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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 89/25

10:00 a.m., March 1, 1989

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

Executive Directors	Alternate Executive Directors
	C. Enoch
	C. J. Jarvis, Temporary
Dai Q.	Zhang Z.
	D. C. Templeman, Temporary
	A. Rieffel, Temporary
	J. Prader
	A. Y. El Mahdi, Temporary
	M. Hepp, Temporary
	E. Ayales, Temporary
	N. Kyriazidis
M. Finaish	A. M. Othman
	O. Kabbaj
G. Grosche	
J. E. Ismael	E. Kiriwat
	L. E. N. Fernando
A. Kafka	L. M. Piantini, Temporary
	D. McCormack
	W. N. Engert, Temporary
Mawakani Samba	
	I. A. Al-Assaf
J. Ovi	M. Fogelholm
H. Ploix	
G. A. Posthumus	G. P. J. Hogeweg
	C. Y. Legg, Temporary
	M. J. Shaffrey, Temporary
K. Yamazaki	N. Adachi, Temporary

L. Van Houtven, Secretary and Counsellor
M. J. Miller, Assistant

Also Present

IBRD: L. E. Derbez, Latin America and the Caribbean Regional Office. Asian Department: H. Neiss, Deputy Director; B. B. Aghevli, Y.-W. Chin, R. Hemming, J. S. Kakonen, T. Krueger, S. M. Schadler, D. A. Scott. Exchange and Trade Relations Department: J. T. Boorman, Deputy Director; A. Basu, E. Brau, R. G. Kincaid, S. Kanesa-Thasan. Legal Department: P. L. Francotte, A. O. Liuksila, J. W. Head. Middle Eastern Department: P. Chabrier, Deputy Director; S. H. Hitti, M. D. Knight, C. A. Yandle, M. Yaqub. Secretary's Department: C. Brachet, Deputy Secretary; J. W. Lang, Deputy Secretary; A. P. Bhagwat. Treasurer's Department: J. E. Blalock, S. J. Fennell, P. S. Ross. Western Hemisphere Department: S. T. Beza, Director; J. Ferrán, Deputy Director; J.-P. Amselle, J. Berengaut, R. A. Elson, S. Kawar, C. S. Lee, A. S. Linde, E. Sumar, S. J. Stephens, J. Thornton. Office of the Managing Director: P. Shome. Personal Assistant to the Managing Director: H. G. O. Simpson. Advisors to Executive Directors: M. B. Chatah, P. O. Montórfano, P. D. Péroz, M. Pétursson, G. Pineau, S. P. Shrestha, R. Wenzel, J. E. Zeas. Assistants to Executive Directors: S. K. Fayyad, S. Guribye, M. E. Hansen, C. L. Haynes, J. Heywood, Hon C.-W., P. Kapetanovic, R. Marino, T. Morita, C. Schioppa, Shao Z., C. C. A. van den Berg.

1. MESSAGE OF CONDOLENCE

The Managing Director made the following statement:

Before turning to our agenda, I would like to take a moment to say a few words about Mr. Dannemann; I know that Directors have all learned with great sadness of his recent untimely death.

Mr. Dannemann had a distinguished career, first with the Bundesbank, and since 1969 with the International Monetary Fund, where for a period of more than ten years he was Director of the Fund's Bureau of Statistics.

Mr. Dannemann was an outstanding economist and statistician. We will particularly remember him for his substantial contributions in the management of the Fund's data base, statistical publications and methodologies, and also technical assistance in statistics, all of which continue to play such an important role in ensuring the effectiveness of the Fund's work with member countries.

We will recall with fondness his fine personal qualities as senior manager of a large department and as an individual, and for his continuing concern for the needs of the staff at all levels.

At the memorial service for Mr. Dannemann, Mr. Erb offered a eulogy on behalf of all his many friends in the institution, which I hope has been of comfort to his family, to whom we wish to state again the great respect and esteem in which he has been held by all in the Fund. I am certain that the Executive Board will wish to join management in expressing these sentiments to his family.

2. REPORT BY MANAGING DIRECTOR

The Chairman noted that he had traveled to Japan to attend the funeral of Emperor Hirohito. He had had the opportunity, while in Tokyo, to speak at some length with the Minister of Finance, Mr. Murayama, and had dined with the Governor of the Bank of Japan, Mr. Sumita. He had also met a number of heads of state and representatives of several international organizations.

President Suharto of Indonesia, President Mubarak of Egypt, Prime Minister Bhutto of Pakistan, and President Daniel Arap Moi of Kenya had all requested meetings with him while he was in Tokyo. He had met, more informally, President Mobutu of Zaïre, President Mitterand of France, President Ershad of Bangladesh, and Mr. Masao Fujioka, President of the Asian Development Bank. He had also discussed the topic of structural

policies with the Secretary-General of the Organization for Economic Cooperation and Development (OECD), Mr. Jean-Claude Paye. He had met with Mr. Dunkel, Director-General of the Secretariat of the General Agreement on Tariffs and Trade (GATT), and with Mr. Frans Andriessen, Vice-President of the Commission of the European Communities.

He was grateful to his Japanese hosts and especially to Mr. Yamazaki, who had traveled with him, for making those meetings possible, the Chairman concluded.

Mr. Yamazaki said that he wished to thank the Chairman for traveling such a long distance to attend the funeral of the late Emperor. He also wished to thank his colleagues for making it possible for the Chairman to attend, in spite of his busy schedule.

The Chairman remarked that he had taken the occasion of the flight back from Tokyo to confer with the President of the World Bank about Bank-Fund collaboration. Directors might have seen a report in the New York Times about the supposed conflicts that had arisen between the Fund and the Bank. In fact, he and Mr. Conable had been in close touch over the previous few weeks, in an effort to ensure that the procedures for collaboration between the two institutions were strengthened, and that the perception of conflict was avoided. He would apprise the Board of the conclusions he and Mr. Conable had come to in that respect shortly, for which he trusted he would receive the Board's support.

3. VENEZUELA - REPORT BY STAFF

The Director of the Western Hemisphere Department reported that late on the preceding day the staff had completed most of the work on Venezuela's economic policy memorandum, which Executive Directors would be receiving later in the day. The cover letter to that memorandum indicated that the authorities saw the memorandum as the beginning of a process of involvement with the Fund in an extended arrangement, perhaps to be preceded by a stand-by arrangement. As an initial step, the authorities were requesting a first credit tranche purchase. The staff would be preparing papers for that purchase, which would be brought to the Board possibly in early April.

The staff would be having further discussions with the authorities to develop another arrangement with the Fund, the Director concluded. The document that Directors would be receiving later in the day described some of the policy measures to be taken in the medium term. The staff would continue working on those measures with the authorities in the coming weeks, also taking into account the work that the World Bank was currently conducting with the Venezuelan authorities.

4. VIET NAM - OVERDUE FINANCIAL OBLIGATIONS - REVIEW FOLLOWING DECLARATION OF INELIGIBILITY - POSTPONEMENT

Without discussion, Directors took the following decision:

Paragraph 4 of Executive Board Decision No. 9037-(88/175), adopted December 7, 1988, shall be further amended by substituting "on March 16, 1989" for "within three months from the date of this decision."

Decision No. 9097-(89/25), adopted March 1, 1989

5. HONDURAS - OVERDUE FINANCIAL OBLIGATIONS - REPORT AND COMPLAINT UNDER RULE K-1, AND NOTICE OF FAILURE TO SETTLE TRUST FUND OBLIGATIONS

The Executive Directors gave substantive consideration to the Managing Director's report and complaint under Rule K-1 relating to Honduras' overdue financial obligations to the Fund, and the notice of Honduras' failure to settle Trust Fund obligations (EBS/89/12, 1/30/89; and Sup. 1, 2/24/89).

