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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 90/69

3:00 p.m., April 30, 1990

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

Executive Directors	Alternate Executive Directors
G. K. Arora	L. E. N. Fernando
F. Cassell	C. Enoch
C. S. Clark	
	Zhang Z.
T. C. Dawson	
	J. Prader
E. T. El Kogali	
E. A. Evans	S.-W. Kwon
	R. J. Lombardo
L. Filardo	
R. Filosa	
M. Finaish	
M. Fogelholm	I. H. Thorláksson
M. R. Ghasimi	O. Kabbaj
G. Grosche	B. Goos
J. E. Ismael	T. Sirivedhin
A. Kafka	
J.-P. Landau	J.-F. Cirelli
	C. V. Santos
Y. A. Nimatallah	
G. A. Posthumus	G. P. J. Hogeweg
K. Yamazaki	S. Yoshikuni

L. Van Houtven, Secretary and Counsellor
K. S. Friedman, Assistant

Also Present

African Department: G. E. Gondwe, Deputy Director. Exchange and Trade Relations Department: L. A. Whittome, Counsellor and Director; T. Leddy, Deputy Director; G. R. Kincaid, C. Puckahtikom, M. Shadman-Valavi, B. S. Stuart. External Relations Department: E. Ray. IMF Institute: O. B. Makalou, N. A. Munla. Legal Department: F. Gianviti, General Counsel; W. E. Holder, Deputy General Counsel; R. H. Munzberg, Deputy General Counsel; P. L. Francotte, A. O. Liuksila. Research Department: P. Isard. Secretary's Department: C. Brachet, Deputy Secretary; J. W. Lang, Jr., Deputy Secretary; A. Tahari. Treasurer's Department: F. G. Laske, Treasurer; D. Williams, Deputy Treasurer; M. N. Bhuiyan, J. E. Blalock, W. L. Coats, D. Gupta, R. B. Hicks, C. P. McCoy, J. A. McLaughlin, G. Wittich. Western Hemisphere Department: K. Thugge. Office of the Managing Director: Internal Audit: R. Noë, Director; A. K. Sengupta, Special Advisor to the Managing Director; E. A. Milne. Personal Assistant to the Managing Director: B. P. A. Andrews. Advisors to Executive Directors: N. Adachi, M. B. Chatah, Z. Iqbal, J. M. Jones, K.-H. Kleine, B. S. Newman, D. Powell, P. Péterfalvy, F. A. Quirós. Assistants to Executive Directors: T. S. Allouba, B. A. Christiansen, E. C. Demaestri, S. K. Fayyad, S. Gurumurthi, M. Hepp, M. E. F. Jones, K. Kpetigo, C. Y. Legg, R. Marino, S. Rouai, D. Saha, J.-P. Schoder, Shao Z., J. C. Westerweel, Yang J.

1. INTERIM COMMITTEE - DOCUMENTATION

The Chairman commented that questions had recently been raised about the documentation for the coming meeting of the Interim Committee. It would be useful to have the Secretary briefly review that documentation.

The Secretary remarked that, for the item on the world economic outlook, the Interim Committee would have the Managing Director's usual note, which should be ready for circulation in the coming day or so as ICMS/Doc/90/3. For the debt strategy, the summing up of the Board's latest discussion on that subject had just been circulated as ICMS/Doc/90/9. As to the Ninth General Review of Quotas, the draft report of the Executive Directors and the proposed Resolution of the Board of Governors on increases in quotas would be available as ICMS/Doc/90/4. However, Mr. Dawson had recently circulated a memorandum drawing attention to the relationship between the quota increase and the proposed amendment on suspension. In that connection, it would be helpful to have Mr. Dawson's views on how to proceed with the documentation on quotas for the coming meeting of the Interim Committee.

With respect to the strengthened arrears strategy, the discussion would be based on ICMS/Doc/90/5, which would contain the Managing Director's statement on arrears at EBM/90/37 (3/16/90) and his statement at EBM/90/80, (4/27/90) on the use of the resources of the enhanced structural adjustment facility in connection with the rights approach; the staff paper on burden sharing (EBS/90/76, 4/20/90) would also be available, the Secretary added. It would remain to be seen whether, as a result of the forthcoming discussion at the present meeting on a gold pledge and extended burden sharing, documentation would need to be added to the other material for the Interim Committee item on the strengthened arrears strategy.

