Indeed, at the time of the Board's last discussion on access, and as indicated by Mr. Al-Jasser, it was clear that current limits did not pose a binding constraint on the ability of the Fund to respond quickly and on an appropriate scale in support of strong adjustment measures. The present review of our recent experience does not cause me to question the veracity of that conclusion. If anything, it demonstrates, once again, that there remains considerable scope for increasing access without raising the limits; and furthermore where there is adequate justification to exceed present limits, the Fund has the option to invoke the exceptional circumstances clause. The argument that more frequent use of this clause would, in some way, devalue or routinize its use, is not a sufficient basis for not seeking recourse to it where circumstances warrant.

However, notwithstanding the unused scope for flexibility in the present limits, as Mr. Shaalan points out, to the extent that there is a perception that actual access is being suppressed to levels below what might otherwise be permissible under the present access policy, one can see the merit of raising access if it facilitates an upward adjustment in the standard by which average access is judged. I can therefore go along with the proposal to increase the annual limit under the stand-by and extended arrangements. I also share Mr. Sirat's concern about the rationale behind excluding ESAF countries from the larger involvement of the Fund proposed in the staff paper.

The question whether the decision on access should extend automatically to the STF, however, raises a number of difficult issues and questions, most of which have been raised by other speakers. Of course, maintaining the evenhandedness in the Fund's treatment of all its members is important. But, as Mr. Calderón asks, does not a generalization of an increase in overall access to a specific, temporary and low-conditionality facility discriminate in favor of a particular group of countries? And does not such a strategy run counter to the guiding principle that it is only strong programs of high quality that should be deserving of substantial Fund support? Mr. Waterman has reminded us of how vital it is to ensure that higher access only be granted where the reform effort is sufficiently strong to warrant that access. To the extent that the Fund is being called upon to agree to an extension and enlargement of a low-conditionality facility, we are shouldering a very high--in fact inordinately high--degree of financing and risk concentration and, in the process, stand to undermine our credibility as well. Mr. Calderón's "default scenario" is an outcome that should not be dismissed out-of-hand as extreme.

If the Fund wishes to lead the effort to be responsive to the needs of its members, its monetary character and catalytic role must be safeguarded; it must elicit the fullest support of all potential bilateral and multilateral creditors in providing adequate and timely assistance; and it must proceed in plain view of the potential risks involved. These risks can be considerably attenuated if all instruments are brought to bear in fashioning a response that has strong cooperative features. I have in mind a package that has, as its centerpiece, a new general allocation of SDRs, together with an adequate revision of burden sharing, an extension of the STF for one year, and cofinancing provided by individual members using the technique of the cofinancing trust accounts. In this context, I would like to reiterate the readiness of countries in my constituency to participate on a voluntary basis, in a postallocation arrangement, and we look forward to the detailed staff paper on this issue. It is time to turn away--as the Managing Director put it recently--from "metaphysical debates about the nature of the SDR and of long-term global need" and to make a start by taking full, practical advantage of the potential of this instrument. Moreover, it would have to be understood that the membership would stand ready to increase Fund quota if the Fund's financial involvement in transition economies and other members brought its liquidity position close to the traditional threshold for action to raise its capital resources. Only with such an integrated package of financing can we, in Mr. Shaalan's words, reconfirm "this institution's commitment to the universality of its mission" in responding to the historic task before us and the needs of all our members.

Mr. Santos made the following statement:

This chair has generally advocated the need for the Fund to take a global and long-term approach to the issue of adequacy of its resources that would enable it to respond in a timely and appropriate manner to the demands of its membership. It is in this regard that we have supported the establishment of the STF as an appropriate instrument in support of the initial stage of reform in the transition countries. However, we have some doubts regarding the proposal being presented today to meet the special needs of the transition countries in their difficult task of integrating into the world economy. While we note that this proposal responds to the call made by the Interim Committee that the Fund play a central role in this process of historical proportions, we note also that the Interim Committee communiqué stressed that the monetary character and the catalytic role of the Fund must be safeguarded and that it called on potential bilateral and multilateral creditors and donors to provide adequate and timely assistance in conjunction with the Fund. On this latter issue, the staff report makes it clear that the recent experience has not been encouraging. We wonder whether the staff has, at this stage, new indications that commitments made at the time of the establishment of the STF will now be forthcoming.