The staff representative from the Western Hemisphere Department said that a staff mission had returned from Tegucigalpa over the preceding weekend. The mission had held discussions with the authorities on the settlement of the arrears and on a policy package to improve the country's economic and financial situation. The authorities were aware that delays in implementation of the adjustment measures would increase the cost of adjustment. They were thus open to discussing adjustment measures, particularly in the fiscal area, and also modifications in the exchange rate system.

However, the staff representative went on, the authorities were requesting a few more days' time, in part because the President of the country had returned from official business abroad only over the previous weekend. On Monday and Tuesday of the current week, there was to be a meeting of members of the Government's economic team, in which he would be involved. The Honduran authorities might request that a mission return to Honduras to finalize discussions on the use of Fund resources under a stand-by arrangement if Honduras' arrears to the Fund were settled by that time.

With respect to the outlook for the clearance of Honduras' arrears to the Fund, the staff representative continued, the reserve position was quite weak, in part because of the wide spread between the official and parallel market exchange rates, so that the central bank was having difficulties in purchasing foreign exchange at the official rate from exporters. The authorities understood that substantial additional financial assistance would be forthcoming only if an appropriate policy package was introduced and implemented within the next few days or weeks. The

authorities had indicated that they would try to settle the arrears to the Fund as soon as possible, in the context of a discussion on the policy package.

The staff had found that the authorities had a positive attitude toward taking the difficult decisions that would be needed to implement the adjustment measures, the staff representative concluded. However, more time was needed to consider the extent of those decisions, and the timing of the implementation of the associated measures.

Mr. Ayales said that the Honduran authorities believed that it was necessary to view the current arrears situation in the context of the country's efforts to cope with the extremely difficult financial situation of the previous few years. Honduras had made important payments to the Fund--over SDR 110 million--despite adverse external circumstances over that period, such as the severe deterioration in the terms of trade and the sharp reduction in official transfers and disbursements of official capital. The ratio of use of Fund credit to Honduras' quota had thus fallen from 180 percent in early 1986 to about 35 percent currently. Also, although Honduras had fallen into arrears with the Fund in February and September of 1988, it had become current as soon as the availability of foreign exchange had permitted. In fact, over 50 percent of the current arrears had fallen due during February 1989.

The authorities wished to reiterate their intention to settle fully the arrears as soon as the central bank's foreign exchange situation permitted it, Mr. Ayales concluded. Furthermore, in the light of the staff's past visit to Tegucigalpa, they wished to continue discussing the use of Fund resources to support their economic program, and had already requested that a staff mission visit Honduras as soon as possible. He wished the decision to refer to the recent contacts that had taken place between the staff and the authorities.

Mr. Rieffel made the following statement:

> My authorities are deeply concerned about the emergence of new arrears to the Fund, after the disconcerting episode of arrears that occurred last year.
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> My authorities agreed last September, on an exceptional basis, to support in the World Bank Board a structural adjustment loan to Honduras despite the existence of outstanding arrears to the Fund. They agreed to do so on the understanding that the Fund arrears would be cleared within a short period of time, and that the Honduran authorities would adopt economic reforms needed to maintain the confidence of external creditors and donors.
>
> My authorities were doubly disappointed. While Honduras cleared its arrears on November 9, new arrears to the Fund emerged within a week, and no payments have been made since

then. Furthermore, arrears to the World Bank have emerged, triggering the suspension of Bank disbursements, and delaying the disbursement of related cofinancing. At the same time, Honduras has not responded meaningfully to proposals from the Fund staff for the formulation and implementation of a comprehensive adjustment program.

From my perspective, the course of action that offers the best chance for Honduras to avoid arrears problems with the Fund and the Bank in the future is the adoption of an adjustment program that can be supported by a Fund stand-by arrangement. My authorities urge Honduras to act quickly to adopt such a program before their room for maneuver is further circumscribed, and before financing arrangements in support of such a program become substantially more complicated. In particular, we urge Honduras to eliminate its arrears to the Fund before the April meeting of the Interim Committee, in which progress in overcoming the problem of arrears to the Fund will be assessed. In the absence of a clear commitment by Honduras to sustainable, growth-oriented policies, multilateral and bilateral donors are likely to find it increasingly difficult to justify the amounts and forms of external financing they have provided in the past.

Finally, my authorities regard this case as a measure of the ability of the Fund and the Bank to collaborate in promoting growth and adjustment in member countries, and in mutually reinforcing their status as preferred creditors. In this connection, we would appreciate hearing the views of the Bank on current economic policies in Honduras, and Honduras' prospects for the remainder of 1989.

Mrs. Hepp stated that she regretted that Honduras had been unable to settle its overdue obligations to the Fund, and that arrears had re-emerged at the end of 1988. However, she also noted that the mission had held negotiations with the Honduran authorities on an economic program to be implemented by Honduras in the context of the discussion on the settlement of Fund arrears. She welcomed Mr. Ayales's indications that considerable progress had already been made in the negotiations, and hoped that they could be completed and an economic program adopted soon. She was certain that such a program would permit the clearance of the outstanding arrears to the Fund. She supported the proposed decision, as well as the amendment to it that had been requested by Mr. Ayales, adding a sentence welcoming the progress that had already been made in the negotiations.

Mr. Enoch stated that he was not very much reassured by the staff's report of its recent discussions with the Honduran authorities. Much of it seemed very familiar. The Board had had similar discussions about Honduras' arrears in February, May, and September 1988. On September 15, 1988, the World Bank had approved a structural adjustment loan to Honduras

on the premise that arrears to the Fund, which were then still outstanding, would be cleared by the end of October. In the event, it was November before the arrears were cleared--just in time to avert yet another arrears discussion in the Board. As Mr. Rieffel had pointed out, Honduras was in arrears to the Fund again almost immediately. Since then, Honduras had fallen yet again into arrears with the Fund and the World Bank.

Such continual falling into arrears raised questions about the ability of the authorities to make repurchases, Mr. Enoch concluded. For that reason, the Board would need to think very carefully before considering a Fund-supported program for Honduras. The Board would also need to see a number of prior actions from the authorities to demonstrate their commitment to the adjustment process. The first requirement was undoubtedly a prompt settlement of all outstanding arrears to the Fund.

Mr. Grosche said that he was deeply disappointed about the failure of Honduras to honor its obligations to the Fund. He fully agreed with previous speakers that a sound program of adjustment was of the essence, and he shared Mr. Enoch's concern about the continuous postponement of measures and the re-emergence of arrears. The Board would certainly need to see some prior actions taken, along with clearance of arrears as soon as possible, before it could be assured that drawings by Honduras on the Fund's resources would be justified.

Mr. Adachi said that he shared the views of previous speakers. He too was deeply concerned by Honduras' arrears to the Fund, especially since Honduras was a case of a country that had experienced chronic arrears. There was clearly only one action that was open to Honduras at present--beginning to implement an appropriate program of economic adjustment. His authorities would be ready to support Honduras' adjustment efforts once the country had cleared its arrears to the Fund and the Bank, and had adopted an appropriate economic package. Like Mr. Rieffel, he wished to stress the importance of close collaboration between the Fund and the Bank in addressing the problem of Honduras' arrears to both institutions.

The Chairman commented that Honduras was indeed an example of a case in which collaboration between the Fund and the Bank would be essential.

Mr. Legg commented that it was increasingly difficult to think of new things to say in arrears cases. Like every other speaker, his authorities were very disappointed that Honduras was once again in arrears to the Fund.