Mr. Dawson said that the simplest approach would be to include in brackets in the documentation on quotas appropriate language presenting the various alternatives that had been mentioned by Executive Directors.

The Chairman commented that the text that Mr. Dawson had described could be the subject of a brief discussion in the Board in the coming several days.

Mr. Yamazaki remarked that he continued to have strong reservations about proposals contained in the Managing Director's statement at EBM/90/80.

Mr. Grosche said that, if necessary, the documentation on the strengthened arrears strategy could include a note explaining that the documentation contained proposals that had not yet been approved by the Executive Board.

After a further brief discussion, the Executive Directors concluded their discussion on the documentation for the coming meeting of the Interim Committee.

2. EXTENDED BURDEN SHARING; AND ENHANCED STRUCTURAL ADJUSTMENT FACILITY - RIGHTS APPROACH

The Chairman recalled that at EBM/90/67 (4/27/90), the Executive Directors had agreed to consider a statement by the staff containing an outline of a possible decision on a gold pledge with respect to lending under the enhanced structural adjustment facility to finance the rights approach, as well as a staff paper summarizing possible options for extended burden sharing (EBS/90/81, Sup. 1; 4/30/90).

The Director of the Exchange and Trade Relations Department made the following statement:

> The following outlines how a gold pledge decision with respect to ESAF lending for rights could operate.
>
> 1. The Executive Board would decide as soon as possible to sell up to [3] million ounces of gold under certain procedures and conditions, which would be specified in the decision. Sales would be on the basis of market prices at the time of sale. This decision would require approval by an 85 percent majority of the total voting power and would authorize sales in accordance with the specified procedures and conditions.
>
> 2. The essence of the procedures and conditions specified in this decision would be as follows:
>
> a. The Executive Board would review the adequacy of the ESAF Trust Reserve Account every (say) six months.
>
> b. If the Board found that the amount held in the Reserve Account was insufficient to meet all Trust obligations to lenders falling due in the coming (say) six-month period, and the shortfall was attributable all or in part to cumulative non-payments of principal and interest on ESAF Trust loans extended under the rights approach (plus foregone investment earnings on these amounts not paid to the Trust on the due date), gold would be sold so as to generate profits equivalent to the amount of the shortfall so attributable.
>
> c. The Board could consider any alternatives that would effectively restore the resources of the Trust available for payments to lenders and thus forestall the need for these last resort sales; but absent such alternatives, gold would be sold.
>
> d. The cumulative amounts of such sales would be subject to the overall limit specified in the basic decision taken under paragraph 1.

e. The profits would be placed to the SDA and transferred to the Reserve Account.

3. The determinations by the Board required to implement the sales of gold under the conditions specified in the basic decision would be made by a majority of the votes cast. Alternatively, it could be provided that the Managing Director would make these determinations and report to the Board.

4. The basic decision authorizing sales would not be amended without the consent of all lenders to the Trust's Loan Account. Provision could be included to reduce the amount of gold authorized to be sold, also with the consent of all lenders to the Trust's Loan Account.

The Chairman invited Executive Directors to comment on the staff statement on a possible gold pledge before turning to the staff paper on extended burden sharing.

Mr. Dawson said that, at first glance, the proposed outline of a possible gold pledge was a positive response to his request to have a text that his authorities could carefully examine in the coming days. He wondered whether, under the provisions of the final paragraph of the staff statement, the consent of all the lenders would be needed to reduce the amount of the gold pledge in the period after the pledge had gone into effect. Presumably, while the lenders would of course be interested in the security of their loans, they would be willing to see the amount of the pledge be reduced in line with the actual demand for the resources involved.

Mr. Grosche commented that he agreed that, at first glance, the staff proposal was satisfactory. Of course, he would wish to review it carefully in the coming days.

Mr. Cassell said that he had no difficulty with the staff statement as it stood.

The General Counsel, responding to Mr. Dawson's question, explained that the intention was to establish a right for the creditors, and that the practice of the Fund had been that, once such rights were established, they could not be taken away without the creditors' consent. The staff proposal did not constitute a commitment to sell a particular amount of gold, but rather a commitment to sell gold in order to generate proceeds from the sale to discharge the Fund's liability to the creditors. It was not possible to know in advance what the sales price would be. If the price of gold were to fall dramatically, sale of the full 3 million ounces suggested in the staff proposal might well be necessary. The staff had thought it would be useful to avoid any discussion with creditors on the extent of their rights at a later stage. Of course, if creditors were willing to agree in advance to a unilateral reduction of the Fund's obligations, that would be a different matter.

