INTERNATIONAL MONETARY FUND

Secretary's Journal of Executive Board
Informal Session 96/7

10:00 a.m., September 25, 1996

Contents

Executive Board Attendance

M. Camdessus, Chairman
S. Fischer, First Deputy Managing Director
P.R. Narvekar, Deputy Managing Director

Executive Directors	Alternate Executive Directors
A.A. Al-Tuwaijri	S.M. Al-Turki
	A. Fayolle
L.E. Berrizbeitia	V.J. Fernández
	C.X. O'Loghlin
	D.Z. Guti
B. Esdar	W.-D. Donecker
H. Evans	J. Shields
E.R. Grilli	N. Coumbis
	L.M. Cheong
D. Kaeser	
A. Kafka	
W. Kiekens	J. Prader
	J.-C. Obame, Temporary
K. Lissakers	B.S. Newman
H. Mesaki	H. Ono
	S. Rouai, Temporary
	A.G. Zoccali
	Y.Y. Mohammed
M.R. Sivaraman	H.B. Disanayaka
	B. Andersen
	A.V. Mozhin
	V.Y. Verjbitski, Temporary
E.L. Waterman	J.-H. Kang
J. de Beaufort Wijnholds	Y.G. Yakusha
	Han M.

L. Van Houtven, Secretary and Counsellor
R.H. Munzberg, Associate Secretary
G.N. Walton, Assistant

Also Present

African Department: C. Brachet, Deputy Director. Central Asia Department: K. Saito, Director. External Relations Department: S.J. Anjaria, Director; P.J. Bradley, M.E. Hansen. Legal Department: F.P. Gianviti, General Counsel; W.E. Holder, Deputy General Counsel; H. Elizalde, H.V. Morais. Policy Development and Review Department: J.T. Boorman, Director; J. Ferrán, Deputy Director; T. Leddy, Deputy Director; N.L. Happe, K.J. Langdon, R.H. Nord. Research Department: M. Mussa, Economic Counsellor and Director; M. S. Khan, Deputy Director; F. Caramazza, G. Hacche. Secretary's Department: W.S. Tseng, Deputy Secretary; A. Mountford. Statistics Department: J.B. McLenaghan, Director. Treasurer's Department: D. Williams, Treasurer; D. Gupta, Deputy Treasurer; G. Wittich, Deputy Treasurer; J.C. Corr, E. Decarli, L.U. Ecevit, O. Roncesvalles. Western Hemisphere Department: C.M. Loser, Director. Office of the Managing Director: S. Sugisaki, Special Advisor; J.A. Quick, Personal Assistant; J.A.P. Clément. Advisors to Executive Directors: M. Askari, P. Cailleteau, R.F. Cippa, S.S. Farid, T.K. Gaspard, A. Guennewich, He J., G.M. Iradian, J. John, R. Kannan, W.C. Keller, J. Leiva, M.F. Melhem, H. Mori, M. Petrie, M. Sobel. Assistants to Executive Directors: W.F. Abdelati, J.G. Borpujari, M.A. Brooke, M.A. Cilento, A.L. Coronel, J.A. Costa, D.A.A. Daco, C.K. Duenwald, D.S. Hakura, R.J. Heinbuecher, O. Himani, Huang X., G.A. Kyriacou, J.P. Leijdekker, H. Ogushi, D. Saha, Song J., V. Trivedi, L.B.J. van Geest, M.Yiu, Zubir bin Abdullah.

1. NEW ARRANGEMENTS TO BORROW—STATUS OF NEGOTIATIONS

The Executive Directors met, in informal session, to discuss the current status of negotiations on the New Arrangements to Borrow.

The Chairman said that the purpose of the meeting was for the staff to outline the progress that had been achieved on the New Arrangements to Borrow (NAB). Progress had been made by the G-10 countries, and other countries with financial capacity to support the Fund, in developing an instrument that would contain the legal and operational details of the NAB. The potential participants had continued their discussions, and most features of the NAB had been agreed. However, a number of institutional issues remained to be resolved. In particular, agreement had yet to be reached on setting up a secretariat, and the frequency and terms of reference of meetings of participants. In addition, the list of participants and the amount of their respective credit arrangements had not been finalized. It was unlikely that those pending issues would be resolved before the 1996 Annual Meetings.