The Board would recall that extraordinary efforts had been made in 1988 by other Fund members to assist Honduras in clearing its arrears, Mr. Legg went on. It was therefore especially frustrating that the authorities had allowed the situation to deteriorate again so quickly. Mr. Rieffel had referred to the lessons in the Honduran case that his chair saw for Bank-Fund collaboration, with which he concurred. There

was perhaps another lesson for the implementation of the collaborative approach: the need to ensure that the basis was laid for a sustainable solution. That did not mean that the Board should move slowly, but that it should avoid any unseemly haste when its own actions were not matched by real progress on the policy front on the part of the country. With that thought in mind, Mr. Rye had cautioned against focusing too much on the semblance of cooperation, rather than the substance of performance and adjustment. Although in the case of Honduras the amount involved was not large, the forthcoming obligations were of sufficient significance to again pose a problem to the Honduran economy if they were allowed to accumulate. In passing, he wondered whether the case of Honduras was perhaps one in which penalty charges might have been useful in encouraging the authorities to make greater efforts to meet their obligations as they fell due.

It was clearly within Honduras' ability to clear its arrears to the Fund and meet future obligations as they fell due, Mr. Legg observed, and he would strongly urge the authorities to consider the importance of normalizing relations with the Fund and vigorously pursuing discussions with the Fund staff on the comprehensive policy reforms that were necessary to address the underlying weaknesses of the economy and the external accounts. The staff's comments were mildly encouraging, but the points made by Mr. Enoch and Mr. Grosche on the need for prior actions were particularly pertinent.

The wording of the draft decision was very much the standard formulation for members that had just started down the path of arrears, Mr. Legg concluded. He had no amendments to suggest, and was prepared to go along with the draft decision, particularly if it was a matter of days before things were sorted out. But whether it was appropriate in the case of Honduras to presuppose that, in that event, the authorities were starting with a clean slate was a moot point. The Board ought to be able to distinguish in its judgments between members which had a track record of habitually falling into arrears, and those that did not. Perhaps the staff might have some comments on that point, and could give some thought to it in future cases like that of Honduras.

Mrs. Ploix stated that like Mr. Enoch, she was not very reassured by the staff's report. She would like to see more commitment on the part of the Honduran authorities, especially because as more and more slippages occurred, the actions that would be necessary later on to reverse them would be more and more difficult to implement. Her authorities, like others, were very disappointed by the buildup of arrears, and wished that Honduras would be more resolute in trying to solve the problem. Honduras should implement a sound, strong adjustment program. She hoped that through closer Bank-Fund collaboration, the authorities would be encouraged to develop such a program.

Mr. Kyriazidis said that he joined Mr. Enoch, Mr. Grosche, and Mrs. Ploix in expressing deep disappointment about the emergence of arrears in the case of Honduras. He felt some apprehension about the

prospects for a resolution of the arrears, and, in the light of recent experience, the staff's reassurances in that regard were not really very reassuring. He strongly believed that some serious prior action should be required of the Honduran authorities. If such prior action was absent or weak, the Fund would be close to a situation in which the resources made available under a stand-by arrangement would be used to finance overdue financial obligations to the Fund--that should be avoided at all costs.

The staff did not seem to have presented the usual information given in arrears cases, Mr. Kyriazidis noted. That information was useful for estimating the dimensions of the particular arrears problem.

The staff representative from the Treasurer's Department said that the data to which Mr. Kyriazidis had referred was contained in the paper for the Board on the Managing Director's complaint. The proposed decision was, as Mr. Legg had noted, a decision of the standard type that had been proposed in other cases at the same stage. Although the staff hoped that Honduras' arrears could be resolved quickly, the staff would keep the points raised by Mr. Legg in mind if it became necessary to come to further decisions at subsequent stages.

The staff representative from the World Bank stated that a World Bank mission had returned from Tegucigalpa three weeks previously. The World Bank had discussed creation of a program that would allow clearance of all of Honduras' arrears--to the World Bank, to the Fund, and to the Inter-American Development Bank. The authorities had expressed their willingness to try to solve the arrears problem in the immediate future.

A program of economic adjustment would be useful not only to enable the authorities to perceive their short-term situation more clearly, especially with respect to arrears, but also in order to design a long-term foreign exchange budget, which had been one of the primary topics in the World Bank's discussions with the Honduran authorities, the World Bank staff representative went on. A foreign exchange budget would assure that the resource flows required to clear financial obligations were taken into account in the adjustment process.

The World Bank had approved a structural adjustment loan for Honduras in 1988, the World Bank staff representative continued. A mission for the review for the second tranche under the structural adjustment loan to determine adherence to the targets would be necessary. A preliminary review had taken place in January 1989, and it appeared that most of the targets--except the fiscal targets--would be met, although final statistics on the public enterprises remained to be received. The World Bank was discussing the possibility of adjustments in the public sector program, and sectoral lending in the area of power generation. The Bank had discussed with the authorities the possibility of a joint Fund-Bank mission to consider together a Fund stand-by arrangement and related conditionality and another World Bank structural adjustment loan, which had been well received.

The possibility of further World Bank involvement depended first on the fulfillment of the conditions attached to the second tranche disbursement under the current structural adjustment loan, the World Bank staff representative concluded. In order to proceed with the disbursement, Honduras' arrears would first need to be cleared--at present, Honduras was $43 million in arrears to the Bank. The World Bank supported fully the Fund's position.

The Chairman commented that in the Fund's view, the clearance of arrears was not simply one concern among others, but the pre-eminent concern, before all others. The Fund was paralyzed to assist the country while arrears persisted. He hoped that the Honduran authorities were conscious of the absolute priority that they needed to attach to the settlement of arrears.

Mr. Ayales said that the Honduran authorities were willing to cooperate with the Fund and the Bank. He hoped that agreement could be reached on the policies that would need to be adopted in the current year.

The Chairman, in response to the suggestion by Mr. Ayales and Mrs. Hepp to express in the decision the Board's satisfaction that discussions were proceeding with the Honduran authorities, proposed the addition of the following words at the beginning of paragraph 3 of the draft decision: "While noting with satisfaction that discussions are developing with a view to adopting comprehensive adjustment measures preceded by clearance of the arrears,...."

The Executive Board then took the following decision:

1. On January 30, 1989, the Acting Managing Director submitted a report and complaint to the Executive Board (EBS/89/12), under Rule K-1 of the Fund's Rules and Regulations, setting out the facts on the basis of which it appeared to him as of the date of this report that Honduras was not fulfilling its obligations under the Articles of Agreement. The complaint under Rule K-1 was that as of January 30, 1989, Honduras was not fulfilling its obligations relating to repurchases and the payment of charges in the General Department in the total amount of SDR 3,415,646. In addition, the Acting Managing Director issued a notice of the facts on the basis of which it appeared to him that as of January 30, 1989, Honduras was not fulfilling its obligations under Decision No. 5069-(76/72) to repay disbursements and to pay interest under its Trust Fund loans, and pursuant to Decision No. 8165-(85/189) G/TR to pay special charges with respect to its overdue interest and repayments under Trust Fund loans. These facts, and the complaint under Rule K-1 and notice of failure to settle Trust Fund obligations, were communicated to the authorities of Honduras on February 6, 1989.

2. Having considered the report of the Acting Managing Director, the complaint under Rule K-1 and notice of failure to settle Trust Fund obligations, and the views of Honduras, the Fund finds that Honduras has failed to fulfill its obligations under the Articles of Agreement as stated in paragraph 1 above.

3. While noting with satisfaction that discussions are developing with a view to adopting comprehensive adjustment measures preceded by clearance of the arrears, the Fund regrets the nonobservance by Honduras of its financial obligations, urges Honduras to give these obligations the highest priority and to resume their observance forthwith, and decides (i) pursuant to Rule K-2 of the Fund's Rules and Regulations, that Honduras shall not make use of the general resources of the Fund until such time as Honduras has become current in its obligations under the Articles of Agreement relating to repurchases and the payment of charges in the General Department, and (ii) if Honduras were otherwise eligible to make use of the general resources of the Fund and that use were not limited, to take account of the existence of any overdue obligations to the Trust Fund in considering any request by Honduras for the use of the general resources.