Mr. Dawson commented that he had in mind the extent to which the amount of gold pledged would be a function of the actual number of arrears cases and the actual extent of the use of the rights approach by individual member countries. In that sense, it should perhaps be understood at the outset that if the number of countries availing themselves of the rights approach were to prove to be smaller than expected, then less gold than originally anticipated would have to be mobilized. It had been suggested in earlier staff papers that the potential use of the enhanced structural adjustment facility under the rights approach was about SDR 2 billion. If for some reason the amount of actual use were to be much smaller, there could be a case for reducing the amount of the gold pledge, independent of the price risk issue that was clearly a cause for concern for the creditors.

The General Counsel said that, in principle, it would be feasible to agree that, on the basis of an established ratio, the Fund would be authorized to reduce the gold sale commitment in proportion to the actual use of the rights approach.

Mr. Yamazaki commented that he wondered whether, under the staff proposal, the amount of gold to be sold could be increased if the price of gold were to fall.

The General Counsel replied that the amount of gold could not be so increased.

The Director of the Exchange and Trade Relations Department commented that, while it was true that the kind of ratio that the General Counsel had described could be established, it could conceivably create substantial inflexibility. The case of Guyana had shown how very difficult it was to look even a few months ahead in an effort to estimate the likely use of Fund resources under the strengthened arrears strategy. Establishing a ratio at the outset would mean that the Fund would be operating on the belief that it could foresee with precision the partition in three years' time between the use of the resources of the General Resources Account and the enhanced structural adjustment facility--something that was highly debatable.

The Chairman said that it could be agreed that if the Fund were to see at some time in the future that the amount of the gold pledge was providing an additional cushion that had not been foreseen, then there would be a clear case for reducing the pledged amount.

The Director of the Exchange and Trade Relations Department replied that the present staff proposal could be interpreted in the way that the Chairman had described.

Mr. Grosche said that the point about an established ratio that the Director of the Exchange and Trade Relations Department had just made was well taken. Nonetheless, he himself could agree to such a ratio, provided the initial one was sufficiently large.

Mr. Yamazaki inquired whether, under the staff proposal, it was assumed that the amount of gold sold would have to be increased in the event that the amount of reserves was less than expected.

The Director of the Exchange and Trade Relations Department responded that there would be no direct relationship between the size of the reserve and the amount of gold pledged.

Mr. Yamazaki remarked that changes in the price of gold were of course unpredictable and, as a result, the creditors could not be fully secured in advance. His authorities continued to attach importance to that security, and he wished to reserve his position on the staff proposal until his authorities had an opportunity to consider it more closely.

The Chairman remarked that, while it was true that changes in the price of gold were unpredictable, the amount of reserves was already significant. In addition, creditors could be assured by the far-reaching pledge to consider all the means available to the Fund, if necessary, in the event that the reserves should prove to be insufficient. Hence, in effect, the gold pledge under discussion was the third line of security that would be given to lenders.

Mr. Grosche commented that, while he greatly valued the general pledge that the Chairman had described, unfortunately it presented a risk for the creditors, as it would not be backed up in advance by the U.S. Congress.

The Chairman remarked that that risk certainly existed. Still, it seemed highly unlikely that the additional Fund resources would actually be needed or that the U.S. Congress would fail to take the steps required.

The Chairman then invited Executive Directors to comment on the staff paper on possible alternatives for extended burden sharing.

Mr. Dawson said that he continued to feel that SDR 1.5 billion would be a reasonable target for the amount of resources that was to be generated through extended burden sharing. However, the staff had noted that its presentation of the options was based on the assumption that half of charges from members with protracted arrears would be settled when they became due. In that connection, he wondered whether the staff assumed that each member concerned would pay about half of its charges as they fell due, or whether some of the countries would make full payment and others less than full payment, with one half representing the average for the whole group of countries in question.

The Chairman remarked that in preparing the table under discussion, the staff had tried to be as precise as possible in order to give Executive Directors a clear picture of the various risks and possibilities involved and to try to narrow the scope of uncertainty. In the actual application of the arrears strategy, the final outcome would probably not coincide precisely with the figures in the table.

