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J. de Larosière, Chairman
R. D. Erb, Deputy Managing Director

Executive Directors	Alternate Executive Directors
	L. K. Doe
	M. K. Bush
	H. G. Schneider
B. de Maulde	
M. Finaish	
H. Fujino	M. Sugita
	D. Hammann, Temporary
J. E. Ismael	
	G. W. K. Pickering, Temporary
A. Kafka	
H. Lundstrom	
E. I. M. Mtei	A. Abdallah
	J. J. Dreizzen, Temporary
Y. A. Nimatallah	J. E. Suraisry
	G. Ortiz
J. J. Polak	J. de Beaufort Wijnholds
	A. V. Romuáldez
	H. Alaoui-Abdallaoui, Temporary
	A. S. Jayawardena
	T. A. Clark
S. Zecchini	N. Coumbis
	Wang E.

L. Van Houtven, Secretary
J. M. Oppenheim, Assistant

Also Present

Administration Department: V. R. Sertic. European Department: M. Dakolias, T. M. Ter-Minassian. Exchange and Trade Relations Department: W. S. Tseng. External Relations Department: A. F. Mohammed, Director; N. K. Humphreys, Chief Editor; H. P. G. Handy, R. W. Russell. Fiscal Affairs Department: V. Tanzi, Director; G. M. Bartoli, C. A. Sisson. IMF Institute: O. B. Makalou, C. Tognetti. Legal Department: G. P. Nicoletopoulos, Director. Middle Eastern Department: R. H. Floyd. Research Department: R. R. Rhomberg, Deputy Director; D. Folkerts-Landau, M. Goldstein, M. S. Khan, M. D. Knight. Western Hemisphere Department: E. Wiesner, Director. Personal Assistant to the Managing Director: S. P. Collins. Advisors to Executive Directors: K. A. Hansen, S. M. Hassan, J. Hospedales, H.-S. Lee, M. Z. M. Qureshi, E. M. Taha, N. Toé. Assistants to Executive Directors: W.-R. Bengs, M. B. Chatah, S. de Forges, J. de la Herrán, R. Fox, L. Hubloue, M. Sarenac, A. A. Scholten.

1. FUND-SUPPORTED ADJUSTMENT PROGRAMS

Executive Directors resumed from the previous meeting (Seminar 85/2, 7/19/85) their discussion of papers relating to the effects of Fund-supported adjustments programs on economic growth: a survey of the empirical literature (SM/85/96, 4/4/85); the global effects of Fund-supported adjustment programs (SM/85/97, 4/4/85); and Fund-supported adjustment programs, fiscal policy, and the distribution of income (SM/85/113, 4/25/85; and EBD/85/182, 7/16/85).

The staff representative from the Research Department noted that the first general issue raised by Executive Directors had been whether the conclusions of the staff paper on the effects of Fund-supported adjustment programs on economic growth were too guarded and perhaps too defensive. The problem that the staff faced was that the scarcity of studies on the subject made it difficult to reach any strong conclusions. The available studies were at best indirect and often reached ambiguous conclusions; thus, it was preferable to err on the side of caution. Otherwise, the paper would not have satisfied Mr. Polak's third criterion for publication--that the paper should not make any broad claims beyond the evidence provided. Further studies should look at whether Fund programs had effects on growth that were different from those of other feasible stabilization strategies. It would be best to make the investigations on a case-by-case basis. The evidence produced could be used to answer questions, such as that raised by Mr. Ortiz, whether the programs achieved their stated goals and objectives at some notional minimum cost. The difficulties involved in that type of exercise should not be downplayed, however; the proper instruments of analysis were lacking. Further models to handle the counterfactual issues would have to be developed, and the problem would be to develop models that were sufficiently general with respect to policies and specific enough to the individual country to be able to deal with such issues. Modeling exercises were the only way to address the counterfactual issue objectively.