4. The Fund shall review the matter of Honduras' overdue financial obligations to the Fund within a period of three months from the date of this decision.

Decision No. 9098-(89/25), G/TR adopted
March 1, 1989

6. THAILAND - 1988 ARTICLE IV CONSULTATION

The Executive Directors considered the staff report for the 1988 Article IV consultation with Thailand (SM/89/24, 2/2/89; and Sup. 1, 2/27/89). They also had before them a background paper on recent economic developments in Thailand (SM/89/37, 2/17/89).

Mr. Kiriwat made the following statement:

I would like to join my authorities in expressing our appreciation to the staff for their excellent report on Thailand. My authorities feel that it is a very fair appraisal, and are in broad agreement with the thrust of the policy recommendations. I would like to provide a more recent evaluation of Thai economic performance in 1988, together with a look into the economic prospects and the economic policy direction for the medium term.

More recent information indicates that real GDP growth in 1988 was even greater than envisaged during the staff's visit to

Thailand. Encouraged by the favorable external environment, as well as by prudent policy management, domestic factors, and the weather, the economy grew by 10.3 percent. The growth performance of the agricultural sector, at 8.4 percent, was the highest in ten years, and deserves special mention. The manufacturing sector also performed well, achieving a growth rate of 12.6 percent, surpassing the already high growth rate of 10.3 percent in the previous year.

The export sector and the manufacturing sector can be considered the engines of growth in 1988. Indeed, the value of exports increased by 38.6 percent in dollar terms, as a consequence of an expansion in world trade, higher commodity prices, the greater competitiveness of Thai exports, and the promotion efforts of the Thai authorities. At the same time, imports, stimulated by strong economic activity, likewise surged by 49.4 percent. The trade balance thus registered a large deficit of $3.7 billion. The current account deficit, equaling about 3.0 percent of GDP in 1988, however, fared better, as income from tourism increased by over 40 percent. The overall balance of payments was $1.5 billion in surplus, largely because of an enormous increase in net private capital inflows. International reserves, therefore, strengthened to $7.1 billion, equivalent to 4.3 months of imports, while the debt service ratio declined sharply.

With strong domestic demand and demand for exports, as well as higher world prices in general, the consumer price index rose by 3.9 percent, somewhat higher than the 2.5 percent registered in 1987.

Spurred by a sharp rise in economic activity, domestic bank credit to the private sector surged by 26.5 percent, while bank deposits expanded at a slower rate of 17.8 percent. The high liquidity at the beginning of the year, therefore, gradually eroded; and by year-end, a tight money situation prevailed. The rise in international interest rates during the last quarter of the year also put pressure on domestic deposit and lending rates, which eventually followed suit.

The performance on the fiscal front was exceptional, as revenue collections turned out to be much higher than expected because of the rapid expansion in domestic production, business profits, and imports. Meanwhile, expenditures remained very much within the planned budget. As a consequence, the central government budget registered a surplus of revenue over expenditure equivalent to 1 percent of GDP.

Barring an unexpected deterioration in the international environment, prospects remain bright for the Thai economy in 1989. The economy will continue to expand strongly by about

8 percent, with the manufacturing and the export sectors continuing to be dominant. The increase in the consumer price index is expected to remain about 4 percent.

Slower growth in export markets, together with a tapering-off of the effects of exchange rate movements of recent years, should slow export growth. Slower export growth, together with a more moderate increase in investment, should also dampen import growth. Nonetheless, the current account deficit is projected to widen.

For the last three years of the Sixth National Economic and Social Development Plan, which ends in 1991, a modified broad target has recently been set providing for GDP to grow at an average rate of 7.5 percent, with the current account deficit being maintained at not more than 4 percent of GDP on average. The staff's revised medium-term scenario, which reflects weaker developments in the terms of trade, envisages an increase in the deficit to 4 1/2-5 percent of GDP in 1990. Thereafter, the deficit declines to below 4 percent of GDP by the end of the period. The authorities' more optimistic outlook reflects their intention to vigorously restrain domestic demand. Revenue targets and current and investment expenditures have been set to ensure that the budget remains in broad balance. The annual ceiling on public foreign debt commitments has been raised to $1,200 million during FY 1989-91. To achieve these targets, my authorities have spelled out a combination of measures that will have to be taken.

In order to attain the country's medium-term targets while minimizing the risk of overheating, the Prime Minister of Thailand has recently sanctioned a set of measures designed to mobilize domestic savings, as well as to ensure the worthiness of investment projects. My authorities are in the process of drafting work plans to implement these measures.

Emphasis will be placed on developing existing as well as new financial instruments for both money and capital markets, in order to mobilize additional domestic savings, particularly debentures, convertible debentures, warrants, and long-term certificates of deposit. At the same time, strong efforts will be made to promote secondary markets for government bonds and other securities.

Incentives for small savers, such as increasing the tax deduction allowance for contributions toward life insurance schemes and improving regulations covering tax and dividend payments in the capital market, are being contemplated. The possibility of setting up a national provident fund and increasing the role of the specialized financial institutions,

particularly the Government Savings Bank and the Bank of Agriculture and Agricultural Cooperatives, is being explored.

Foreign portfolio investment in the form of closed-end funds and mutual funds is being encouraged.

As for the public investment program--in particular, infrastructural projects--active private participation in providing needed resources is considered essential. The minimal increase in the ceiling on public sector foreign borrowing implies that state enterprises will have to seek much of their financing elsewhere. The possibility of selling shares in some state enterprises to the general public is being actively pursued. At the same time, state enterprises will be required to devote more of their own resources from retained earnings to their investment expenditure. They will also be encouraged to borrow domestically.

Investment promotion policy will be reviewed and directed toward activities with low import content, in order to slow down imports, and toward activities which earn high economic returns. Promoted industries will be encouraged to bring in capital funds and loans from abroad rather than rely on domestic sources of funds.

In terms of export promotion measures, besides paying urgent attention to infrastructure bottlenecks and improvements in packaging and product development, an export credit guarantee fund will be created to assist small exporters. The flexible exchange rate policy, which has been in place for the past four years, will be maintained.

The relatively favorable macroeconomic outlook will provide the opportunity for my authorities to pay more attention to dispersing the benefits of growth. Various fiscal and monetary measures are already being taken toward this end, or are being contemplated. For example, tax privileges given by the Board of Investment are to favor factories established in rural areas, the Bank for Agriculture and Agricultural Cooperatives is to expand lending to poor areas, and the policy relating to the establishment of commercial bank branches is to be reviewed to favor rural areas.

The Thai economy has arrived at an important crossroads, with attractive growth prospects ahead of it. As everyone knows, driving in the fast lane involves an exposure to higher risks. My authorities will continue to identify bottlenecks which could hinder growth and to remedy the situation prudently, taking into consideration all conceivable repercussions on the economy, particularly those threatening economic stability.

With a little luck and a great deal of hard work in maintaining cautious policies, my authorities are confident that the Thai economy can maintain the momentum of growth while preserving external stability.

Mr. Hogeweg made the following statement:

Thailand's performance is most impressive. Economic management will clearly have to center on creating conditions in which growth can be sustained. In essence, that means first striking a balance between directly productive investment, and investment in infrastructure that is needed to support productive investment. Second, sufficient savings should be generated to finance the overall level of investment without recourse to amounts of foreign borrowing that could jeopardize Thailand's debt profile. In other words, consumption growth will have to lag behind the growth of the economy. Only in this way can the investment level be sustained without jeopardizing the balance of payments and/or the inflation rate.