The Treasurer added that in preparing the table the staff had experimented with optional assumptions concerning the charges to be paid by arrears countries during the period of the three years when the rights approach would be operational--namely, that all the charges would be paid, and that no charges would be paid. The staff had finally decided to employ a middle scenario, under which it was assumed that half the charges would be paid. Countries with Fund-monitored programs would be expected to pay all charges falling due. If the amount of charges actually paid were to vary from the assumption, then, of course, the outcome would differ from the estimates in the table. If the amount of charges paid were to exceed half the charges paid, then the adjustments to the rate of remuneration would be the same as shown in the table, but they would generate a larger amount of resources than was shown in the table, and the adjustments to the rate of charge might be a little smaller than was suggested in the table. Or it could be decided to adjust the rate of charge by the agreed amount and accumulate a larger amount for the SCA-2 than was shown in the table. If less than half of the charges falling due during the period of the rights approach were paid, then the amounts that could be generated for the SCA-2 would be smaller than was assumed in the table.

Mr. Kafka said that his position on extended burden sharing remained unchanged. No one could say in advance how much money would be needed. At present, the arrears amounted to SDR 3.3 billion and, in the absence of any action, that amount would increase by about SDR 500 million by the end of 1992. At the same time, there was no way of knowing at present precisely how many countries would decide to take advantage of the collaborative strategy or might be able to find some other way to eliminate their arrears. In those circumstances, the Fund should not try to take a decision at the present stage--before it knew how much money would be needed--on extended burden sharing. In that connection, the only clear fact was that any burden-sharing extension would weigh very heavily on the existing debtor countries. Therefore, the Board should postpone taking a decision on burden sharing until the first case actually came up; at that stage, there would be more information on the relevant factors in a decision on extended burden sharing.

The Chairman commented that presumably the membership would like to have in advance a reasonably precise idea of the steps that the Fund would take if the problem addressed by the proposed extended burden sharing were actually to materialize. Hence, it would be difficult to delay adopting a decision. At the same time, it would be reasonable to agree to review periodically, and adjust as necessary, any scheme that was approved at the present stage.

Mr. Dawson remarked that Mr. Kafka seemed to be suggesting that burden sharing should not be established until the need to use the rights approach actually arose. However, it would clearly be prudent to start now to accumulate precautionary balances for the purpose of financing a rights program later on. As the Chairman had suggested, the Board could decide at any future time, in the light of the actual demand, to reduce the amount of the balances that was thought to be needed.

Mr. Kafka considered that it would be best to see the extent of the availablity of the Fund's resources in comparison with the actual demand for them. That assessment could not be made for a while yet.

Mr. Dawson remarked that, unlike a gold sale and a quota increase, extended burden sharing would lead to an accumulation of resources over time, rather than to a sudden increase in resources. If extended burden sharing was not implemented soon, there was likely to develop eventually a mismatch between the resources accumulated under burden sharing and the financing required under the rights program.

Mr. Kafka remarked that the Fund already had sizable resources, inlcuding SDR 4 billion for the enhanced structural adjustment facility and SDR 1.6 billion in Special Contingent Account No. 1, compared with SDR 3.3 billion in arrears at present, which could rise to SDR 3.8 billion in the coming two years. Hence, there seemed to be no need to take a decision forthwith on extended burden sharing.

Mr. Grosche commented that, given the hope that a number of countries would take advantage of the rights approach, and since the access to the resources under the enhanced structural adjustment facility obviously was not sufficient to accommodate the financing of the rights approach, it would be wise to start now to accumulate resources for that particular purpose. And the earlier a start was made, the easier it would be in terms of the increase in the rate of charge paid by debtors and the loss of remuneration paid to creditors. Hence, he agreed with Mr. Dawson that it would be prudent to start at the present stage to accumulate what he hoped would have to be only a relatively small amount of resources instead of waiting until some time in the future, when the rate of charge might have to be suddenly increased by a number of basis points while the rate of remuneration was reduced all the way down to 80 percent. No one knew how interest rates would behave in the coming period; while there was widespread hope that the rates would fall, there was of course no certainty that they would.