The proposals under discussion today raise a number of key issues and concerns. Most of these have been well elaborated in the statements by so many of our colleagues. I do not see any need for further elaboration. I can endorse the general thrust of their comments. First, although we are prepared to review the operational issues relating to the STF in a manner that will maintain the momentum of reform and facilitate the rapid move of the transition economies to upper credit tranche arrangements with the Fund, we cannot ignore the reservations expressed already with regard to the proposal to extend and augment the STF.

Increasing access limits to Fund's lower conditionality resources will undoubtedly heighten the concerns over the riskiness of the Fund's portfolio and the adequacy of its precautionary balances. Difficult issues such as the nature and modalities of additional safeguards needed to protect the Fund resources and the mechanisms for sharing the burden entailed by these additional risks would need to be addressed. Previous speakers have reminded us again today that there is no good substitute for conditionality when it comes to protecting the Fund's resources. Moreover, the continued access to resources with lower conditionality for one particular region beyond the initial critical period could raise the issue of evenhandedness in the Fund's dealings with the membership and affect the image and credibility of the institution.

Second, there is enough room for increased access within the current annual limits under stand-by and extended arrangements. But if, in the judgment of the Board, increased annual access limits represent a pragmatic course of action that could enhance the Fund's catalytic role, we are prepared to support the proposal for a temporary increase in the annual limits applying to stand-by and extended arrangements from 68 percent to 85 percent of quota.

Third, although the staff paper focuses on the question of access to Fund resources, like Mr. Shaalan and others, it is my expectation that these proposals are part of an integrated package in which a general new allocation of SDRs will play a crucial role.

Mr. Mwananshiku made the following statement:

During our discussion last April on external financing requirements of transition economies and possible sources of financing, this chair supported the Managing Director's proposal that the Fund should continue to play an active role in supporting the reform efforts of countries making the transition to a market economy. In so doing, we recognized the serious difficulties facing those countries, and the large amount of financing they need in order to carry out a successful transition.

In the paper now before us, the staff has set out detailed proposals of how the Fund intends to fulfill its financing role. Specifically, three related proposals are made, as follows:

It is proposed to make a temporary increase in the annual access limits applying to stand-by and extended arrangements, raising them from the current 68 percent of quota to 85 percent; it is proposed to extend the STF and increase its access limits from the current 50 percent of quota to 85 percent; it is proposed to create a system of cofinancing trust accounts to supplement the financing efforts of the Fund.

I support the first proposal as it is consistent with our past positions on this question. When we discussed the present limits, this chair argued strongly against reducing the level of access, not only because of the prospective large financing requirement of the economies in transition but also because such limits were expected to be unduly restrictive, with a considerable proportion of the membership suffering a reduction in absolute potential access, as has now become clear. However, an increase in access, if approved, should apply to all members implementing strong programs in line with the policy of equal treatment. And, even with an increase in access limits, the problem of low reserves facing the economies in transition and many other economies will remain and continue to hamper their adjustment efforts. For this reason, an increase in access limits should be part of a package containing a general allocation of SDRs to all Fund members. In this way, the Fund's role would be enhanced, and at the same time, the principle of equal treatment would be observed.

With regard to the second proposal, we support an extension of the structural transformation facility. However, we see problems with regard to the proposal to increase access limits. We supported the creation of an STF with soft conditions only as a transitional facility intended to lead quickly to the regular facilities of the Fund. Consequently, increasing its access limits at this stage, without at the same time strengthening its conditionality, would represent a departure from the principles on which it was established. It would also challenge the fundamental policy on which Fund financing is based. I am not even sure that it would be of much help to the countries concerned. Moreover, the proposal raises questions relating to the concentration of risks, with implications on the level of precautionary balances and the rate of charge. The financial health of the Fund could also be put in jeopardy.

On cofinancing trust accounts, we look forward to a detailed staff paper.

Finally, we believe the access limits under the ESAF should be reviewed.

Ms. Langdon made the following statement:

We welcome today's discussion on access to Fund resources and the Fund's role in financing the economies in transition. As this chair has stated before, the main contribution that the Fund can make to those countries in difficult circumstances--that is, countries in transition to market economies--is to provide policy advice, and to link the Fund's own financing to policy conditions.

It is because of our confidence in the Fund, and the benefits of conditionality, that we think the Fund should play a pivotal role in providing financial support to these countries, and in encouraging strong adjustment, which is key to securing sustainable economic transformation. Two lessons have been revealed, thus far, from our experience with economic stabilization and reform of economies in transition: first, the cost of economic adjustment is higher than we anticipated; but, second, the more front-loaded the adjustment is to lower inflation and to remove the most salient distortions, the earlier the benefits of reform are reaped in terms of raising living standards.