For fiscal policy, this implies that there is indeed no room for stimulus by lowering the government surplus. For monetary policy, there is a clear need, as the authorities recognize, to create attractive savings instruments. Interest rate ceilings can clearly be counterproductive, both from the perspective of stimulating savings and of allowing sufficient policy restraint when it is needed.

The policy dilemma seems to be that in order to keep the expansion of private credit within the target, interest rates may need to be raised, but higher rates could induce capital inflows at the same time, thereby undoing the effect on money growth of credit restraint. Nevertheless, controlling domestic credit expansion should prevail. Part of the bank credit will be used for consumption, while there is a better chance that foreign capital inflows will be used for investment purposes. Moreover, I understand that financial markets in Thailand are quite segmented.

In connection with the adverse effects of capital inflows on monetary conditions, the staff report states that maintaining the present ceiling on the banks' open foreign exchange position is critical for preserving monetary control, as well as for upholding prudential standards. This, however, relates to foreign currency inflows to banks, which, it is presumed, will not react positively to higher domestic interest rates. The report could have been clearer about the role of these ceilings; they typically appertain to prudential supervision, as banks should not be allowed to bear too much exchange risk. Of course, prudential regulation can have monetary consequences,

and vice versa, but the two should be clearly separated for analytical purposes. If I understand it correctly, if banks borrow abroad in foreign currency, they will sell the currency to the central bank, thereby creating domestic bank liquidity. The changes in the net foreign asset positions of the central bank and the commercial banks cancel each other out, implying that no change takes place in the overall balance of payments position and that there is no direct monetary effect. Only the money supply will be affected by an expansion of credit financed in this way, but the central bank has a number of instruments to counteract that effect. Thus, the ceiling on banks' open foreign exchange position may be excellent for prudential purposes, but I doubt that it is really critical for monetary control.

Finally, I wonder why the staff recommends that a deposit insurance scheme should be actively considered while a scheme for reimbursing depositors of liquidated financial institutions already exists. Does the difference between the two lie in the way the reimbursements are financed? Of course, deposit insurance in itself does not strengthen financial institutions; in fact, experience elsewhere suggests that the opposite may be true.

Mr. Yamazaki made the following statement:

Assisted by the decline in the price of petroleum and the realignment of currencies, the Thai economy improved in the mid-1980s and experienced a third successive year of high growth in 1988.

Although this boom was triggered by favorable changes in the external environment, it was also due to the implementation of adjustment efforts and prudent policies. This is clearly evidenced by the fact that the Thai economy achieved a slower but steady rate of growth in the first part of the 1980s, and the variance in its rate of growth from year to year has been relatively small, unlike the growth rates of most other countries in the Association of South East Asian Nations (ASEAN). It is also clear that the efforts of the 1970s and 1980s to diversify the export base have made it possible for the Government to take advantage of the economy's increased international competitiveness, which was brought about by the exchange rate realignment. Indeed, the current boom is different from that of the 1970s, in that the growth of export receipts from the manufacturing sector--rather than primary commodities--is one of the main features supporting domestic demand expansion. Furthermore, looking at the investment/savings gap, the role of fiscal retrenchment in causing an increase in the ratio of saving to GDP was relatively large, so that the need for a

reduction in the level of investment was relatively less in Thailand than in other Asian countries, such as Malaysia and the Philippines. The sustained level of investment during the adjustment period seems to be another factor behind the current boom. All in all, the authorities' export-oriented policy measures proved successful, and their judicious policy management should be commended.

Nonetheless, we see some scope for further improvements in their strategy.

First, there is a need to develop support industries in order to gradually reduce the economy's heavy dependence on imported capital goods and intermediate goods. As the staff report illustrates, capital goods and intermediate goods are the two largest categories of imports, which have increased hand in hand with the growth in the volume of exports. Therefore, the current account deficit would decline only gradually, and there is a need for a broad expansion of the industrial base, including the small to medium-sized enterprises.

Second, tariff reform will be required. We believe that protective measures for the domestic industries persist, and are creating an adverse situation for export industries. We recognize that import duties are important for the fiscal objectives, as they remain one of the major revenue sources, but there is much scope for improvements in the tariff system. The staff may wish to incorporate a further study of that issue into the report on the next Article IV consultation with Thailand.

Third, there may be scope for further improvement in the procedures of the Board of Investment (BOI).

To achieve the targeted high growth rate in the medium term, economic growth needs to rely on the manufacturing sector, and much investment will be required in that sector for some time to come.

Although Thailand's external debt situation is improving significantly, heavy reliance on foreign financing of investment would not necessarily be desirable. The efficient use of domestic savings and the encouragement of foreign direct investment should thus be pursued vigorously. In this context, the fact that the Thai economy has been a favored destination of foreign direct investment, and that foreign direct investment is increasing substantially, are welcome developments. However, much remains to be done to improve the approval procedures of the BOI. First, there still appears to be a discrepancy in the criterion for approval. Second, the investments that have been

approved may have been biased too much in favor of large import-substituting capital-intensive enterprises. Third, much could be done in connection with the approval follow-ups.

In the context of the promotion of foreign direct investment, the land problem is another issue. The land market in the Bangkok metropolitan region seems tight, and land prices there are increasing. Also, aspects of the decentralization of industrial locations should be taken into account in order to disperse the benefits of industrialization to rural areas. In the light of this consideration, the regulations introduced in January 1989 are a most welcome achievement.

I generally share the staff's views in the area of macroeconomic policy. It is commendable that fiscal policy has been conducted generally countercyclically. The clear emphasis on investment in infrastructure is another welcome development. But with the current state of the economy--which is overheating somewhat--the policy stance should be kept generally tight. A broader-based and more equitable tax system would probably be preferable to the current system. We support the idea of introducing a value-added tax by January 1990. The current monetary policy stance seems appropriate. The efficient mobilization of domestic resources should be pursued further, and the reform of the monetary market is important from this point of view.

Diversification of the export base should be sought. In our view, the shift of the industrial structure to a higher value-added production would be advisable. From the experience of other Asian countries, there seems to be a positive correlation between a higher grade of industrialization and increases in per capita income. At the same time, we should not forget that the larger part of the labor force in Thailand is engaged in the agriculture sector. That being said, the promotion of labor-intensive employment-generating, and perhaps agro-based industries is no less important; I am not sure which area should be given greater emphasis. I would appreciate it if further staff study and assessment of that issue could be incorporated into the report for the next Article IV consultation with Thailand.

Mr. Grosche stated that like previous speakers, he was impressed by Thailand's economic performance over the previous year. Strong growth, relatively modest inflation, and a remarkable turnaround in the fiscal position were the welcome results of comprehensive and sustained adjustment policies implemented at an early stage. The staff's analysis and recommendations covered the immediate and medium-term challenges confronting the authorities.

The immediate and most pressing challenge for the Thai authorities would be to assure a smooth transition from the current boom to a sustainable path of growth, Mr. Grosche observed. The first steps in that regard had been taken, such as adherence to the original fiscal expenditure plans that ensured that higher than expected levels of revenues would turn the fiscal policy strongly countercyclical. Nevertheless, it appeared from the staff report that the tax changes that were introduced at the beginning of 1989 would create a little bit of stimulus to the economy. Those changes were welcome in themselves, as they would provide for better incentives, but it would have been preferable if they could have been implemented in a revenue neutral fashion.

The authorities needed to focus on domestic savings in order to generate sufficient resources for continued high investment without endangering the external position, Mr. Grosche continued. The widening current account deficits did not at present pose a threat to the economic balance, but the position had become more vulnerable, and the authorities should be prepared to react quickly to signs of further pressure, and not allow developments to get out of hand. Only slight corrections might be necessary if implemented at an early stage, but if investors' confidence was shattered and inflation accelerated, far more decisive--if not disruptive--action would be necessary in order to return things to a sound economic path.