It was important to highlight that the General Arrangements to Borrow (GAB) would continue in effect, under which an amount of SDR 17 billion, plus SDR 1.5 billion under an associated arrangement with Saudi Arabia, could be made available to the Fund, the Chairman stated. However, the NAB would be the facility of first and principal recourse in the event that a need arose to provide supplementary resources to the Fund. The total amount that would be available under the NAB would be SDR 34 billion. The combined amount of drawings and commitments under the NAB and the GAB would at no time exceed SDR 34 billion. Although the NAB would be the facility of first and principal recourse, in the event of a request for a drawing on the Fund by a participating member, or a member whose institution was a participant in both the GAB and the NAB, a proposal for calls could be made under either of the arrangements; in the event that a proposal for calls under the NAB was not accepted, a proposal for calls could be made under the GAB. The provisions governing the NAB would to a large extent follow the provisions of the GAB.

As with the GAB, the NAB would take the form of a decision of the Fund, the Chairman continued. It would enter into force when it had been adhered to by members or institutions with credit arrangements amounting to no less than SDR 28.9 billion (85 percent of the total) including amounts from participants with the five largest credit arrangements. The decision would remain in effect for five years, and could be renewed for such period or periods and with such modifications as the Fund may decide, except in respect of those provisions requiring unanimity.

The General Counsel stated that the NAB could be activated for the benefit of a member that was a participant or whose institution was a participant, and also for the benefit of a nonparticipant, under circumstances similar to those in which the GAB could be activated, except that the activation for nonparticipants was no longer subject to the stricter test of the Fund's liquidity position.

With regard to voting majorities, a favorable decision on a proposal by the Managing Director to activate the new arrangements would require an 85 percent majority of total credit arrangements of participants eligible to vote, and that majority was different from the majorities and procedures under the GAB, the General Counsel said. Neither the prospective drawer, if it were a participant, nor its participating institution, nor participants that had opted

out would be eligible to vote on the proposal. A proposal would be effective once it had been accepted by the participants, and approved by the Executive Board.

Admission of new participants at the time of renewal of the arrangements would require a decision of the Fund and the concurrence of participants representing 80 percent of total credit arrangements under the renewed arrangements, the General Counsel added. An increase in the interest rate provided under the arrangements would require agreement between the Fund and participants representing 80 percent of total credit arrangements. The same majority would be required to apply a change in the method of calculating the combined market interest rate to indebtedness under the arrangements.

Amendments to the arrangements during the period of effectiveness, or any subsequent renewal, including increases in the total amount of credit arrangements owing to admission of new participants, or changes in the amounts of participants' credit arrangements, would require both the agreement of the Fund and of participants representing 85 percent of total credit arrangements, the General Counsel continued. In the latter case, however, each participant whose credit arrangement changed would also need to concur to the change. Moreover, certain provisions of the arrangements could only be amended by the Fund with a consent of all participants, for instance, changes in the amount of participants' credit arrangements, withdrawal by a participant that voted against an amendment if the participant was of the view that it materially affected its interest, and withdrawal of adherence to the decision at the time of renewal.

The participant's individual credit arrangements and the loans made to the Fund under them would be denominated in SDRs, like the GAB, and would be made in the currency of the participant, or in the currency or currencies of other members of the Fund as agreed among the participants of the Fund, the General Counsel stated. As required by Article VII, if the loan was in a currency other than the participant's, the concurrence of the member whose currency was to be used in the loan would be needed. The provisions on exchange rates for transactions would be the same as for the GAB and for all other Fund transactions.

The provisions on repayment were generally the same as under the GAB, the General Counsel remarked. To give the quality of reserve assets to claims of participants on the Fund, a participant would be able to request early repayment of all or part of the Fund's indebtedness if it gave notice to the Fund representing that there was a balance of payments need for such repayment. The Fund would give such a representation the overwhelming benefit of any doubt. Repayments by the Fund to each participant would be, whenever feasible, in the currency or currencies that had been borrowed by the Fund for the participant, or in the currency of the participant, or in SDRs, or, in consultation with the participants, in other currencies that were actually convertible.

As in the case of the GAB, a participant would be able to transfer all or part of its claim to repayment with the prior consent of the Fund and on such terms and conditions as the Fund may approve, the General Counsel said.

A participant could withdraw its adherence to the NAB decision at the time of renewal, the General Counsel concluded. A participant could also withdraw within 90 days from the date of adoption of an amendment if, in its view, the amendment materially affected the participant's interest and the participant had voted against it. Otherwise, the participant could only withdraw with the agreement of the Fund and all participants.