The table under discussion would be very helpful in guiding the coming discussion by the Ministers, Mr. Grosche said. The table was admittedly based on several assumptions that might or might not prove to be accurate, but the main topic of the present discussion in the Board should be to ensure that the assumptions could be made, and options presented, in a reasonable manner. In that sense, the table was already very useful.

Mr. Landau said that he agreed with Mr. Kafka that, in assessing the need for resources to finance the rights approach, the Executive Directors should always bear in mind the fact that none of the Fund's resources, including quota resources, should be excluded.

Mrs. Filardo commented that she agreed with Mr. Kafka that the hope was that some of the arrears could be eliminated during the period up to, and in which, the rights approach would be available. Hence, there was no way of knowing at present the amount of resources that would be needed later to finance the rights approach. It would not be wise to establish the burden-sharing mechanism at present, as that would place an excessive burden on the debtor countries. Extending burden sharing should not be seen as one of the alternative means of solving the arrears problem.

The Chairman remarked that if cooperative efforts succeeded in reducing the number of arrears countries, the contribution of burden sharing could be limited to a strict minimum.

Mr. Cassell commented that that it was not easy to clearly interpret the table under discussion. It would be helpful to know what the relevant figures would be on the assumption that no charges would be paid in the period covered by the table. That scenario presumably would include the possibility of compulsory withdrawals by some of the members concerned and should give a good idea of the outside limits on the burden-sharing options. Conceivably the Fund could find that it suddenly faced the need to finance the rights approach for a large member at a time when the Fund did not have sufficient resources to do so--or could not raise the resources in an acceptable fashion. He fully agreed that the Fund should start forthwith to accumulate the resources that could be used later to finance the rights approach, but it would be useful to know more about the sensitivity of the figures in the table to changes in selected factors. Obviously it was important to feel comfortable that there would be sufficient reserves to meet the worst-case scenario. The present table gave the impression that the amount of reserves to be accumulated was merely a residual; in fact, the Board should decide first how large prudentially the reserves should be and then take a view on what the rate of charge should be.

Mr. Filosa said that the Board should not wait to take a decision on extended burden sharing until it had more information, as Mr. Kafka had suggested. Even if the Board knew later--in say, the spring of 1991--how many countries intended to use the rights approach, the precise amount of resources needed to finance the approach would not be known, as adjustment programs supported by the Fund in that period could conceivably go off track. If the Fund did not start extending burden sharing soon, it would run the risk of not having sufficient resources to finance the rights approach when the need for such financing actually arose some time in the future.

Mr. Arora said that it would be useful to know what would happen to the rate of charge if the contribution ratio was 2:1 and the amount generated over five years was SDR 1 billion or SDR 0.75 million. As he had stated on previous occasions, any further extension of burden sharing was a cause for concern. In his view, the Board needed to discuss the very basis of the system of burden sharing in order to adjust it so that all member countries would participate--an objective shared by a fairly large number of Directors. It would not be appropriate to take a position on the options outlined by the staff until the Board had conducted the basic review of burden sharing that he had described.

It was important for the Fund to be prudent and to plan to have enough resources available to finance the rights approach, but the amount of reserves available was already significant, Mr. Arora continued. The SDR 2.2 billion in resources available under the enhanced structural adjustment facility could be seen as a kind of measure of the amount that would have to be guaranteed for creditors. At the present stage, there was no reason to assume that the guarantee would have to cover a larger amount partly in view of the general assurance that the Chairman had described with respect to the availability of the Fund's resources to reassure creditors. In addition, the risk to creditors would be limited because the borrowing members concerned would have to implement a Fund-supported program. Later, when more information was available, developing countries would certainly be willing to step forward to participate in some form of extended burden sharing, including, perhaps, a quota-based system, if any such system were thought to be necessary; there was at present no question of the willingness of those countries to participate at the appropriate stage should the need to do so arise. For the moment, it was clearly best not to burden developing countries forthwith with the cost of increased charges on the use of Fund resources; many of them were poor countries that had already undertaken to implement programs supported by the enhanced structural adjustment facility.

Mr. Posthumus commented that he, too, was worried about the increase in charges that would result from extended burden sharing, but it would not be wise to postpone a decision until more information on the likely use of the rights approach was available. One year previously the Board had postponed a decision to increase reserves, and the Board now faced a problem with respect to the amount of available resources. At the same time, the staff paper and summary table contained what was perhaps an excessively large number of options; it might be preferable to agree, on the basis of a formula, on the amount of resources that should be accumulated over time. Finally, it would be helpful to restructure the table to make the presentation of the options more straightforward.

