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COMMITTEE ON MEMBERSHIP—EAST TIMOR

Meeting 02/1

10:00 a.m., April 23, 2002

C.D.R. Rustomjee, Chairman

Executive Directors	**Alternate Executive Directors**
	A. S. Alosaimi
M. J. Callaghan	A. Baukol, Temporary
A. V. Mozhin	
P. C. Padoan	
K. Yagi	
A. G. Zoccali	

S. Soromenho-Ramos, Secretary
M. Schrader, Assistant

Also Present

	S. Boitreaud
D. I. Djojosubroto	
F. Varela	
Wei, B.	

IBRD: E. Sanidad, S. Lawani. Asia and Pacific Department: Y. Horiguchi, D. Citrin, S. Schwartz, I. Kim. Fiscal Affairs Department: K. Ogata. Legal Department: S. Ho. Policy Development and Review Department: L. Ebrill, A. Pitt. Secretary's Department: L. Hubloue. Treasurer's Department: B. Newman, H. Trines, P. Ross, S. Ding, B. Yuen. Advisors to Executive Directors: M. F. Melhem, J. N. Santos. Assistants to Executive Directors: M. Abbing, T. Koranchelian, K. Kpetigo, R. Maino, M. Marques, Y. Saito, D.B. Waluyo.

1. EAST TIMOR—CALCULATION OF QUOTA

The committee members considered a staff paper on the calculation of a quota for East Timor (EB/CM/East Timor/02/1).

The Chairman stated that the Committee's task was to recommend a quota for East Timor and other terms and conditions of its membership in the Fund. It was a privileged opportunity to consider membership for a new member in the Fund. Following past practice, the Bank staff had been invited to attend the meeting, as East Timor was applying for membership in both the Fund and the Bank. As noted at the Board on the occasion of the announcement of East Timor's application, the authorities were eager to minimize the gap between independence—scheduled for May 20, 2002—and membership in the Fund, as well as in other international organizations, in order to expedite the integration and regularization of their relations with the international community. To accommodate the authorities' request, the Committee should try to conclude its deliberations as soon as possible so as to send a recommendation to the Board at the end of April 2002, and leave enough time for the Board of Governors to vote on the membership resolution during the month of May 2002, and hopefully conclude in time for East Timor's independence on May 20, 2002.

In order to calculate a quota for East Timor, the staff had used three different methods, the Chairman continued. The first approach used the official GDP data, but the data for current transactions had been imputed by assuming that the openness ratios for East Timor during 1982–94 had been equal to its average openness ratio during 1995–99. That approach had been based on the assumption that information on East Timor's external transactions during the recent period was more reliable than the data for the earlier period, and that GDP data were relatively reliable. The second method used the official 1994 GDP figure of East Timor to impute external transactions data from the data used for Indonesia under the Eleventh Review of Quotas, based on East Timor's share in Indonesia's GDP in 1994. The third approach used the average "openness ratio" of 10 other Pacific island countries with similar characteristics to East Timor to derive data for the quota calculation. All methods had been used previously in membership application processes. Using each of the three methods, the resulting calculated quotas for East Timor were SDR 7.9 million, SDR 6.8 million, and SDR 14.5 million, respectively. Those calculations—based on ratios of actual to calculated quotas for broadly comparable groups of countries—yielded a range of SDR 3.7 million to SDR 8.7 million for the initial actual quota for East Timor. The staff had suggested, however, that a plausible initial quota would be in the upper half of the illustrative quota range, or between SDR 6.2 million and SDR 8.7 million.

The staff representative from the Asia and Pacific Department (Mr. Schwartz) informed the committee members that East Timor's Minister of Finance—and the Fund's designated contact person on membership issues—had recently resigned. However, that development would not affect the envisaged timetable and the membership process. The staff had been in contact with the office of the Chief Minister of the Second Transitional Government of East Timor, who had reiterated East Timor's interest in joining the Fund as early as possible, and had not raised any issues with respect to the quota calculation. The staff's understanding was that a new finance minister would soon be appointed, and the Chief Minister would take care of the membership aspects in the meantime.