The authorities needed to press ahead with reforms in the financial sector, Mr. Grosche went on. What was most important, they should ensure that the interest rate structure provided the right signals for savings and investment.

Looking ahead, it would be essential to keep the private sector, which was the engine of growth, running smoothly and efficiently, Mr. Grosche remarked. In that regard, the authorities should be encouraged by their success so far in making further progress in liberalizing external trade and domestic investment. The recent initiatives that had been taken by the authorities were encouraging, but they should be pursued somewhat more vigorously, in his view.

Like the staff, he was convinced that Thailand's economy was well poised for the medium term, and he was confident that the authorities would deal with new challenges as effectively as they had done in the past, Mr. Grosche concluded. Thailand's success could indeed provide an excellent example for others, an example which demonstrated that comprehensive and sustained adjustment efforts within the context of a market-based incentive structure could pay off handsomely in terms of growth and employment.

Mr. Fernando made the following statement:

> The Thai economy has had an enviable record of growth over the past several years. After having achieved the magic double digit rate of growth last year, the economy looks set for an

average growth rate of 7 percent per annum over the next few years. This has been accompanied by remarkable price stability; there are shortages of manpower, not unemployment. Balance of payments developments reflect the successes achieved in diversification not merely of the commodity structure of exports, but of export markets as well. The external current account deficit is low, and its recent widening reflects, if anything, the robustness of the economy and the continuing impact of inflows of foreign direct investment--induced by economic opportunity, as well as by confidence in the economy, which is the vital factor. The rapid and sustained correction of fiscal conditions so as to achieve a fiscal turnaround, and the prospects for a continuation of those enlightened policy decisions, augur well for price stability and the balance of payments. The level of external debt--already moderate--has been reduced still further, and the debt service burden is low and still declining. At the same time, external reserves are at a comfortable level, and, while this level should reflect the precautions against negative exogenous developments, one must recognize the safety margins implied by the confidence factor, which makes Thailand an attractive place to invest and hold money. This chair holds the view that when something is working well, it should be left alone.

However, the staff report rightly draws attention to the possible overheating of the economy, and the growth constraints encountered as a result of the level of infrastructure, which is currently unable to cope with the demands of an economy in high gear. The inadequacy of the economic infrastructure must be seen as the inevitable consequence of a policy of fiscal correction, which in its early years was anchored to expenditure restraint. In most developing countries expenditure restraint has inevitably fallen heavily on central government investment outlays, given the constraints imposed by social and political factors.

In addressing this matter, the authorities plan to step up public sector investment in infrastructure within the parameters of a balanced budget, or even a budget with a small surplus. The staff recognizes that such a course is logical, given past cutbacks. However, there is also the expectation of strong investment by the private sector in infrastructure, which is increasingly evident. If that continues, well and good; but at the same time, we should recognize at least one factor that is working to dampen such a prospect--the interest rate. The staff supports a tighter monetary policy and raising interest rates further so as to curb any inflationary impulse. Of course, rising interest rates will act as a deterrent to any kind of private investment, but for investment in infrastructure that applies with even greater force. Infrastructure investments are typically large and could therefore involve a high capital

gearing ratio. The interest cost element should also be seen in the context of the longer gestation period for infrastructure investment to bear a dividend. Profit margins in the operation of infrastructure facilities are generally not particularly enticing, although I am not sure what the effects will be in the case of Thailand. I would be interested to hear any staff comment on this point.

The staff report says that private savings tend to be unresponsive to policy measures, and most of the domestic savings requirements will have to be met by the public sector. The staff thus stresses the need for a fiscal surplus, because even though personal tax rates have been lowered, hence increasing disposable income, it is not expected that savings will thereby be enhanced. There is also the question of the marginal propensity to consume in the face of rapid income growth. Income growth is likely to benefit those in the urban areas because of the dynamism of the manufacturing sector, which is concentrated in urban areas. One would think that that factor would tend to provide an added impetus to savings by well-to-do individuals. I would appreciate hearing the staff's thoughts on that aspect.

There is another related point which is unclear. Although the staff has said that private savings tend to be unresponsive to policy measures, it also says that increases in interest rates are likely to be needed to promote private savings. These two views need to be reconciled.

We are impressed by the safety margins which are available to the authorities for facing any adverse external developments. We have already referred to the Thai authorities' track record of resolute action, and the confidence factor. Another is the potential for an even stronger fiscal performance, as revenue estimates are on the conservative side. On the external front, because of foreign direct investment in manufacturing industries, the prospects for exports could well go beyond what the conventional variables--such as the exchange rate, and protectionist trends in foreign markets--would otherwise suggest.

Mr. Enoch stated that Thailand's economic performance had continued to be most impressive in 1988. Real per capita income had grown again very strongly, unemployment had fallen significantly despite the sharp growth of the labor force, exports and investment had surged ahead, and the debt service ratio had fallen to its lowest level in the 1980s. Overall, the Thai economy was rapidly being transformed, in both its agricultural and industrial sectors. As the staff had pointed out, the exceptional performance owed a great deal to the successful adjustment measures undertaken by the authorities in the early 1980s.

The question at present was what the authorities should do to ensure that Thailand's take-off into high growth could be maintained, Mr. Enoch continued. Thailand possessed a number of advantages that were not shared by all countries at its stage of development. The export base was relatively diversified, the private sector was the main engine of growth, and the country was not burdened by a high fiscal deficit or excessive debt service burden. Thus, although, as the authorities themselves recognized, the growth in domestic demand and national income achieved in 1988 could not be sustained, there were good prospects that a healthy rate of growth--of perhaps 7 percent a year--could be achieved over the medium term. Such a favorable outcome would require careful handling, however. Despite cautious monetary and fiscal policy, some signs of overheating had emerged during the course of 1988, including shortages of skilled labor, infrastructural bottlenecks, capacity constraints, and shortages of raw materials. Reflecting those strains, the current account deficit had widened sharply, and inflation had doubled. The staff report therefore rightly focused on the need to remove bottlenecks and improve the infrastructure, and commended the authorities for their plans to increase public investment. The staff report also stressed the need to moderate the rapid growth in domestic demand in the short run.

In the coming year, an important question would be whether the measures the authorities had already taken to rein in demand would be sufficient to dampen inflationary pressures and forestall a serious deterioration in the external balance, Mr. Enoch noted. Like the staff, he had some doubts on that score. It was notable that the authorities were projecting a more rapid growth in both broad money and domestic credit in 1989 than had been seen in 1988. A further sharp deterioration in the current account deficit was consequently expected, together with a fall in reserves coverage. On the monetary side, he had been interested to read in the paper on recent economic developments in Thailand that banks' deposit and lending rates had tended to be much stickier over the recent past than money market rates. Thus, despite the sharp increase in the interbank lending rate over the course of 1988, it was apparent that the actual interest rates faced by domestic agents in Thailand had not risen much over the previous year, and indeed may actually have fallen in real terms. Although the recent staff supplement suggested that those interest rates in fact had begun to move up around the beginning of 1989, the general stickiness of interest rates was not helpful. He would be interested to know whether the staff had any explanation for that phenomenon--for example, did it reflect a lack of competitiveness in the banking system?

The authorities would thus need to keep a very close eye on monetary developments over the coming months, Mr. Enoch commented. He agreed with the staff that interest rate ceilings must not be allowed to obstruct a further tightening of monetary policy, should that prove to be necessary. Indeed, the authorities might wish to consider whether the retention of any interest rate ceilings was warranted in the present circumstances. Regarding the dilemma over external financial inflows, he fully agreed with Mr. Hogeweg's observation that it was necessary to distinguish

between foreign currency borrowing by domestic banks and foreign demand for domestic currency, and between prudential and monetary control objectives. Inflows from abroad in the present circumstances should not be a reason to relax domestic monetary conditions; the central bank had instruments at its disposal that would enable it to achieve its monetary objective. That being said, it was of some concern that external flows appeared to have led to an unwarranted relaxation of monetary conditions over the preceding few months, including a fall in money market rates.