Although Executive Directors had not found it surprising that Fund programs should have an adverse effect on the rate of economic growth in the first year, the staff representative noted, there had been certain differences of opinion about whether the initial effects were offset in the medium to long term. The staff's view was that there would be a positive effect on growth provided that the appropriate supply-side measures were included in the program. The speed of supply response depended upon the individual characteristics of each country. There was some evidence, albeit limited, that the supply response could be quite rapid in certain countries. The staff's view was that when programs were considered in a medium-term perspective, there might well be no tradeoff between adjustment and growth.

Given that a desired balance of payments outcome could be achieved by a combination of policies designed to reduce absorption, increase domestic output, increase production, and reduce the consumption of tradables, it remained a matter of judgment to determine the mix or

weight placed on different policies in the program, the staff representative observed. There was no really general answer to the question how much emphasis should be given to demand management relative to supply-side policies. The answer would depend on a number of factors, including the nature of the disequilibrium that had initiated the program, the availability of foreign financing, and the political feasibility of certain policies. Deterioration in the current account often occurred because the growth of absorption had outstripped output growth, leading to a need for demand restraint. The paper therefore took for granted that a reduction in absorption rather than output was almost always called for. Policies affecting the level and composition of absorption could have an effect not only on current but also on future output, an effect to which Mr. Kabbaj had alluded in noting that credit restraint adversely affected private investment and therefore growth. Demand and supply policies were closely interrelated: policies designed to achieve a higher rate of growth or domestic output in the medium term generally required an increase in the rate of productive investment, while at the same time, demand management policies were needed to achieve a reduction in the gap between savings and investment. To be consistent, the policy package had to be designed in order to shift aggregate demand toward fixed capital and away from current consumption, a complicated task for the policymaker.

Executive Directors had clearly recognized that Fund programs should stress policies that enhanced growth in the long term, the staff representative continued. Supply-side measures that raised savings and investment ought to be given special emphasis in programs. In that connection, cooperation should continue with the World Bank on investment plans, the effects of changes in producer prices, and trade liberalization. The idea of comparing experience under Fund programs with that of Bank structural adjustment loans and separate loan policies deserved serious consideration.

More specifically, as a number of Directors had rightly pointed out, the evidence cited in SM/85/96 suggested that real domestic savings in developing countries were not interest elastic, the staff representative remarked. The general theory on the relationship between savings and investment, in both developing and developed countries, was currently uncertain. All the same, raising real interest rates to market levels was still an important aspect of adjustment policies, even if it did not have an immediate impact on prior savings. First, such a policy tended to discourage domestic investment projects that would yield an inadequate rate of return over the longer run. Efficient investment projects were encouraged and inefficient ones discouraged. Second, other things being equal, raising domestic real interest rates would tend to increase the supply of foreign savings; therefore, total savings could still rise significantly. Finally, eliminating distortions caused by interest rate ceilings and other constraints tended to increase the flow of savings intermediated by the domestic financial markets, thereby increasing the overall efficiency of the savings and investment process.

The issue of what policies, in addition to interest rate changes, might be used to stimulate savings was complex, the staff representative continued. First, programs placing more emphasis on expenditure taxes might tend to shift the private sector toward more saving and less consumption. Second, the public sector might be able to increase total national savings directly by measures to reduce fiscal deficits, thereby releasing resources to private capital formation. The Fund should work closely together with the Bank and perhaps with the IFC on the development of alternative financial institutions that might generate savings in less developed countries.

As Mr. Ortiz had correctly said, a devaluation might cause a liquidity squeeze for firms that had significant foreign liabilities, thereby resulting in the contraction of domestic activity, the staff representative noted. However, prior to the devaluation, the country had presumably had an overvalued exchange rate, and the same firms had been earning higher profits than would otherwise have been generated. The wrong exchange rate influenced the foreign asset and liability positions of firms, and the correction of that distortion should not be viewed as an unfavorable effect of devaluation. Further, those residents who were net creditors in foreign-denominated assets could become better off as a consequence of the devaluation.