The staff representative from the Treasurer's Department (Mr. Trines) noted that, on the quota calculation itself, the staff had been following established procedures, using available precedents wherever possible, particularly given the existing data deficiencies in some areas of East Timor. The main aspect to consider in making a decision on the quota was how to derive the actual quota based on the calculated quota. Table D on page 31 of the staff paper showed quite large ranges of actual to calculated quota ratio for the countries listed in that table. The ranges for the Fund membership as a whole were even larger, ranging from a minimum of 0.1 for Singapore to a maximum of 4 for Equatorial Guinea. One reason was the growing divergence between actual and calculated quotas often experienced over time by countries that had joined at an earlier stage, either because variables used for their quota formulas had in some cases grown faster than the general quota increases, or in other cases they had grown slower. Considering countries similar to East Timor, the staff had recommended the quota to be in the upper range of the total calculated range, but in the end it was up to the Committee and the Board to decide on the ratio to be used to derive the actual quota for East Timor.

Mr. Padoan made the following statement:

> Let me take this opportunity to thank the East Timor authorities for having asked my office to look after their interests during this important transition phase. It is, indeed, an honor to look after the membership process of a new member in the IMF. On behalf of my authorities, I wish the East Timor authorities much success and express my gratitude. We will fully support them in this process.
>
> I would also like to thank the staff for a well-balanced and comprehensive paper. I agree with the staff that the actual quota be located toward the upper end of the suggested range, between SDR 6.2 million and SDR 8.7 million, for two reasons. First, while the openness of East Timor's economy is limited at the present stage, there is clearly a potential for increased openness in the short to medium-terms, not only based on the oil sector but also on the fast integration of the world economy; and second, because of the comparison with similar economies in the region and elsewhere.

Mr. Callaghan made the following statement:

> I would like to thank the staff for a useful and concise paper, which is particularly good given the fact that there is no precision in terms of quota calculations and that other, more policy-related considerations, should be taken into account. The determination of the actual initial quota for a new member requires—besides mathematical calculations—also prudent judgment. The staff paper provides useful guidance in that respect. I agree with Mr. Padoan and the staff that the actual quota for East Timor should be at the upper end of the suggested range. The most unreliable data is on external transactions, and it is likely that the amount was significantly underestimated.

For that reason, considering the three different methods for the quota calculations, Method 3 seems to be the appropriate one to apply. Although it seems unclear whether East Timor has currently the same degree of openness as the other Pacific islands, other aspects, such as its relative size, its GDP, and its population indicate that in comparison to the other countries, its quota should be at the upper end of the range.

Mr. Baukol made the following statement:

I would like to thank the staff for a well-written and concise paper.

Of the three different data calculation methods, Method 3 seems to be the most problematic approach, because the comparability of data should be treated with caution. Methods 1 and 2 provide a calculated quota of SDR 7.9 million or SDR 6.8 million, respectively. Deflating these numbers to derive an actual quota delivers a range of up to SDR 4.8 million. This is the range that, on first glance, seems appropriate to me. However, there are a number of reasons that justify a slightly higher quota. As noted in the staff paper, current transactions are probably underestimated, particularly when using Method 2. Therefore, a slightly higher quota would be justified. In addition, as Mr. Padoan has already mentioned, the potential for greater openness in the future may also justify a higher quota. Also, like Mr. Callaghan, I believe that Table D of the staff paper and the comparison to other countries indicate that a quota of SDR 4.8 million would probably be too low. Comparing the GDP of East Timor to countries like Bhutan, St. Vincent and the Grenadines, and the Maldives, all with slightly lower GDPs, but with quotas between SDR 6.3 million and SDR 8.3 million, would lead me to agree with the staff and to consider the upper end of the range in the staff paper as a reasonable actual quota. From the staff's suggested range of SDR 6.2 million and SDR 8.7 million, I tend toward the lower end, around SDR 6 to 7 million. However, I remain open to arguments in the discussion.

Mr. Zoccali made the following statement:

We are grateful to the staff for this well-balanced paper, which provides useful guidance for our discussion. I would also like to welcome the opportunity to discuss the application for membership of East Timor. We fully concur with the Chairman that we should strive to minimize the gap between independence and Fund membership. Substantial progress has been made, and I believe the Fund should be accommodative of the authorities' desire in this regard.

On the choice and specification of the variables, we concur with the staff that the data to be used should coincide with that used for the Eleventh General Review. We agree that 1994 GDP adequately reflects East Timor's estimated economic size and indicates the potential need for Fund resources.

As Mr. Callaghan has said, the derivation of an initial quota formula for any member is more an art than science, and we certainly welcome the fact that the staff has provided three alternative approaches for estimating a complete set of data for quota calculations.

We also recognize, as other Directors, the problem of data quality and the obstacles detailed by the staff in Box 3 of the paper. We also acknowledge the cautious remarks with respect to the balance of payments information, external transactions, and reserves. In any event, as other speakers, we would have some difficulty to agree to apply Method 3, which uses the average "openness ratio," for the determination of the initial actual quota, given the existing problems with the comparability of the data. Instead, as Mr. Baukol noted, we should be focusing our overall judgment on the basis of the Methods 1 and 2.