The Chairman commented that, in order to reduce the number of options, the Board could agree to aim to accumulate a specific amount of resources--say, SDR 1 billion or SDR 1.25 billion--and center the proposed system on that goal. It could also approve a review clause that would, with reasonable automaticity, allow the Board either to increase the prudential accumulation of resources, if necessary, or to reduce the amount to be accumulated, if it were found to be larger than necessary.

After a further brief discussion, the Chairman said that, for the next stage in the discussion, the staff could provide a somewhat different table, based on an accumulation of SDR 1 billion over five years, with the contribution ratios on the verticle axis and the adjustments in the rates of charge and remuneration on the horizontal axis. The Board could agree at the outset that the decision on extended burden sharing would be reviewed, in the light of future developments, particularly the evolution of the SDR interest rate, the effects of which could be highlighted in the next version of the table presenting the various optional solutions.

Mr. Zhang said that his position on extended burden sharing remained unchanged. The present rate of charge was already very high. In addition, he agreed with Mr. Kafka that the Board did not yet know how much resources would be needed to finance the rights approach. Hence, there was no need to take a decision on the extension of burden sharing at the present stage.

Mr. Clark remarked that he agreed with the Chairman's suggestion of a simplified table that would, in particular, show the sensitivity of the extended burden-sharing mechanism to the evolution of the SDR interest rate.

Mr. Dawson said that he continued to prefer to aim to accumulate SDR 1.5 billion. The Chairman's suggestion seemed to provide for a fairly small amount--SDR 1 billion--over a fairly long period, five years. He wondered whether the system that the Chairman had described would not be overdetermined--in terms of the resources raised and the contributions made by creditors--if the rate of remuneration were adjusted immediately to 80 percent of the SDR interest rate.

Mr. Enoch commented that he agreed with Mr. Dawson that the system that was under discussion might well be overdetermined. Creditors would not wish to see sizable asymmetry in the system, and it might be necessary to move to the 80 percent floor only gradually, or to agree to accumulate more than SDR 1 billion, or to maintain the system over a period of something less than five years.

After a further brief discussion, the Treasurer noted that if the rate of remuneration were reduced to 80 percent of the SDR interest rate and the contribution ratio were 1:1, the amount accumulated over five years would be SDR 1.9 billion; with a ratio of 2:1, the amount would be SDR 1.4 billion; with a ratio of 3:1, the amount would be SDR 1.3 billion. If the ratio were 1:1 and there was an annual accumulation of SDR 200 million to reach

SDR 1 billion over five years, the adjustment of the rate of charge would be 70 basis points and the remuneration coefficient would be 86.4 percent; with a ratio of 2:1, the adjustment of the rate of charge would be 47 basis points and the remuneration coefficient would be 84.1; with a ratio of 3:1, the adjustment of the rate of charge would be 35 basis points and the remuneration coefficient would be 82.9 percent.

Mr. Fogelholm remarked that his authorities were willing to go along with the floor for the remuneration rate of 80 percent of the SDR rate, provided that the burden sharing was symmetrical. If the amount to be accumulated was not more than SDR 1 billion over five years, then there probably would be no need to reduce the rate of remuneration to as low as 80 percent, and it would be helpful to have in the next table figures showing that possible outcome.

Mr. Grosche commented that the Executive Directors seemed to have made significant progress in moving toward a solution through their willingness to consider a new table of options based on the accumulation of a specific amount--SDR 1 billion--over a certain period, namely, five years. The only remaining factors on which agreement was needed were the ratio of contributions and the resultant rate of remuneration. Such a table would be relatively easy for the Ministers to consider at their coming meeting.

Mr. Nimatallah commented that the amount suggested by the Chairman--SDR 1 billion--seemed reasonable; it could be accumulated over five years, or even four years. The remaining difficult unresolved issue was the ratio of contributions--he preferred to propose 2:1 and 3:1--and it could be left for the Ministers to deal with.

Mr. Ghasimi said that he appreciated the Chairman's efforts to create a consensus, and he recognized the sensitivity and importance of the extended burden-sharing issue. However, his views had not changed, and he was therefore not in a position to support extended burden sharing.