Climatic conditions were very important in the growth process, as Mr. Doe had pointed out, the staff representative commented. Other important factors were the growth in the labor force, education, and technological innovations. However, the staff did not have any clear ideas how policies in Fund programs could affect those factors. There was perhaps a need for more studies in that area.

As Mr. Doe had also noted, large and persistent monetary changes would have a cumulative effect on growth over time, the staff representative continued. The paper had agreed that changes in the money supply or domestic credit might be, and certainly would be, large if they persisted over time.

There was little evidence on the effects of changes in the level and composition of fiscal policy, the staff representative pointed out, largely owing to the problems of modeling such shifts in policy.

Mr. Finaish had asked whether the 1981 programs' emphasis on demand-side measures explained why growth targets in the programs had been missed by such a large extent, the staff representative from the Research Department recalled. That was certainly one interpretation. Another might be that the targets themselves had been overambitious or based on forecasts of other exogenous variables that had turned out to be incorrect. It was difficult to say what the reasons for the non-achievement of the targets might be.

The staff representative from the Research Department with responsibility for the paper on the global effects of Fund-supported adjustment programs (SM/85/97) considered that the global effects of programs could be altered by efforts on the part of the international community to slow down the speed of adjustment in program countries. The best way to look at the issue was to consider the "own" and cross-country effects of alternative adjustment speeds. In order to estimate the "own" country effects of different adjustment speeds, the Fund staff had used macroeconomic models to carry out certain simulations of small, open economies, the conclusion having been that national authorities could reduce somewhat the effects on output and employment of tighter monetary and fiscal policies by slowing down the speed of adjustment. It was necessary to recall that under Fund programs, the speed of adjustment was an endogenous variable determined largely by the size and time pattern of external financing and by the necessity to preserve the revolving nature of the Fund's resources. The cross-country effects would be little affected, simply because the size of the basic structural parameters that weighed most heavily in the international transmittal process was so small. The basic message of the paper was that, unless those structural parameters--such as the share of program countries in world trade or the export openness of nonprogram countries--were altered, it was difficult to generate large global effects. That conclusion was fairly reliable.

The staff had tried to give some indication of the regional impact of programs in Tables 7, 8, and 17 of SM/85/97, the staff representative continued. The practical constraint was that the existing world trade models usually did not have that type of regional breakdown. In the exceptional cases when they did, it simply covered the effects of exports and imports and not real income.

The question of the appropriate counterfactual had also been raised, the staff representative noted. A number of Directors had expressed a strong preference for an interpretation of program effects that compared actual performance under the program with the performance that would have been expected in the absence of the program. In a theoretical sense, that was the most appealing definition of program effects. The problem was that the counterfactual was difficult both to identify and to estimate. All the relatively simple and straightforward ways of estimating the counterfactual were either a priori implausible or inconsistent with the data. Observed behavior in program countries prior to the program would not be a good estimate of the counterfactual, nor would the observed behavior in nonprogram countries between the preprogram and the program period, in that nonprogrammed countries were systematically different from program countries prior to the program period. Nor would the trend extrapolation of past policies in program countries be a good estimate of the counterfactual. Estimates of program effects under those alternative definitions suggested that before-after comparisons were not always less favorable than the counterfactual. Often, between the preprogram period and the program period itself, there had been some favorable nonprogram-related shock--for example, an increase in OECD real GNP growth rates--which made the

before-after comparison come out extremely favorably. Sometimes, stabilizing policy action took place even in the absence of programs, making it more difficult to generalize.

Another issue that the paper could have discussed and that had not been raised by critics of the Fund was whether the level of global demand was a legitimate concern in the design of programs, the staff representative observed. The view was offered on pages 78-79 of SM/85/97 that if any decrease in absorption in countries previously experiencing balance of payments deficits was not to weaken global demand, then the best strategy would be for those countries experiencing balance of payments surpluses to increase absorption. That view presumed symmetry in the adjustment process and symmetrical multilateral Fund surveillance, and it also emphasized that the global effects of Fund intervention were necessarily broader than the effects of Fund programs themselves, since the former included the effects of Fund policy advice in nonprogram countries.