The recent growth in personal sector indebtedness should enhance the leverage of interest rate policy on consumer demand, Mr. Enoch went on. Thus, despite the staff's somewhat pessimistic assertion that private savings tended to be rather unresponsive to policy measures, a further increase in real deposit rates, together with the development of more attractive longer-term savings instruments, should contribute to a reduction in consumption growth. Beyond that, the need to increase the level of private savings over the medium term suggested that the authorities should give considerable priority to financial sector reform. He was encouraged by the emphasis Mr. Kiriwat had placed on that issue in his statement.

Nevertheless, it was clear that over the short run, public sector savings would need to remain at historically high levels, Mr. Enoch remarked. In that context, and given the continued conservatism of the authorities' revenue projections, the small budget surplus envisaged for 1988/89 seemed prudent. However, the authorities would need to ensure that fiscal policy remained supportive of their monetary objectives. In addition, every effort should be made to limit the "knock-on" effects of the sharp increase in government salaries on other sectors of the economy.

Provided that the authorities could engineer a soft landing for the economy, the outlook for the future appeared bright, Mr. Enoch observed. In the staff's medium-term scenario, a period of strong output growth, combined with low inflation and a manageable external position, appeared to be within the authorities' grasp. Nevertheless, there were some uncertainties surrounding those projections.

He wondered how confident the staff was that vigorous export growth could be sustained over the medium term, for example, Mr. Enoch continued. Annex III of the background paper on recent economic developments suggested that the impact of a real depreciation on the demand for Thailand's manufactured exports had largely been felt within the first year. Given the prescription of a constant real effective exchange rate, that implied that continuing strong export growth into the 1990s would largely depend on increasing world demand. However, the growth rate of trading partners' imports was projected to fall. Moreover, Thailand might face increasing constraints in the form of nontariff barriers in industrial countries. In that connection, the United States accounted for almost 20 percent of Thailand's exports; he wondered whether the staff had any estimate of the effect of the lessened privileges under the U.S. Generalized System of Preferences on exports to the United States in 1989.

Notwithstanding continuing strong export growth, Mr. Enoch went on, the staff envisaged that Thailand's current account deficit would remain large over the medium term. If the external position was to remain manageable, continuing strong inflows of foreign direct investment would be necessary. While direct investment was less volatile than other capital inflows, continuing inflows would nevertheless depend on the investment climate in Thailand. That underlined the importance the authorities should attach to pursuing steady and cautious macroeconomic policies. In addition, in order to prevent undue uncertainty, the current review of the policies of the Board of Investment should be completed as expeditiously as possible; and in order to promote further foreign portfolio investment, the authorities should consider a liberalization of the capital market restrictions on foreign ownership.

There were two areas in which progress appeared to have been somewhat slower than might have been hoped for, Mr. Enoch remarked. First, the authorities had put active consideration of privatization proposals in abeyance because of strong opposition from the unions. He hoped that the authorities would reconsider that decision. He had therefore been reassured by Mr. Kiriwat's statement that the possibility of selling shares in some state enterprises was again being actively pursued. In other countries, privatization had proved to be a very popular measure with those working in the particular companies concerned, despite the initial resistance of worker representatives. The unions' support might be obtained by offering a portion of the stock in the company to employees on favorable terms.

The second area in which little progress had been made was the issue of whether Thailand should move to Article VIII status, Mr. Enoch concluded. He had understood that a mission would go to Bangkok sometime in 1988 in order to pursue the matter. Both Indonesia and Korea had accepted the obligations of Article VIII in 1988. He hoped that Thailand would be prepared to follow the example of those countries, and he would be grateful for a report--from Mr. Kiriwat or the staff--on where matters stood in that regard.

Mr. Dai made the following statement:

> The Thai economy performed remarkably well in 1988. Economic activity, led by a rapid growth of exports, remained robust, owing to the authorities' prudent and successful management, as well as to a favorable external environment. The momentum was maintained because of a strong recovery by the agricultural sector. While private investment continued to grow at a fast pace, the public sector showed a large surplus, which was mainly attributable to a continuous increase in government revenue and expenditure restraint. This strong budgetary position is expected to continue into 1989. Monetary policy is also on the cautious side. The money supply showed no further rise in 1988, despite an increase in net foreign assets. A major offsetting factor was the sharp reduction in domestic

claims on the government. The authorities have expressed their intention of maintaining a restrictive monetary policy. The general thrust of macroeconomic policies for 1989 seems satisfactory. I am in general agreement with the staff's appraisal, and will just touch briefly upon a few issues.

First, the wider margin between private investment and savings seems to point toward an external imbalance which will continue to increase. The domestic economy has already started to show signs of an increased, although modest, inflationary trend. According to Mr. Kiriwat's statement, the expansion in bank deposits was much smaller than that of credit to the private sector toward the end of 1988. A tight liquidity position would undoubtedly put pressure on monetary policy to increase the money supply. At this juncture, it is important for the monetary authorities to maintain this tight position. Such a restrictive demand-management policy would not only prevent the economy from overheating by slowing down private investment, but also contribute to the development of secondary markets for government bonds and other securities. This would certainly be desirable in terms of domestic savings mobilization, which is highly important in order to ensure sustained noninflationary growth for the country's medium-term development.

Second, I notice that capital inflows were huge in 1988, and that a major part of the inflows was comprised of short-term capital, as well as direct investment. It is likely that this situation was associated with buoyant private investment and the resultant import boom over the last two years. While the dampening effects of domestic demand-management measures would tend to restrict further inflows, the increased domestic interest rates may still attract foreign capital inflows. Again, this would exert pressure on monetary policy to lessen the restraint on credit. The authorities have been fully aware of this tendency, and seem prepared to deal with any problem arising from it. However, as suggested by the staff, more cautious measures, such as maintenance of the present ceiling on the banks' open foreign exchange position, may be advisable.

Third, the increase in investment by state enterprises is very noticeable. I am under the impression that most of this investment went toward alleviating infrastructural bottlenecks, and it seems to have been quite efficient in the public sector. Since the amount of finance that these investments will need will be enormous, it is clear that measures to support public savings are essential. In addition, a modest relaxation of the current external borrowing policy, as suggested by the staff, may be advisable in order to meet the compelling need for additional spending on infrastructure. In this regard, I wonder whether World Bank financing is more desirable.

Fourth, I am also very much impressed by the authorities' policy intention to pay more attention to dispersing the benefits of growth to the poorer rural areas. This would lessen the imbalances between different regions and sectors in the economy, and would contribute to further sustained development of the economy.

I would like to commend the Thai authorities for their skillful management of the economy. The excellent performance of recent years has been impressive indeed. In particular, it is noteworthy that, under its industrialization policies, Thailand has moved from being chiefly a primary product exporting country--a major trader in rice--to being an important regional exporter of both manufactured and agricultural products. An important contribution to this remarkable progress has been successful policy management, as well as the country's rich endowment of natural resources. I believe that Thailand's experience is worth studying, and can be useful for other countries.

I fully agree with Mr. Kiriwat that driving in the fast lane involves an exposure to higher risks. I also share the staff's view that in light of the authorities' outstanding success in recent years and the efforts made during 1988, there is every reason to expect that Thailand will be able to maintain a satisfactory rate of growth in the year ahead.

Mr. Kabbaj made the following statement:

We welcome this opportunity to review recent economic developments in Thailand, and support and commend the authorities' efforts and initiatives in sustaining remarkable economic progress.