Increased access under Fund-supported adjustment programs is consistent with, and will help the staff to promote, strong economic programs. I wholeheartedly agree with Mr. Evans's remarks that we want to maintain the level of conditionality of Fund programs, but, at the same time, we want the Fund to increase the value of the resources attached to conditionality.

We are supportive of the general thrust of the staff's proposals. However, my authorities have some adjustments--many of which will sound familiar at this stage of our discussion--that they believe would improve upon them. Like Mr. Sirat and others, we believe that having relatively higher access on upper credit tranche arrangements than on STF resources enhances the incentive to accelerate the reform process. On the STF, my authorities support an extension and enlargement of the facility along the lines described by Ms. Lissakers.

With regard to access to stand-by and extended arrangement resources, my authorities believe that the suggestion for increasing the annual access limit to 85 percent is in the right direction; however, they see a case for increasing annual access under stand-by arrangements somewhat further, while retaining the cumulative limit. This would convey a powerful signal of the Fund's ability to support strong programs and would increase the incentive for countries to undertake strong adjustment programs. It would also give the Fund more scope for supporting faster adjustment.

In respect of the STF, we support an extension and an enlargement of the facility of the magnitude suggested. However, my authorities have considerable difficulties with the proposed modifications of the phasing of the facility. The five-tranche approach risks conveying a disincentive to move ahead to a stand-by arrangement, and detracts from the STF's paving the way characteristic. Reducing the number of tranches and forging a stronger link between access to an STF and a stand-by arrangement is an alternative they strongly prefer. This would serve to reinforce the incentive for stronger adjustment by creating greater scope for financing front-loaded adjustment.

To conclude on the access issues, we are comfortable with a temporary increase in annual access limits, as the Board will have the opportunity to review this change in the light of program experience and the Fund's liquidity position.

We share the skepticism expressed by others that cofinancing trust accounts would provide additional resources. For my country, contributions to cofinancing trust accounts would not be counted as official reserves. Thus, financing through cofinancing trust accounts would have budgetary implications. Suggestions (g) and (h) in the staff paper may increase the attractiveness of cofinancing trust accounts, but this may simply lead to cofinancing trust accounts cannibalizing other forms of worthy assistance.

Mr. Kaeser made the following statement:

As the Managing Director and some of my colleagues set the stage for today's discussion in producing valuable statements, I can be brief. Everyone will be able to recognize the line of argument that this chair is willing to follow.

To summarize our position, we favor a solution that is impossible to put into practice in real life, as we are ready to make the second step, but not the first. To be more explicit, we are in favor of considering an increase of the access limits under the STF from 50 percent to 85 percent of quota. This can be justified by the fact that the problems and the financing needs of the countries in transition are much larger than foreseen one year ago, and by Mr. Posthumus's remark regarding the relatively low size of most FSU quotas. We can also agree with the extension of the deadline for expiration of the STF to the end of 1995, because the time needed to implement economic reforms was underestimated.

As regards the disbursement of the STF, I do not favor the perfusion approach envisaged by the staff. I prefer Ms. Lissakers's solution of adding a third tranche that would be available when an upper credit tranche arrangement is approved by the Executive Board. Mr. Kiekens and others favor a similar solution. As Ms. Lissakers writes, "the linkage of additional STF financing to regular Fund progress would provide a useful incentive for the borrower to implement stronger policies." When the reform process is under way, and the country in transition qualifies for an upper tranche arrangement, other sources of financing will become more readily available.

However, we are not yet fully convinced that we should enlarge the access to Fund resources for the upper tranches agreements. The average access is currently low, but the room for maneuver is large. The staff states that the current limits are not expected to impose constraints on the ability of the Fund to assist most member countries. If needed, we can have recourse to the exceptional circumstances clause. Enlarging the access only to raise the moral comfort of potential borrowers is not appealing to me. The case for enlarging the access to the Fund resources can only be made if our institution is urged to cover such a large share of the financial needs of the countries in transition--and perhaps others--that we should be concerned about the preservation of its financial integrity and monetary character.

In any case, we favor the reaffirmation of the preferred creditor status of the Fund. Member countries should respect this status, not only in their relations with the Fund but also in their financial arrangements among themselves.