On the issue of simultaneous exchange rate action by program countries, the staff representative agreed with Mr. Doe that high supply and price elasticities for certain primary commodities were no guarantee of success for exchange rate depreciation in developing countries, especially if those effects were negated by protectionism in industrial countries. Business cycle conditions in industrial countries were usually a more dominant influence on prices of primary commodities than supply changes induced by exchange rates in developing countries. Mr. Romuáldez had been quite right to argue that non-oil developing countries with trade deficits could be placed in a difficult position because of the adverse price effects that resulted from simultaneous exchange rate action. There were perhaps three offsetting considerations. First, it would be helpful if countries with very similar commodity bundles of exports did not alter their exchange rates at the same time. Second, even where there were certain adverse aggregate price effects, the volume effects of exchange rate depreciation might be large enough to more than offset them them. Third, over the longer term, serious consideration had to be given to export diversification in the direction of those products with high income elasticity of demand.

A question had been raised whether it was necessary in SM/85/97 to isolate two groups of program countries: Group A, which included use of the compensatory financing facility, and Group B, which did not, the staff representative from the Research Department concluded. In doing so the staff had not wished to draw any a priori judgments about whether conditionality in compensatory financing drawings was different from that under stand-by or extended arrangements, but simply to test the sensitivity of the results to alternative definitions of the program country groups. Although the groups had been virtually identical in recent years, that had not always been the case. According to Table 6 in SM/85/97, Group B program countries had had about four times as large a share of world trade as Group A in 1976. During the past four or five years, there had been little difference between the two groups, but, beyond six or seven years previously, there had been no necessary equivalence between Group A and Group B program countries.

The Director of the Fiscal Affairs Department observed that Executive Directors had expressed several opinions on whether the income distribution in program countries was a legitimate Fund concern; management and the Board would have to decide. A further question was whether the staff should routinely pass judgment on the impact of programs on income distribution. Again, that was a decision for management and the Board. If judgments were based on a superficial analysis, they would always be subject to criticism; if, however, they were to be based on detailed analysis, many more resources than were available in the Fund would be required. Consideration would have to be given to the opportunity costs of carrying out such analyses, compared with the allocation of resources to alternative activities.

There was no reason why the staff should not answer specific requests by countries related to income distribution, the Director continued. The Fund staff had already provided technical assistance and had occasionally been asked to analyze the impact of taxes on income distribution. Major studies in Portugal and Korea had been carried out at the request of the authorities. A routine question put to the Minister of Finance of a country before the Fund undertook a technical assistance study of the tax system was whether emphasis should be placed in the proposed tax reform on the efficiency or the equity of the tax system. Fund advice in that area would therefore not represent a departure from present practice.

It would be reasonable to assume, the Director suggested, that, during negotiations with national authorities, the staff already presented alternative policies describing different income distributions for a given fiscal balance, provided that it was able to do so.

As to whether lengthening the adjustment period would diminish the negative impact of demand restraint on certain groups, the Director noted that, if the program were extended over a longer period, additional financial resources would have to be made available. That was not an issue that could be addressed in a paper on income distribution.

The only objective of the paper had been to answer those critics who had argued that Fund programs were almost always biased against the lower end of the income distribution scale, the Director explained. There were indeed programs that had a negative impact on income distribution; by the same token, there were many programs that had a positive impact. However, a priori, it was difficult to make a case that Fund programs displayed a consistent bias against the poor. The results presented in the paper were on average a good indication that no such bias existed.

He did not agree that the paper should have dealt with other dimensions of income distribution, the Director said. The staff had pointed out in the paper that the issue of income distribution was multifaceted: in certain countries, the important aspect of income distribution was regional; in others, the issue was a racial one; in yet others, it was

either that of the old versus the young or capital versus labor. An attempt to examine all those facets would have made it impossible to obtain any meaningful results. After all, the basic issue was whether Fund programs consistently made income distribution worse.