In any event, for assessing the actual quota, we would consider it appropriate to place the country within the group of very small quotas for the Pacific island members. At the same time, the information provided in Table D shows that the calculated quotas for East Timor are on the low end, considering the country's size, population, and economic prospects associated with the major oil and gas discoveries, as well as the potential improvements in agricultural productivity; all these aspects would have an impact on the degree of future openness. With this in mind, we concur with staff that an appropriate initial quota range would be in the upper half of the suggested range, between SDR 6.2 million and SDR 8.7 million. We would agree to an initial actual quota right in the middle of that range.

Mr. Alosaimi thanked the staff for a well-written and informative paper. On the determination of the appropriate initial actual quota for East Timor, it seemed that all three methods discussed in the paper had their weaknesses. However, in view of data deficiencies and the precedent of using Method 3 in the case of Eritrea, and taking into account the reasons detailed in paragraph 75 of the staff paper, an initial actual quota in the middle of the upper half of the illustrative quota range, between SDR 6.2 million and SDR 8.7 million, seemed reasonable.

Mr. Yagi thanked the staff for the well-balanced paper and welcomed the application of East Timor for membership in the Fund. The membership process would hopefully be concluded as quickly as possible, according to the wish of the authorities. Concerning the calculation of the initial actual quota, Method 2 did not appear to be appropriate as it was based on the concept of dissolution rather than succession. As East Timor was deemed to be in a succession process, Methods 1 and 3 appeared to be more appropriate. Method 3, in particular, seemed to deliver some advantages as it had been used in the case of Eritrea and used the average "openness ratio" of 10 other Pacific islands. As East Timor was quite small, similar to the Pacific island members, this comparison appeared to be also applicable to the calculation of the initial actual quota. In that sense, the proposed upper range of SDR 6.2

million to SDR 8.7 million was justified. Based on those considerations, an initial actual quota at the upper end of that range seemed appropriate.

Mr. Mozhin thanked the staff for its informative and well-balanced paper. Based on his own experience after the states of the former Soviet Union became independent countries, he was aware of the difficulties in calculating quotas, given the limited reliability of data on external transactions, which used to be domestic, but would become external after independence. There seemed to be broad agreement among the committee members that the initial quota for East Timor should be in the range of SDR 6.2 million to SDR 8.7 million. He would appreciate some further information on the envisaged timetable for the Committee's work before expressing his own views.

The Chairman stated that, in the past, the quota for a new member had usually been determined in the first meeting of the Committee on Membership. After agreement was reached on the initial actual quota, the Committee's decision would be communicated to the authorities. If the authorities accepted the Committee's proposal, a brief report would be prepared for consideration by the Board. The report would include a draft Resolution, containing the terms and conditions of membership as proposed by the Committee, for a vote by the Board of Governors.

Thus far, there appeared to be consensus that the staff paper was well-prepared and covered the whole range of possible options; that the staff's recommendation that the quota should be within the range of SDR 6.2 million and SDR 8.7 million was acceptable; and that the Committee should try to accommodate the authorities' wish to proceed expeditiously, the Chairman continued. On the issue of methodology, different preferences existed among Directors as to which of the methods was most appropriate to determine the quota, with some Directors preferring Methods 1 and 2, and others Method 3. Considering Table D on page 31 of the staff paper, he wondered whether a compromise could be forged around a quota between SDR 8.2 million and SDR 8.3 million, which was within the upper end of the range the staff had suggested, and seemed appropriate and justified. He had been impressed by the close correlation between the figures, particularly GDP, for East Timor and Kitts and Nevis using Method 3. The average current payments were also almost identical. In addition, the GDP of East Timor was the seventh highest and population the fourth highest among the group.

Mr. Padoan reiterated that no single method was the optimal one, and based on the Chairman's considerations, his chair supported the Chairman's proposal. To form a prudent judgment on the quota, it was not only important to consider the current figures, but also taking into account the potential of East Timor in the near future, particularly in view of the likelihood that independence will generate economic units with usually a high rate of expansion, growth, and integration. The calculations offered a good base to start one's considerations. However, they inevitably underestimated the economic potential not only of East Timor, but of any country at the beginning of its economic and political life.