Mr. Santos remarked that his position was the same as that of Mr. Ghasimi.

Mr. Posthumus said that he hoped that Executive Directors who were opposed to extended burden sharing would pay due regard to the willingness of the so-called creditor countries to accept a decline in the rate of remuneration to 80 percent of the SDR interest rate.

The Chairman commented that, as Mr. Posthumus had implied, the creditor countries had made a major effort in agreeing to see the rate of remuneration fall to 80 percent of the SDR interest rate. Of course, the contribution that the debtor countries were being asked to make was sizable, particularly as a number of them were poor countries. However, the contribution that the creditor countries were willing to make was clearly significant. He strongly hoped that the Executive Directors would be able to agree on a system of extended burden sharing before the coming meeting of the Interim Committee.

Mr. Clark said that he agreed that the system summarized in the staff's table was likely to prove to be overdetermined. As Mr. Posthumus had suggested, in order to facilitate the discussion at the coming meeting of Ministers, the table should be simplified by emphasizing the amount to be accumulated, the period of accumulation, and the remuneration rate. It would be particularly important to show the effects on the various factors of changes in interest rates.

The Treasurer said that, assuming that the amount accumulated would be SDR 1 billion, the period would be four years, the SDR interest rate would be 9 percent, and half the charges falling due during the period of the rights approach would be paid, then, at a ratio of 1:1 between creditors and debtors, the rate of remuneration would be reduced to 84.7 percent and the upward adjustment to the rate of charge would be 88 basis points; at a ratio of 2:1, the rate of remuneration would be reduced to 81.7 percent and the rate of charge would be adjusted upward by 59 basis points; and at a ratio of 3:1, the rate of remuneration would be reduced to 80.2 percent and the adjustment to charges would be 44 basis points.

Mr. Grosche considered that the Board should agree at the present stage on the period for the accumulation under the extended burden sharing. In the light of the increase in the rate of charge required with a period of four years, he was willing to accept a period of five years.

Mr. Posthumus said that he preferred to accumulate an amount in excess of SDR 1 billion.

Mr. Enoch considered that the presentation to the Ministers should be simplified. He was willing to accept a period of five years, provided that the extended burden-sharing decision would be reviewed regularly. It seemed unlikely that the 80 percent floor for the rate of remuneration would be reached quickly; the rate of remuneration was likely to be several points above the floor for a while.

Mr. Prader said that his position was similar to that of Mr. Grosche. As Mr. Kafka had remarked, additional information relevant to the extended burden-sharing mechanism would not be available for some time; meanwhile, it would be helpful to have some margin for maneuver under the mechanism, and that could be given through the rate of remuneration. In any event, none of the creditors seemed willing to see the contribution ratio be as high as 3:1; a ratio of 2:1 appeared to be the maximum acceptable.

Mr. Grosche commented that the Directors seemed to be making significant progress toward reaching a consensus. He could accept a period of five years, an amount of SDR 1 billion, and a reduction, if necessary, in the rate of remuneration to 80 percent of the SDR interest rate. The main unresolved issue was whether the system should be asymmetrical and, if so, to what extent.

Mr. Dawson remarked that, while he continued to prefer a larger amount than the Chairman had proposed, he was willing to ask his authorities to consider SDR 1 billion.

Mr. Evans said that the general assumption seemed to be that an agreement extending burden sharing would have to be approved at the coming meeting of the Ministers. He wondered whether it was thought that extended burden sharing was an essential part of the overall strengthened arrears strategy.

Mr. Grosche stated that there was a clear need for more resources in the General Resources Account, in addition to the proposed quota increase. For example, it might prove necessary to expel one or two countries from the Fund's membership, which would require a reduction in the Fund's reserves, which would in turn substantially affect the Fund's precautionary balances. The resources of the enhanced structural adjustment facility alone would not be sufficient to finance the rights approach. Hence, there was a clear need to accumulate resources in SCA-2. That action was necessary in the context of the Fund's overall strategy for dealing with the arrears problem.

The Chairman remarked that he was confident that the Ministers would be willing to accept the extended burden-sharing mechanism if they felt assured that it would be reviewed after a year, with a view to ensuring that it remained equitable.

Mr. Evans said that he understood the argument in favor of accumulating additional resources. But that argument was not strong enough to convince everyone that burden sharing should be extended.