Many critics had said that the Fund's main concern should be whether the bottom 10 percent, 20 percent, or 30 percent of the income distribution scale was negatively affected by a Fund-supported adjustment program, the Director observed. Such a large issue required and would call for an explicit Fund policy. Technically, the exercise would be extremely difficult. The Fund did not have the administrative resources, the tools, or the knowledge to identify those people in the bottom 20 percent of the income distribution and to propose policies that would protect them. In many countries, there was a shocking lack of surveys and information on the poor. Policies that attempted to deliver basic goods to the poor, such as subsidies, might end up benefiting the not-so-poor. However, it was important in designing Fund programs to keep in mind that the poorer group should not suffer disproportionately, and, when it was possible to identify selective policies to help those groups that were not costly in administrative terms, such policies should be carried out. Nevertheless, it would be difficult to establish a general Fund policy in that area, given available knowledge.

As for the methodology, it was true that the analysis was theoretical, a priori, and partial, the Director remarked. A number of Executive Directors had suggested that a case study approach would have been more helpful. He was surprised by some Directors' comments that the conclusions of the paper seemed strong; it had been concluded simply that there could not be any presumption that Fund programs necessarily worsened income distribution. On average, it was unlikely that there would be more programs that had had a negative than a positive impact on income distribution. Therefore, it could not be claimed that Fund programs always had a negative impact on income distribution.

Nor was it likely that an ex post evaluation of programs would have provided less ambiguous results, the Director added. It had long been a basic tenet of economic theory that the with/without criteria were better than the before-after criteria. Valid conclusions about the effects of Fund programs on the income distribution of a country before and after a Fund program could not be reached on the basis of a before-after criterion. A judgment had to be made about what would have happened in the absence of a program, an extremely difficult exercise. The answer was not to be found in other countries. The staff had developed a counterfactual argument that appeared to make some sense, although the counterfactual assumption that policies would not have continued along the same lines in the absence of a Fund program might have been too extreme, yet there was plenty of evidence from around the world that that was what actually happened. In any event, the case-by-case approach would also be open to the objection of selective bias, for instance, in the matter of drawing a random sample to make the study. On the other hand, to

include within the study all 90 Fund programs would consume almost all of the Fund's academic resources. Even the general equilibrium models used at the World Bank would be too time consuming. In any event, the computable general equilibrium models were open to all sorts of objections--not least because of their use of static parameters with data that were often not very good. For most developing countries, such models would be beyond reach for some time to come. Typically, the staff had to make do with much cruder and more partial approaches. However, if the various partial data contained in Appendix I of SM/85/113 were put together, the overall picture would probably not be very different from that contained in a general analysis.

If the paper had concentrated too much on fiscal issues, the Director remarked, it was because it had been prepared in the Fiscal Affairs Department.

In a number of countries, wage policy was at the heart of income distribution issues, the Director observed. For instance, in Argentina, there was a close identity between the poor and wage earners. In most other countries, regular wage earners were more likely to be higher up in the income distribution; the truly poor did not work for wages. It would therefore be inaccurate to generalize about the importance of wage policy for income distribution.

It was far from clear that the problem of stabilization in conjunction with the elimination of excess foreign debt was a problem in all program countries, the Director commented, although it might be in certain program countries. However, within a country, those at the bottom end of the income distribution scale were unlikely to be able to contract domestic debt.

The staff would have had great difficulty in dealing simultaneously with the impact of Fund programs on income distribution and the tradeoff between equity and efficiency, the Director remarked. A very different paper would have resulted. In any event, the staff had considered the question of efficiency in certain cases, including that of export taxes, which had been criticized.

The relationship between the removal of subsidies and the rate of inflation was extremely ambiguous, the Director continued. The removal of subsidies was not part of the inflationary process but a once-and-for-all adjustment. Moreover, the issue should be considered over a slightly longer time period. If the removal of subsidies reduced fiscal deficits, thereby reducing monetary expansion, the effect on inflation could be expected to be positive rather than negative.