The Treasurer said that there were a considerable number of operational features of the NAB that were different from the GAB. The total amount of the credit arrangements would be for SDR 34 billion, and that total would remain in effect until changed either by the adherence of new participants, or as a result of a decision to increase the amount of an individual credit arrangement. For example, the instrument would provide for changes in each participant's credit arrangements in the event that new participants were admitted, or because of changes in the size of individual arrangements in the light of developing circumstances. One of the criteria that would be taken into account would be the results of changes in Fund quotas. But there could be other criteria, for example, the number of new participants could change.

The combined use of drawings and commitments of the NAB and GAB could not exceed SDR 34 billion, the Treasurer said. The available commitment of a participant under the NAB would be reduced by any outstanding drawings on, and commitments of, the participant under the GAB, or under the associated borrowing arrangement with the GAB. Moreover, the available commitment of a participant in the GAB, or associated arrangement, would be reduced as a result of drawings or commitments under the NAB by the extent to which its credit arrangement under the GAB exceeded its available commitment under the NAB.

The proposals for calls under the NAB would in principle be proportional to each participant's credit arrangements in the NAB, the Treasurer sated. The Managing Director could, however, make proposals for nonproportional calls, but only in specific circumstances. For example, the Managing Director could propose nonproportional calls if the outstanding commitment of at least one participant was insufficient for the proposed exchange transaction for it to meet the Fund's need for a specific currency. Moreover, if at least one participant's available commitment under the NAB was not sufficient to meet fully proportional calls, the Managing Director could ask every participant that had sufficiently available commitments to meet fully such a proportional call up to the extent of its available commitment. Every participant that would undertake to provide proportionately more resources than at least one other participant would be required to concur before a proposal for nonproportional calls by the Managing Director could be accepted. Unless otherwise provided in a proposal for future calls that had been approved, each call would be made in proportion to the amounts in the proposal.

A member could opt out of a proposal for calls under the decision if it determined that it was unable to meet calls, the Treasurer continued. A member's inability to meet calls would normally be reflected in the member's exclusion from the Fund's call to the operational budget for transfers of its currency. The member should notify the Fund and the other participants if it intended to opt out of a proposal for calls. Moreover, participants would be expected to exercise restraint and take into account the views of the Fund and other participants in that respect. There was no provision for partial opting out. Either the participant opted out of all calls under a proposal and did not vote on the proposal, as the General Counsel had mentioned, or the participant did not opt out and voted, and would be bound by the specified majority of the decision.

The basic provision on the interest rate paid to the Fund's creditors would be, in principle, the same as under the GAB, the Treasurer added. The Fund would pay interest on its indebtedness under the arrangements at the rate equal to the combined market rate which was computed for determining the SDR interest rate. However, the draft instrument also

provided that a higher interest rate could be agreed between the Fund and the participants representing 80 percent of total NAB credit arrangements. That higher interest rate could come into effect, for example, if the Fund decided to levy a surcharge on holdings of members' currencies exceeding a certain percentage of quota, and those holdings had been financed by borrowings under the NAB.

New participants could adhere to the GAB at any time provided that the Fund agreed and no other participant objected, and provided that the amount in the GAB for it would not be less than the amount of the credit arrangement of the participant with the smallest credit arrangement, the Treasurer said. However, under the NAB, it was expected that new participants would normally be accepted at the time of each five-year renewal of the NAB if the Fund and participants representing 80 percent of the total credit arrangements under the renewed decision agreed to the request of the prospective participants. New participants could, however, be accepted at other times by an amendment of the arrangement adopted by decision of the Fund, and with the concurrence of participants representing 85 percent of total credit arrangements.

2. DRAFT INTERIM COMMITTEE DECLARATION

The Executive Directors met, in informal session, to discuss a draft Interim Committee Declaration (EBD/96/125, 9/24/96).

The Chairman said that, following the recent luncheon discussions, he was under the impression that Directors wished to revise the Madrid Declaration to take account of the new dimensions that had emerged during the discussion of the world economic outlook. A revised draft had been prepared for the consideration of Executive Directors.

Mr. Waterman considered that the draft declaration was more comprehensive than the Board had agreed. It had therefore become somewhat of a mixture of a declaration and a communiqué. While the Madrid Declaration was not perfect, it was much tighter and more sharply focused than the revised declaration. It would be preferable to make more use of broad economic statements, and to avoid reference to particular countries. In addition, statements on purely political objectives, such as "renovating the state" should be avoided. Finally, the material on HIPC, ESAF, SDRs, and quotas represented more of a commentary on detailed policy issues than general policy positions.

Mr. Evans said that the draft declaration was too broad in its coverage, for example, of health care issues. The document should focus rather on areas for which the Fund had a clear line of responsibility.