Concerning the cofinancing trust accounts, after listening to the comments made by different chairs, I doubt that it will prove possible to mobilize much additional financing through this instrument. But we should continue our discussion on this issue, because the possibility to cofinance a Fund program--perhaps with untied resources--deserves careful consideration.

Like Mr. Geethakrishnan, I believe that we are heading toward a package deal, and we will be ready to help wrap a well-balanced one.

Mr. Zhang made the following statement:

As I share the concerns and views of the previous speakers, I would like to make just a few remarks. When discussing access limits, we should bear in mind three related aspects: the principle of uniform treatment for membership; the financial integrity of the Fund; and the Fund's catalytic role in providing financial assistance to its members.

With regard to the STF, it is fair to say that this facility has helped borrowing countries deal with their balance of payments difficulties. However, in considering an extension and enlargement of the STF, we have to remind ourselves of its temporary character, and its less rigorous conditionality.

Increases in access limits under the STF may increase the flow of Fund resources to a group of countries. In that case, this chair would be worried about the risk of concentration, in particular, as such risk can only be reduced if a strong conditionality is in place. This is, however, not always the case under the STF. Furthermore, the Fund's credibility would be tarnished. Prospective foreign investors generally regard Fund involvement as an indication of confidence in a borrowing country's economic policy. If an increased infusion of Fund resources is not accompanied by strong policy commitments, foreign investors will be skeptical of the signals given by the

Fund's further involvement and will be reluctant to increase their investments, which are ultimately the most-needed financial resource for economies in transition.

This being said, we share Mr. Waterman's view in that, provided strong adjustment programs and reform policies are in place, we can support a temporary increase in the annual access limits for stand-by and extended arrangements.

In view of all this, we should be cautious. If the Fund's sound financial position is affected, the risks will be widely shared by the whole membership. In this process, I reiterate our support of a general allocation of SDRs. This will not only meet the reserve needs of members at large, but also will help economies in transition strengthen their reserve positions.

With respect to the proposal on cofinancing trust accounts, a detailed paper is necessary and welcome. Like some Directors, we believe that a new general SDR allocation could facilitate the preparation process for the creation of this account.

I share Mr. Calderón's concerns that the Fund's liquidity ratio will drop sharply; therefore, we believe that a general quota increase should be considered.

The Director of the Policy Development and Review Department said that although the alternative calculations of the Fund's liquidity position provided by Mr. Calderón were in line with those of the staff, they should be regarded as illustrative calculations, rather than estimates, based on an extreme assumption that the countries under consideration would fully draw down access to Fund resources under one of the scenarios cited in his statement. There was also an underlying debate in the Board about the implications of any increase in access limits for other members of the Fund, which were not accounted for in the calculations presented by Mr. Calderón. In one sense, therefore, the calculations probably overstated the effects of the staff's proposal on the liquidity ratio; to the extent that the sense of the Board was that higher access limits should result over time in an increase in average access by all members, the calculations probably understated the effects on the liquidity ratio.

With respect to the regional concentration of Fund lending, the Director continued, the most recent staff paper on the Fund's liquidity position and financing needs (EBS/94/66, 3/28/94) indicated that the share of outstanding credit extended to the countries covered by the Western Hemisphere Department had been 61 percent in 1990 and had been estimated in that exercise to reach 29 percent in 1995. For the countries covered by the two European Departments, the comparable figures were 4 percent and 36 percent, respectively. The exercise reflected in EBS/94/66 predated the current exercise, which was aimed at examining the Fund's liquidity position in the context of enlarged access for the transition economies, or for the

Fund membership as a whole. He would agree with those Directors who insisted that, to the extent that it reflected an appropriate response of the Fund to problems that had arisen among its membership, increased access was entirely correct; indeed, the proposed response was very much akin to the approach taken in the context of the debt situation of Latin American countries. To the extent that countries and regions were subject to similar adverse economic circumstances, however, there was something to the argument of a concentration of risk. Nevertheless, the discussion of the appropriateness of the proposed approach might be better couched in terms of whether the Fund was responding to the needs of its members in a particular context.

The Board had clearly not been convinced by the staff's proposals for small, multiple tranches under the STF, the Director observed. It was equally clear, however, that the aim of all speakers in that context was the same: to help the transforming economies move as rapidly as possible to a situation where they could be supported under the Fund's regular arrangements. There was also a desire to see a mix of resources before those countries availed themselves of the extended Fund facility, which had on average a somewhat longer maturity than the resources that could be provided under a stand-by arrangement. Those concerns had led to a desire to establish a link to STF resources even after a country had qualified for a stand-by arrangement.