According to a recent survey carried out by economic experts at the University of Toronto, food subsidies had the potential to improve income distribution as well as the nutrition of poorer households, the Director said. However, political considerations often affected program design, and, as a consequence, existing schemes were often, although not always,

biased toward urban areas and probably regressive. Even if food subsidies had had a positive effect on income distribution in some countries, it would not be possible to generalize from their experience.

The experience of the Fiscal Affairs Department was that it was very rare for national authorities to be able to improve the administration of the tax system in any significant fashion, within the context of a one-year program, the Director of the Fiscal Affairs Department stated.

Mr. Kafka remarked that when wages and prices were indexed, the removal of food subsidies was not a once-and-for-all adjustment but part of the ongoing process of inflation. In referring to the improvement of administrative performance, he had had high-inflation countries in mind.

Mr. Polak suggested that certain sentences within SM/85/113--the paper on the effects of Fund programs on income distribution--appeared to be far too general in their claims and not based on sufficient empirical work. For example, on page 4 of SM/85/113, the staff stated that: "In the longer run, increased growth and employment, [coming from devaluation] should raise the level of income and improve everyone's position. The Fund-supported program may have improved the absolute standard of living of the poorest quartile at the expense, temporarily, of the overall level of income." It was difficult to know quite what to make of those sentences.

The Director of the Fiscal Affairs Department agreed that sentences that did not appear to conform with the main thrust of the analysis could be deleted.

Mr. Nimatallah asked for a further explanation of the possible trade-off between high rates of growth and more equitable income distribution.

The Director of the Fiscal Affairs Department suggested that it was no longer conventional orthodoxy within the economic profession to believe that a government, through the tax system, could establish a particular income distribution. There was less confidence that a government possessed instruments allowing it to manipulate income than there had been 10 or 15 years previously. Policies that had been pursued with the objective of improving income distribution or promoting growth had all too often had the opposite effect. His own view was that many countries would be better off if they pursued sound, broad-based economic policies--including budgetary, interest rate, and exchange rate policies--that would have favorable effects on income distribution and growth. Nevertheless, every effort should be made to identify the truly poor and to promote sufficiently selective policies to improve their lot. He had already mentioned the possibly regressive effects of subsidies. Experience with progressive income taxes in developing countries had been similar; the tax base shrank as people found alternative sources of income or claimed exemptions from tax. In practice, income distribution was not improved, and, meanwhile the structure of the economy might have been altered sufficiently to have a negative impact on growth.

Mr. Nimatallah responded that critics of Fund-supported programs should be made aware that because of the imperative need to increase savings, a less equitable income distribution might be unavoidable in the short run. It was not necessarily possible to attain high savings simultaneously with higher growth rates and better income distribution; the third element was irrelevant at a certain stage of development.

Mr. Polak said that he agreed with Mr. Nimatallah in principle. It was not so much that income distribution was irrelevant as that it was not the only relevant question.

Mr. Ortiz suggested that the different debt positions of economic agents within the economy had a major impact on income distribution, once adjustment measures were taken. In that context, the length of the adjustment period was extremely important. The more aggravated the debt problem of a country, the more that consideration became relevant. In any event, there was no necessary correlation between the level of national wealth and the ability of sovereign entities to contract debt. A number of countries with very low per capita incomes were extremely heavily indebted.

The Director of the Fiscal Affairs Department said that his point had been that, within a country, it was unlikely that the bottom 20 percent of the income distribution scale would have access to credit.

The Chairman remarked that governments and firms, rather than extremely poor individuals, contracted debt.

Mr. Kafka suggested that, on the contrary, the lowest-paid 10 percent of the population was extremely dependent on credit. One of the problems that had arisen with the appearance of supermarkets in less developed countries was that poorer people no longer had access to credit for the purchase of essential goods.