The Chairman considered that the Fund should be more explicit with respect to the prioritization of budgetary expenditures such as education, health care, and infrastructure. In that sense, the draft declaration was intended as a document that expressed the direction of the Fund's own surveillance, and policy advice in the context of program design.

Mr. Sivaraman said that, while the draft declaration was comprehensive, it was not appropriate for it to refer to the judicial system, corruption, and money laundering because those were highly sensitive issues. Those issues would be best dealt with indirectly by mentioning the desirability of improving the transparency of banking systems and the accessibility to information with the aim of preventing the movement of "crime" money among

countries. With respect to the judicial system, countries generally preserved the independence of their judiciaries and would not respond well to Fund interference in that area.

The Chairman responded that the Fund needed to be explicit about its objectives, and therefore should not shy away from issues such as corruption and money laundering.

Mr. Kafka agreed that the declaration should not contain references to noneconomic and nonfinancial matters. Moreover, it was not clear that a new declaration would serve any real purpose since the Madrid Declaration was already a comprehensive document.

Mr. Obame made the following statement:

> This chair welcomes the proposed Interim Committee declaration on a new partnership for sustainable global growth. We believe that as it stands, the proposed text is a useful and pragmatic complement to the Madrid Declaration adopted two years ago. We also believe that it is very opportune, as it clearly emphasizes the main element that there should be a common economic strategy on the responsibilities of the entire membership of the Bretton Woods Institutions in the growth and interdependence of economies. Indeed, while the globalization of the world economy is creating new opportunities, it also truly entails potential challenges, particularly for many developing countries.
>
> As far as African countries are concerned, one of the main challenges that they face is their speedy integration into the world economy. This process, as is well recognized, requires both the implementation of ongoing adjustment efforts and a supportive external environment. On the latter, it should be pointed out that African countries' access to international capital and goods markets remains limited, and that the outlook for these countries seems to leave little scope for optimism because of the substantial decline in the volume of private and public flows projected in the World Economic Outlook document. Moreover, despite the growing consensus that has been secured for a continuation of ESAF operations, and the progress made in the adoption of the HIPC Initiative, some uncertainties still remain on their financing modalities.
>
> For these reasons, among others, we consider that a new and effective partnership between the African countries and the international community is urgently needed, and we would have no difficulty in supporting the proposed partnership for sustainable global growth.
>
> Finally, on some specific points underlying the main challenges facing some groups of countries, I would like to propose that the third point dealing with developing countries, on the first page, be slightly amended to read as follows: "Sustaining economic performance and alleviating poverty in developing countries."

Ms. Lissakers stated that she did not see any compelling need for a new declaration. The Interim Committee communiqué had served the institution and its membership well as a means of assessing progress and laying out policy guideposts for the Fund's broad economic strategy. If a new declaration were deemed necessary it should be

more tightly drafted, and could legitimately include reference to the need for human resource development as one element needed for sustainable growth.

Mr. Esdar noted that many elements of the Madrid Declaration remained valid and had simply been repeated in the new declaration. It might therefore be sufficient simply to recall those elements and reaffirm their validity. Care should also be exercised in not extending the mandate of the Interim Committee to cover issues more pertinent to the World Bank, such as human capital development. Caution should also be exercised in making specific recommendations for certain regions.

Mr. Coumbis concurred with the approach suggested by Ms. Lissakers.

Mr. Al-Tuwaijri said that he fully supported the approach proposed by Ms. Lissakers.

Ms. Lissakers questioned whether the document was intended as a statement of an Interim Committee program of action, directed specifically at the Fund, or as a reflection of a broad conceptual agreement by Fund members about what the essential elements of an effective economic growth strategy were. If the latter were to be fulfilled, the document would need substantial revision along the lines that many Executive Directors had suggested especially by deleting regional-specific and institution-specific references.

Mr. Berrizbeitia said that he shared the concerns expressed by most Directors on the drafting and nature of the document. It would be preferable to review the drafting of the Madrid Declaration itself. Many of the concepts contained in the new paper could be included in the framework of an updated Madrid Declaration while maintaining the tightness of the original draft. The revised Madrid Declaration should have a reference to the increasing importance of the social content of economic programs for the sustainability of economic growth. Appropriate language—such as "good governance," "improving governance," or "improving judicial and personal security"—might also be found, for dealing with issues such as corruption and money laundering. More specific reference should be made to the importance of reasonable exchange rate stability among the key currencies of the world as a necessary condition for sustained growth in the world economy. Finally, some reference in the updated version to the importance of the quality and composition of fiscal adjustment could be desirable.

