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September 1, 1983

To: Members of the Executive Board
From: The Acting Secretary
Subject: Final Minutes of Executive Board Meeting 83/54

The following correction has been made in EBM/83/54 (3/28/83):

Page 29: for "Decision No. 7373-(83/54), adopted
March 23, 1983"

read "Decision No. 7373-(83/54), adopted
March 28, 1983"

A corrected page is attached.

Att: (1)

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Department Heads

the same time, the staff had been warning the international community that the use of Fund resources was no substitute for long-term development aid. If the Fund was making available a comparatively small amount at the present time, it was because it was aware of the debt service difficulties that the provision of larger amounts--other than outright aid--was likely to cause.

Mr. Malhotra said that he was grateful to the Chairman for the explanation; naturally, the authorities would greatly welcome more development assistance, which was in general cheaper than the use of Fund resources. He pointed out that if workers' remittances were taken into account, which according to the staff would be appropriate in the case of Bangladesh, the debt service ratio declined from some 29 per cent or 30 per cent to under 20 per cent. He realized that some could still argue that even that ratio was high for a country in the position of Bangladesh. In his own view, Bangladesh could legitimately have recourse to the Fund's resources, if only because its problems were mainly connected with the balance of payments strain due to deterioration in the terms of trade.

The Executive Board then took the following decision:

1. The Government of Bangladesh has requested a stand-by arrangement in the amount of SDR 68.4 million for a period from March 28, 1983 through August 31, 1983.
2. The Fund approves the stand-by arrangement set forth in EBS/83/56, Supplement 1, and waives the limitation in Article V, Section 3(b)(iii) of the Articles of Agreement.

Decision No. 7373-(83/54), adopted
March 28, 1983

2. SURVEILLANCE - REVIEW

The Executive Directors considered a staff paper on the annual review of the implementation of surveillance (SM/83/43, 3/1/83; and Sup. 1, 3/21/83; and Cor. 1, 3/22/83).

Mr. de Groote remarked that, despite the Fund's surveillance, exchange rates for the major currencies continued to be characterized in 1982 by substantial short-term volatility, while some of them remained out of line with economic fundamentals. The reasons for the apparent lack of success were not to be found in inadequate implementation of the Fund's surveillance procedures; the staff had clearly shown that the procedures had been appropriately followed. However, the Fund had no legal powers to enforce its recommendations unless countries applied for the use of its resources. The effectiveness of the Fund's surveillance continued to depend very much on the willingness of major countries to heed its recommendations in formulating their own policies. Japan was

probably the best illustration of how Fund recommendations could be applied effectively when the country cooperated, as was clear from the 1982 Article IV consultation (EBM/83/48 and EBM/83/49, 3/18/83).

The focus of the Fund's surveillance, Mr. de Groote considered, should be different for countries that allowed their rates to flow freely from that for countries with managed floating. For cases of pure floating, Fund surveillance should focus mainly on the broad macroeconomic policies being pursued by the countries as they were reflected in the behavior of the exchange rate. For instance, recent movements in the dollar exchange rate had been closely related to the mix of fiscal and monetary policy. Assessment of the difference between the observed exchange rate and the equilibrium rate required a frame of reference for defining the equilibrium rate itself. Any such frame of reference would have to take into consideration the internal policies of the country and their interaction with the policies of the rest of the world, in order to be sure that the internal policies maintained the countries' competitive position while simultaneously preventing them from imposing excessive burdens of adjustment on other countries. Determination of the criteria to be used for evaluating such policies was one of the most difficult aspects of the Fund's surveillance. It was by no means obvious that such criteria could be agreed upon. He therefore looked forward eagerly to the staff's further reflections on such matters in the coming months, in the hope that more progress would have been made by the time of the 1984 review of Fund surveillance.

Under a system of managed floating, which implied some exchange rate target, Mr. de Groote went on, the focus of Fund surveillance should be on balance of payments objectives and intervention policies. In that case, surveillance would have to function on two levels: first, to determine whether the exchange rate target was appropriate, which implied generally the same sort of surveillance as in the case of pure floating, and second, to assess the appropriateness of the country's policies with respect to the exchange rate target. The appropriateness of the policies could be judged essentially in the light of the sustainability of the balance of payments position. The prospective current account position, incorporating any anticipated debt service, and the likely long-term capital flows, would have to be considered in assessing the viability of the exchange rate, making allowance for the reserves--whether owned or borrowed--on which the authorities could count.

Closely related to the exchange rate targets was the matter of intervention in foreign exchange markets, Mr. de Groote remarked. Considerable further work would be required to obtain a better view of the consequences of intervention on other countries and the intervening country whose capital markets were interrelated. On that point, he urged the participants in the Versailles summit to release the results of the study of exchange rate intervention. The matter of cooperation in intervention policies especially needed further examination. The seminar on the future of the special drawing right had shown that there was considerable scope for closer cooperation of that kind. The interrelationship and interactions