The Chairman said that as he understood him, Mr. Ortiz had based his argument on the impact of debt, in conjunction with the depreciation of the currency, on funds borrowed from abroad.

Mr. Ortiz pointed out that it was not only firms that contracted large debts. When a government was heavily indebted to internal creditors, assuming that the pace of adjustment was too rapid, it might have to default on part of its internal debt. The distributional effects of that default would be felt by a captive audience--the captive holders of domestic wealth, who had been unable to remove their capital from the country. That issue was relevant to many countries and furnished at least a partial explanation for capital flight and exchange rate variability.

The Chairman agreed that there was an important difference between those who could and those who could not protect themselves against the asset-based consequences of adjustment.

Mr. Nimatallah pointed out that in a number of cases, raising the relevant interest rate might not be helpful. Occasionally, nominal interest rates would have to be raised so much that investment in general might be impaired, particularly in the private sector, for reasons including religious beliefs, the lack of monetization of the economy, and limited public awareness of credit and banking practices. In countries where the staff found it difficult to detect a strong positive relationship between the interest rate and savings, it should take the time to see whether a higher interest rate would have a negative impact on investment that would more than offset the potentially positive impact on savings.

The Chairman made the following concluding remarks:

I shall not make a formal summing up, because that is not the usual practice at seminars, but I would like to make some personal concluding remarks.

First, the Fund operates under two fundamental constraints. One stems from the Fund's Articles of Agreement--the revolving nature of its resources and the monetary character of the institution--which govern the way it operates. The Fund cannot act as the agent of growth in the system, but has to model its activities within the limited framework of its Articles. Accordingly, the question is not so much "do Fund programs have a negative effect on growth?"; rather, it is "what would have happened if members had not had the Fund's support in their adjustment programs?" It would be interesting to know what sort of criticism the Fund, as an institution, would have faced if it had abstained from supporting such programs since the end of the 1970s, simply because the problems were too tough. That interesting question is rarely posed. I agree with those Directors who have indicated that the Fund has played a major role in stabilizing the system, reassuring creditors by intervening as a catalytic agent in the system, and thus having had a positive influence on growth or at least having contributed to the moderation of the recession.

The other constraint within which the Fund operates stems from the external financial and economic environment in which the programs are being carried out. In a period characterized by recession, contraction of capital movements, and growing protectionism, the task of adjustment is that much harder. The Fund is not at the source of these evils, but it has to cope with members' individual problems in that environment. The Fund cannot assume the functions of a global anticyclical financial institution that meets the financing gaps created by adverse external conditions; that is not the Fund's mission and would not be consistent with the modalities of its financing and the limitations on its activities and resources. The same constraint

applies, of course, to the ambition that some may harbor for the Fund to assume not only the role of the world's anticyclical agency but also the responsibility for reducing poverty in the world.

My second observation is that, given the above constraints, the objective of Fund-supported adjustment programs is to help countries to regain balance of payments viability while optimizing the allocation of resources so as to pave the way for more growth in the medium run. All Directors have made that point in one way or another.

The manner in which the Fund tailors the adjustment programs can have a substantial effect on the methods by which the overall objectives are achieved. Too deep cuts or the wrong kind of cuts in investment may curtail future growth, as many Directors said. I would agree with Mr. Zecchini's point that the future level of output depends very much on the present structure of domestic absorption. Monetary policy, in spite of its limitations, can have an effect on increasing savings. Fiscal policy probably has a major role to play in increasing savings or decreasing public dissavings, both of which have a major impact on the formation of capital and the medium-term to long-term growth pattern in a country.

I was very interested to hear the persistent call for more supply measures, in particular to help countries set the right price relationships, which have such an important role in supply response. The call for closer collaboration with the World Bank in this field was one of the threads of the discussion that I wished to note. The real problem is to reconcile the need for short-term demand management policies with the opening up of productive opportunities in the medium term. The policies should be implemented at the very outset, but their effects are in most cases to be felt more in the medium term. There is enormous scope for research on all these topics. The discussion that we have had has revealed the need to heighten our understanding of the supply-side aspects of Fund programs, to improve further our collaboration with the World Bank, and to enhance the consistency of the activities of the two institutions, not through cross-conditionality but through complementarity, to use the breathing space provided by short-term adjustment to pursue longer-term growth objectives.