At its heart, however, the issue was how the process could be accelerated, the Director considered. The staff's proposal was an attempt to create at least a fall-back mechanism by which the Fund could continuously and regularly engage in an intensive dialogue through negotiations with the transition countries so as to maintain the momentum for reform. It was from that perspective that the staff had suggested the usefulness of small, regular tranches within the STF. In proposing that approach, there was no suggestion that there should be two different modes of STF operations ex ante, or that the staff would want to create a situation in which the Fund could support weak programs. Thus, the staff's proposal was for a fall-back position in situations in which the program turned out to be more difficult to implement than had been envisaged at the outset.

With respect to the broader issue of conditionality, the relationship between higher access and tighter conditionality was not as straightforward as suggested by some speakers, the Director commented. In general, and especially in the context of the transition economies, there were no levers that could be turned to increase conditionality pari passu with increased Fund resources, which helped to explain the particular formulation of the staff's proposal. Thus, for example, the staff did not present medium-term scenarios in support of some requests for STF resources because it simply did not believe that it knew enough about the likely response of the economy to certain measures; in the transition economies, there was no history in terms of elasticities and other important concepts central to the formulation of quantitative medium-term scenarios. Moreover, the institutional setting, while very weak in many other countries as well, was rather exceptional in the transition economies. That being said, he was impressed by the fact that even Directors representing some of the transition countries had not supported the staff's proposal. Nevertheless, the Fund would continue to face situations in which programs proved not to be implementable, not perhaps for lack of will, and the only available option would be to move to an upper credit tranche arrangement.

In response to the question raised by Mr. Sirat on raising access under the ESAF, he would note only that average access under the ESAF was very much tailored to the availability of ESAF resources, which, unlike the Fund's general resources, were essentially fixed, the Director of the Policy Development and Review Department remarked. The Fund did not, therefore, have the flexibility to modify ESAF access limits; however, existing access limits, which effectively ranged from zero to 255 percent of quota, were applied flexibly to deal with the diverse circumstances of ESAF-eligible countries.

Mr. Sirat agreed that it was necessary to take into account the availability of ESAF resources in determining access to that facility. However, there did not appear to be a striking reason why the Fund should provide for the possibility of maximum access under its general resources while not at the same time providing for maximum access under ESAF arrangements. Indeed, effective access under the ESAF had been 140 percent, far from the theoretical limit. More generally, a decision to agree to heavier Fund involvement in all members except the poorest would be problematic in terms of the message conveyed by the institution. It did not necessarily follow that access limits under the ESAF should be increased commensurately, but the issue would have to be tackled squarely. Further calculations by the staff would be useful; for example, increasing average ESAF access within existing limits would probably result in only a modest shortening of the period in which ESAF resources were expected to be exhausted. Finally, as his authorities had demonstrated in their willingness to contribute to ESAF arrangements, the availability of resources should not necessarily bear only on debtor countries; it was also the responsibility of creditor countries.

The Director of the Policy Development and Review Department remarked that from the outset the operation of the ESAF had involved certain uncertainties. Under the original ESAF, for example, the staff had no reason to assume that the facility would be extended and enlarged, and it had managed access policy within the framework of available resources. The staff had tried to avoid the risk that, without creating a sense of entitlement, countries able to benefit sooner from the ESAF did not squeeze out other ESAF-eligible countries later on. If the ESAF had been established as a more permanent facility, the rules and regulations governing the operation of the facility would probably have been re-examined.

The Chairman made the following concluding remarks:

This has been a very important and constructive discussion. Many of you have emphasized the mandate--the "unequivocal" mandate, in the words of one speaker--we have received from the Interim Committee. Of course, there are different views and different perspectives, but I welcome the clear institutional sense that has permeated the discussion today, both in terms of the mission of the Fund and in terms of our responsibility to safeguard this institution. All Directors agreed that not all elements of the package we are preparing were on the table today. Yet, many referred to the related SDR issues and to cofinancing trust accounts, and I am indeed grateful for the constructive references that were made to the latter instrument. We will discuss this issue separately, and soon, on the basis of a further paper.