Mr. Dawson considered that a rights approach supported by resources of the enhanced structural adjustment facility would not be viable without extended burden sharing. As Mr. Grosche had said, there was a general need for prudential reserves, a view that Mr. Posthumus apparently agreed with. An effort was being made to develop an enhanced arrears strategy that combined "carrots" and "sticks." Without the rights approach, the arrears strategy would lack the necessary "carrot" to complement the suspension and other elements of the overall approach. Without extended burden sharing and the rights approach, the Fund would be forced to face rather earlier than it would have wished the question of expelling members from the Fund. Extended burden sharing was part of a last-attempt effort to make the collaborative approach work. The alternative would be a much tougher approach, under which the Fund would ultimately be protected in a sense because it would continue to have gold resources, if necessary, or other methods of raising reserves. Burden sharing was a very important part of the effort to develop an arrears strategy that could help member countries to eliminate their arrears. The alternative would be an approach that was essentially punitive--an outcome that no one would welcome.

Mr. Landau said that he was willing to see the rate of remuneration fall to 80 percent of the SDR interest rate as a part of extended burden sharing. Earlier in the debate on extended burden sharing, there had been movement toward a system based on quotas. It would be useful to have further information on the results of a system based on a contribution ratio providing for equivalency between debtors and creditors; the calculation could be based on the total quota shares of debtor and creditor countries.

Mr. Arora commented that everyone seemed to agree on the need to build up the precautionary balances; the only issues were the amounts that should be accumulated at the present stage and the modality of the accumulation. He certainly hoped that no member country would have to be expelled, but even if no expulsions were necessary, additional resources would still be needed to finance the rights approach, although there was no need for a rigid agreement under which there must be full backup for all the general resources used to support rights encashment. The rate of charge paid by debtor members was already very high and would be raised significantly under any of the proposals being discussed, which would place a heavy burden on those countries.

Mr. Evans commented that, given the uncertainties involved, there was of course an understandable reluctance to agree forthwith on a system that, although subject to review, would be in place for several years. Moreover, there was still not full acceptance that such a system was really necessary. Hence, the proposed review was very important, as was the question of what would be subject to review. In the circumstances, it was best to start with a system that was on the modest side; in that connection, SDR 1 billion seemed likely to prove to be adequate and, hence, on the modest side, while a period of five years might turn out to be more than enough. Accordingly, the Executive Board should be able to agree on a system based on SDR 1 billion over five years, provided that there was a review in, say, one year, when it might be possible to shed more light on the amount of resources that would actually be required. The review should also encompass the allocation of the burden shared between creditors and debtors at that stage. Interest rate movements were likely to continue to place a particularly large burden on debtor countries in the coming period, and the creditors should be prepared to look at contribution ratios beyond 3:1--at least 4:1. A ratio of 1:1 should be included in the next table only as a reference point for the Ministers, not as point for negotiation.

Mr. Dawson said that the suggestion for reviewing the system after a year was certainly a good one. At that time, the Board should have a clearer idea of the likely extent of the use of the rights approach and the associated demand for resources. It was important to begin accumulating those resources forthwith, rather than wait for several years, as Mr. Kafka had suggested, when the need to finance encashed rights actually arose. The alternative was either to have a mismatch and continue to burden share after the money was lent, which would not be prudent, or to accumulate the money over a very short period, after members made known their intention to use the rights approach, which would place an even larger burden on creditors and debtors alike.

Mr. Kafka noted that, under the proposed system, rights would be encashed approximately three years after a country had undertaken a monitored program. That arrangement seemed naturally to suggest that the right time to take a decision on extended burden sharing would be after the accumulation of monitored programs, should it be evident that there would be difficulty in providing sufficient financing from accumulated reserves and the enhanced structural adjustment facility. That arrangement should leave enough time in which to accumulate the resources that might be necessary to finance the rights approach.

After a further brief discussion, the Chairman proposed that the Executive Directors continue their discussion on extended burden sharing--as well as a gold pledge--on May 2, 1990. For the discussion on extended burden sharing, the staff would prepare a new table based on a period of five years and an accumulation of resources of SDR 1 billion.

The Executive Directors accepted the Chairman's proposal and concluded for the time being their discussion on a gold pledge and extended burden sharing.

APPROVED: February 25, 1991

LEO VAN HOUTVEN
Secretary