My third observation is that, of necessity, Fund programs have concentrated on countries that come to the Fund late in their economic difficulties and that in these circumstances have no other choice but to reduce--often drastically, because of the external constraints--their domestic absorption. Indeed, once they have exhausted their access to external financing, these countries have no other room for maneuver, and the general public

tends to judge Fund programs in that negative timing context. The more fundamental question is whether the real yardstick for assessing Fund policies is not to be found in countries that have applied the Fund's general economic policy prescriptions, thereby avoiding overindebtedness or mismanagement of their economies and, hence, the need to request use of Fund resources. Paradoxically perhaps, we should measure the effects of Fund assistance on growth by looking not at program countries, but at countries that have avoided programs because they have adjusted at an earlier stage of their difficulties. The association of Fund action with dramatic problem cases has, in my view, a methodological bias and a logical inconsistency.

My fourth, more personal point, because I have heard it in only one intervention, relates to the impact of adjustment policies on income distribution. It is difficult to conceive of an adjustment program that has no impact on income distribution. But programs are only one and often a modest factor affecting income distribution. Let us not forget that programs are applied to societies that have been shaped by years of policies or practices that have often led, long before the Fund even comes into the picture, to a very skewed pattern of income distribution. The marginal impact of a Fund-supported adjustment program on income distribution must be seen and evaluated in the context of the basic structure of incomes, which may be extremely imbalanced. However, we should not limit judgments on income distribution to that marginal impact, to the exclusion of the basic historical imbalances in income distribution, in evaluating the impact of an adjustment program.

In terms of the action to be taken following this seminar, first I have noted that a number of Directors would like us to do more work. Mr. Lundstrom in particular, followed by a number of other Directors, would like the staff to investigate whether there might be other effects on growth and/or on income distribution stemming not from the actual programs but rather from other conceivable types of adjustment programs that would still fit within the framework of the Fund.

The work preferably should be conducted on an individual country basis, although it will require an enormous amount of research. Clearly, there are limitations on how far we can follow up that line of inquiry, but we might try in some countries to carry the analysis a little farther. I would hesitate today to launch a vast new set of programs or projects in this field, but the discussion has provided sufficient guidance to the staff to test some of these ideas in a limited format.

The second call for action is to stress supply-side measures at an earlier stage of adjustment. I will ask the staff to put more emphasis on those aspects of Fund programs, in close conjunction with the World Bank. This is not new guidance, but the seminar has reinforced the thrust of concern in this area.

Third, the Board also agrees that although income distribution is a matter for governments to decide on, the Fund should be more ready, as Mr. Lundstrom in particular has said, at the request of a member--and I underscore those words--to provide whatever advice it can, without trying to be too ambitious, on alternative measures that may have different impacts on income distribution, provided that they do not have an adverse impact on the effectiveness or quality of the program itself.

None of this means that any basic change in Fund policies is required. We must continue to act in the framework of our constraints, but also the limits of our potential and within the guidelines that govern our lending policies.

With regard to publication of the various papers, I have noted that a few Directors have expressed reservations about publication of the paper on the global effects of adjustment programs and the paper on fiscal policy and the distribution of income. However, the weight of opinion was clearly in favor of publication, following suitable revision of the former paper and rather thorough revision of the latter paper to take into account the comments made by Executive Directors during the discussion as well as comments that individual Executive Directors might wish to provide bilaterally to the staff in the coming weeks. The revised texts would be resubmitted to the Board before publication. No revisions were suggested before publication of the survey paper of the empirical literature on the effects of Fund programs on economic growth.

LEO VAN HOUTVEN
Secretary