Mr. Baukol expressed concern about the Chairman's suggested range. Table C on page 30 of the staff paper indicated a range from SDR 3.7 million to SDR 8.7 million. The deflation numbers the staff had used (0.602 for pacific island economies and 0.548 for countries with quotas of less than SDR 15 million) reflected a higher net result than a deflation for all Fund members. Therefore, to some extent that method delivered a higher actual quota. Considering the figures in Table C and the concerns some Directors had expressed about Method 3, the suggested quota range of SDR 8.2 million to SDR 8.3 million gave too much weight to the Method 3 calculations. Moreover, having listened to other committee members, a more appropriate consensus on an actual quota would be at SDR 7.5 million, the midpoint of the suggested upper quota range.

Mr. Callaghan supported the Chairman's suggestion of SDR 8.2 to SDR 8.3 million, considering that, like Mr. Yagi, he would have preferred a higher figure. In defense of Method 3, the staff had argued in paragraph 73 of the paper that the sum of East Timor's estimated average current receipts and payments ranked significantly lower, near the bottom for Methods 1 and 2. Those figures were the ones that were probably underestimated, and Method 3 had been an attempt to address that problem. Considering Table D on page 31 of the staff paper and comparing East Timor to other similar economies, the GDP figure of East Timor and the size of population would justify a quota of at least SDR 8 million. Those considerations seemed more relevant than the figures that resulted from applying a particular ratio to the imprecise calculated quotas to yield the actual quota.

Mr. Wei welcomed East Timor's application for membership in the Fund and thanked the staff for a well-written paper. On the issue of the quota calculation, he supported the application of Method 3 and an initial actual quota for East Timor in the upper end of the range, above SDR 8 million, given the size of the population and GDP. The country was in urgent need of financial assistance from the Fund and the Bank, which should also be emphasized in the discussion. In that sense, he supported the highest quota possible.

Mr. Boitreaud noted that the argument in favor of the upper end of the range appeared stronger than the other arguments he had heard. As Mr. Padoan had pointed out, it was important to consider the future potential of the economy, including the prospects of significant oil and gas revenues, and of more open trade. In his opinion, those arguments pointed to the Chairman's proposal of SDR 8.2 million or SDR 8.3 million.

Mr. Varela welcomed the informative and useful staff paper. His chair supported the regularization of the relationship of East Timor with the Fund and its membership, as it would help the country in its quest toward economic development and social progress. On the issue of the quota calculation, his chair supported the argument that some weight should be given to the size of East Timor's population. The growth potential of the economy and the degree of openness, which would further increase in the future, would justify an initial actual quota of SDR 8.2 million or SDR 8.3 million.

Mr. Kpetigo supported the Chairman's proposal of an initial actual quota of SDR 8.2 million to SDR 8.3 million, given the size of the population and the growth potential of the economy.

Mr. Jayatissa also supported the Chairman's proposal.

Mr. Mozhin, noting the need to avoid setting an unhelpful precedent, suggested SDR 8 million.

Mr. Padoan reiterated his support for the Chairman's proposal.

Mr. Baukol supported Mr. Mozhin's suggestion, not only because of the rounded figure, but because it constituted a compromise between the Chairman's proposal of SDR 8.3 million and the proposal for SDR 7.5 million. An initial quota of SDR 8 million better reflected the weight of the arguments that had been put forward during the discussion.

The Chairman suggested that SDR 8.2 million might constitute a viable compromise in view of the figures for comparable countries in Table D of the staff paper. The majority of committee members seemed to favor an initial quota for East Timor in that range.

The Committee agreed to the proposed amount of SDR 8.2 million.

The Chairman turned to the staff's proposal that East Timor's reserve asset payment be set at 24 percent of its total quota.

The Committee agreed to the proposed amount.

The Chairman asked whether committee members agreed that it would be appropriate to allow East Timor six months to pay its subscription.

The Committee agreed to the six-month deadline.

The Chairman asked the Committee Secretary to follow up by contacting the East Timor authorities to inquire whether they were willing to accept the proposals of the Committee. If the authorities indicated their acceptance, he would prepare—and then clear with committee members—a report for circulation to the Executive Board, possibly for discussion by the Board on May 1, 2002. The report would include the draft Resolution containing the terms and conditions of membership as proposed by the Committee, and the matter would then be sent to the Board of Governors for a vote by mail over a period of three to four weeks. Completing the vote close to the date of independence, on May 20, 2002, would be preferable.

Once the vote was completed, and assuming that the resolution was passed, East Timor would have six months to prepare the legal documentation needed to enable a representative from East Timor to come to Washington, D.C. and sign the original Articles of Agreement, thereby completing the membership process, the Chairman concluded.

The meeting adjourned at 10:55 a.m.

APPROVAL: June 6, 2002