Mr. Evans agreed that the best approach would be to update the Madrid Declaration to reflect what had been achieved since its adoption. On the question of human resources, fiscal consolidation should be integrated with the need for quality adjustment, for example through increased attention to health care and poverty alleviation. Corruption and money laundering would also have a direct impact on economic activity and growth, and that should be recognized in the updated declaration.

Mr. Han agreed with the thrust of the draft declaration noting that it should focus on price stability, fiscal consolidation, and structural reform, while care should be exercised when referring to "the renovation of the state."

Mr. Zoccali noted that his authorities attached great importance to the quality of the message that was being portrayed in the draft declaration. Caution should be exercised in the wording, particularly where there were regional or country-specific references. But there was clearly an interdependence between structural and macroeconomic policies, and a recognition

that the soundness of macroeconomic policies alone would not ensure sustainable noninflationary growth. It would be important to rescue that part of the message, be it in an updated Madrid Declaration, another global growth sustainability declaration, or even the Interim Committee communiqué itself.

Mr. Wijnholds agreed that the best way to proceed would be to update the Madrid Declaration ensuring that it made reference to misalignment of exchange rates.

Mr. Kaeser said that he supported Mr. Wijnholds, noting that the issue of governance was quite broad.

Mr. Mesaki agreed that the Madrid Declaration should be updated. In that regard, the new declaration appeared to focus too heavily on regional issues. References to North America, Japan, and Europe should therefore be removed from the draft. More attention should also be paid to human resource issues. A general reference to exchange rate policy would be more desirable than reference to specific currencies.

Mr. Andersen associated himself with the comments made by Mr. Waterman.

Mr. Fayolle agreed that there was a need to update the Madrid Declaration. The text should include broad statements and concentrate on the most important issues, such as fiscal consolidation, inflation, reinforcement of international financial stability, and structural reforms. It was not clear that the revised draft should include references to human resource issues, but it should certainly deal with the quality of fiscal adjustment. Corruption and money laundering would not find an appropriate setting in the updated declaration.

Mr. O'Loghlin agreed with those Directors who were inclined to reaffirm the Madrid Declaration, with appropriate addenda.

Mr. Mohammed agreed with those Directors who wanted to adhere to the Madrid Declaration, with certain refinements while excluding noneconomic issues.

Mrs. Cheong supported the proposal for updating the Madrid Declaration with an emphasis on ensuring continued macroeconomic stability together with the alleviation of poverty. The composition of fiscal adjustment would also be an important consideration. In that regard, the issue of human resource development could be linked in a way that suggested the complementarity between macro and the micro policies. While specific countries should not be mentioned in the Declaration, there should be a reference to the transition process in the European Monetary Union and its impact on the global economy.

Mr. Mozhin agreed that the appropriate course of action would be to update the Madrid Declaration. However, the revised version should contain most of the points raised in the draft declaration. There were some issues that were more suited to the Interim Committee communiqué, such as the quota review and the SDR issue.

Ms. Lissakers agreed with Mr. Kaeser that governance should not be defined too narrowly. The phrase "good governance" itself was broadly acceptable.

The Chairman stated that, to achieve progress on the governance front, there were merits in spelling out exactly what issues were to be considered under the "governance" umbrella.

Mr. Rouai stated that he could go along with an update of the Madrid Declaration, although a short paragraph in the Interim Committee communiqué updating the declaration would have been preferred.

Mrs. Guti said that she could go along with the emerging consensus for a revised Madrid Declaration. It would be appropriate for the revised draft to incorporate Ms. Lissakers's suggested approach to the governance issue and to preserve mention of concessional flows, poverty alleviation, and human resource issues.

The Chairman concluded that most Directors wished to update the Madrid Declaration. A revised text would be prepared that would take into account the concerns raised by Directors during the discussion, in particular, on the human resources issue. In addition, many Directors had expressed reservations about the regional dimension of the updated global strategy. Those references could be dropped from the revised draft, but that would risk de-emphasizing the systemic importance of the major industrial countries. It had to be recognized that budget consolidation in North America had systemic importance, as did the deregulation and further opening of the Japanese economy and the success of European Economic and Monetary Union. In that connection, several Directors had mentioned the issue of exchange rate stability, particularly among the three key currencies.

The meeting was adjourned at 11:55 am.

The Executive Directors agreed to continue their discussion on Thursday, September 26, 1996.

REINHARD H. MUNZBERG
Secretary