With respect to the more precise issues that were to be discussed today, I would first like to welcome the very broad-based support for a temporary increase in the annual access limit applying to stand-by and extended arrangements. Here, I would like to say in passing that I share Mr. Sirat's concern and uneasiness in not recommending changes with respect to the ESAF at a time when we are raising the access limits for other instruments; of course, as we heard from the staff, here we have an extra constraint, but I promise to come back to this issue on the occasion of a future meeting. While most Directors felt that the proposed increase in access under stand-by and extended arrangements provides sufficient scope for the Fund to be responsive in appropriate circumstances, other Directors thought that a somewhat larger increase in the annual access limit was needed--and I had the impression that the figure of 100 percent was in the minds of some of them. We must see how we can accommodate these views, particularly as a few Directors did not think that there is a strong case to increase the access limit at this time. Nevertheless, I observe that those who hold this latter view are willing to go along with a moderate increase in the annual access limit as part of a broader package.

Several Directors made the observation that the Fund's catalytic role makes it possible for us to provide relatively more financing in individual cases, where warranted by strong policies and large balance of payments need, however, it remains generally agreed that the Fund's catalytic role would not be consistent with the Fund substituting for other potential sources of financing.

Views on the proposals for the STF were diverse. Directors generally favored an extension of the facility for another year to provide assistance for potentially eligible countries that have not yet been able to make use of the facility. Most Directors favored adding an additional tranche to be disbursed only in the context of upper credit tranche arrangements; they expressed concern that higher access on the basis of conditionality that does not meet upper credit tranche standards would increase the risk to the Fund and could weaken the incentive to move to an upper credit tranche arrangement. Some Directors did not favor enlarging STF access. The suggestions to introduce multiple tranches in some cases found little support. Nevertheless, I think this meeting has provided a good opportunity for the staff to clarify its intention in this respect, and to explain why it might be useful to maintain temporarily a kind of fall-back approach, in order to provide an opportunity, at a later stage, for slower reformers to jump on the carriage of the fast-track STF. The staff will reflect further on these issues, in view of your suggestions, to see how they can be reconciled.

I want to stress that there is no intention to weaken conditionality or incentives. Programs supported by the STF would continue to be framed, in all cases, with the aim of moving as quickly as possible to an upper credit tranche arrangement, preferably by the time of the second purchase, but certainly within the first year of an STF-supported program. As we have discussed before, experience has shown that transition economies, as others, are best served by strong programs, and it is not the intention to back away from this approach. But experience has also shown that some of these countries face greater difficulty and uncertainty than others. There will be setbacks and, although it may be a second-best approach, we should have a way of dealing constructively with these countries.

It is clear that we need further clarification and debate on the other elements of the package. I would propose that we meet on June 23 to consider again the SDR issue. In the light of this discussion, I would then submit to you an overall package, which we could discuss on June 29 with a view to reaching soon a final agreement.

3. UKRAINE - RELEASE OF INFORMATION

The Executive Board approves the proposal to make available to participants in an aid donors' meeting, to be held in Paris on July 13, 1994, a staff paper updating economic developments in Ukraine (SM/94/146, 6/10/94).

Adopted June 17, 1994

4. 1994 REGULAR ELECTION OF EXECUTIVE DIRECTORS - AD HOC COMMITTEE - COMPOSITION

The Chairman proposed that an ad hoc committee be established to draw up rules for the 1994 Regular Election of Executive Directors.

Without discussion, the Executive Board took the following decision:

An ad hoc committee on Rules for the 1994 Regular Election of Executive Directors is hereby established to propose rules for the conduct of the forthcoming regular election of Executive Directors and to examine and submit recommendations to the Executive Board on any related matters. The composition of the Committee shall beas follows: Mr. Marino, Chairman; Mr. Bergo, Mr. Geethakrishnan, Mr. Mwananshiku, Mr. Santos, Mr. Schoenberg, Mr. Shaalan, Mr. Zhang, and Mr. Zoccali.

Adopted June 17, 1994

APPROVAL: February 27, 1996

LEO VAN HOUTVEN
Secretary

Table Annexed to Statement by Mr. Calderón

Table 1

	Baseline	Maximum Access	Increased Access
Liquidity Ratio	80 percent	50 percent	30 percent
Regional concentration ratio 1/	46 percent	57 percent	63 percent
Catalytic ratio	10 percent	16 percent	20 percent 2/

1/ Fund's credit to Europe would be, by the end of 1996, $19 billion in the baseline case, $29 billion in the maximum access scenario, and $38 billion in the increased access case. We assume that, for the other regions of the world, Fund exposure remains constant in nominal terms.

2/ This ratio would exceed 50 percent for some countries.