The economic adjustment policies initiated in 1980, which were aimed at containing the public sector deficit and strengthening the external economic position, began to have impressive results from 1986 onward. Indeed, the process of diversification of the economy accelerated over the past few years, and the manufacturing sector's contribution to the economy increased significantly. Moreover, the economy continues to be characterized by sustainable export-oriented economic growth, along with satisfactory management of the external position.

In 1988, despite maintenance of the previous economic gains, including a further increase in GDP growth, a steep rise in private investment and rapid export growth, the outstanding rate of the economic expansion--at 10.3 percent--has put some strains on resources. Infrastructural bottlenecks emerged in

the transportation sector. Moreover, with a sharp increase in imports, the current account deficit increased from 1 percent of GDP in 1987 to 3 percent of GDP in 1988.

Taking all these developments into account, we can certainly support the staff's view that the key issue at present for the already overheated Thai economy is how to sustain noninflationary growth and manage the external position in a satisfactory manner. In this respect, we concur with the staff's conclusion that the economy should be cooled down gradually, by implementing more restrictive demand-management policies. In this connection, we commend the authorities for their prudent fiscal policy during 1987/88, which enabled the Government to use excess budget revenue for decreasing its indebtedness to the banking system. It is to be noted, however, that despite the adoption of a restrictive credit policy by the Bank of Thailand since late 1987, the growth of private credit continued to rise in the second half of 1988.

We also share the staff's view that the savings/GDP ratios, particularly of the private sector, need to be increased further. Taking into consideration the envisaged increase in public sector infrastructural investment in the future, it is not certain that the persistent gap between savings and investment in the private sector will be closed through public sector savings. In this regard, it is of paramount importance that the appropriate policies to augment private savings are implemented.

We certainly welcome the development of new financial instruments for both money and capital markets. The promotion of a secondary market for government bonds and other securities is definitely a most appropriate step. The private sector will be more inclined to hold government bonds and other securities if their potential liquidity is enhanced, which will consequently assist in controlling the liquidity of the economy.

As Mr. Kiriwat has indicated, the export sector was the engine of growth in Thailand in 1988; the rate of export growth--of 38.6 percent--is indeed quite remarkable and impressive, for which the authorities deserve to be commended. We note that there is no disagreement between the authorities and the staff on exchange rate policy. However, in maintaining such a rapid rate of growth in exports, it is of utmost importance that considerable attention is paid to the nonprice--or marketing--factors in international markets. It is indeed encouraging to note that the authorities are well aware of the significance of improvements in packaging, product development, and other areas of export marketing. It is needless to say that all these efforts and initiatives will be fruitless unless Thailand is granted sufficient access to markets in developed countries.

Finally, the authorities' commitment to increasing resources to rural development is praiseworthy. We encourage the authorities to give high priority to further development of the agricultural sector, which continues to contribute to exports, employs the majority of the population, and plays a crucial role in securing the country's long-run self-sufficiency in foodstuffs.

Mr. Shaffrey made the following statement:

Like previous speakers, I find that the performance of the Thai economy has been impressive. Although some of the economy's performance is attributable to favorable external developments, much of the credit is due to the authorities' adjustment efforts.

As the staff report points out, the challenge for Thailand is to consolidate its recent gains and remain on a path of sustainable growth. The medium-term scenario is based on reasonable assumptions, and indicates that the Thai economy can maintain a very respectable rate of growth--although necessarily lower than that achieved in 1988--while maintaining the viability of the external sector.

To achieve the outcome outlined by the medium-term scenario, at least for the immediate future, it is clear that domestic demand needs to be restrained, and I agree that a fiscal outcome similar to that of 1987/88 would be required to achieve it. The prospects for achieving that outcome appear good, but fiscal restraint needs to be reinforced by an appropriate credit policy. With most interest rates at their official ceilings, I would strongly endorse the staff's view that these ceilings should not restrict the ability of credit policy to restrain demand and to encourage private savings, thus reducing the demands on public savings.

While domestic demand needs to be restrained, it is equally clear that there is a need to increase investment in the infrastructure of the economy in order to alleviate the strains that were highlighted by the strength of the economy in 1988--strains which will place constraints on the growth capacity of the economy if not addressed now. It is pleasing to note that the Thai authorities are already addressing this problem, and in a responsible manner--although this is no surprise, given the authorities' prudent approach to financial management over the years. Also, I welcome moves to give the private sector a greater role in providing infrastructural facilities; such moves are consistent with the role of the private sector both in maintaining the forward momentum of the economy, and in decreasing the burden on the public sector.

In the area of structural policies, I am pleased to note that plans for a value-added tax to replace the business tax are still in place, although implementation has been set back by one year. Last year, this chair seriously questioned the proposal to exclude about 40 percent of domestic expenditure from the value-added tax, noting the implied subsidy to the nontax areas and the distorting effect on expenditures. The introduction of the new personal income tax schedule only reinforces these misgivings about the proposed coverage of the value-added tax, and I would welcome some indication from Mr. Kiriwat or the staff as to whether the authorities have reconsidered the question of exclusions--or are likely to.

I note also that proposals for financial reform, aimed at mobilizing private savings, are under consideration. Given my earlier comments on credit policy, I urge the authorities to give careful consideration to abolishing ceilings on interest rates completely.

In conclusion, this chair remains impressed with the policies being pursued by the Thai Government. Given Mr. Kiriwat's indications that the authorities intend to restrain domestic demand vigorously--a credible commitment given their record--the Thai economy seems set for a further period of impressive, sustainable growth.

Mr. Templeman made the following statement:

The benefits of Thailand's earlier economic adjustment and reform efforts remain apparent in the generally good economic performance over the past year. Still, there is clear evidence that the boom in domestic demand--both consumption and investment--coupled with continued strong foreign demand, pose some problems that merit prompt attention. The supplement to the staff report reinforces this conclusion. Early corrective actions are likely to be both more effective and less drastic than if excess demand were to be allowed to continue. In fact, coping with strong domestic demand may be the first priority this year. Nevertheless, the focus on the medium term during the consultations was entirely appropriate.

We note that progress on structural reforms in three areas that were mentioned by the Board at the previous Article IV consultation discussion (EBM/87/165, 12/4/87) has been rather uneven--that is, with regard to tax reform, public enterprise reforms, and reduction in the level of protection. In the last case, we welcome some recent market opening measures for certain agricultural products, but tariff rates remain generally high, and we hope that the Thai authorities will take advantage of the Uruguay Round to reduce them.

The key to continued strong economic growth, financial stability, and external viability will be high savings and investment ratios. This underlines the importance of developing long-term savings instruments to help in the process of intermediation for private savings and to provide a vehicle for noninflationary financing of public investment over the medium term. We therefore welcome Mr. Kiriwat's statement that the Prime Minister recently approved a set of measures aimed at these objectives. However, we noticed that bond issues by the public enterprises have been small so far, and we wonder why this is so. It also seems clear that the level of public savings will need to be substantial in order to help to finance the needed investment in infrastructure. Therefore, careful attention to the revenue effects of planned tax and customs tariff reforms will be required, as will the need for prompt adjustment of public enterprise prices and tariffs. The planned private sector participation in the construction of infrastructure offers a very useful degree of complementarity and flexibility.

On the one hand, the fact that Thailand has achieved approximate fiscal balance, at both the central administration and overall public sector levels, creates a strong base for the necessary savings and investment effort. On the other hand, given current strong domestic demand, we share the staff's cautionary note about the inappropriateness of any fiscal stimulus this year, even at the margin.

I have already mentioned the need to keep in mind the revenue effects of fiscal reforms, such as tax and customs tariff reforms. In addition, we note that the introduction of the value-added tax has been delayed for a year, although at the time of the previous Article IV consultation discussion it was expected that it would take effect at the beginning of 1989. We commented then that not much progress had been made on customs tariff reform--which still seems to be the case. We also read in the staff report that privatization of public enterprises is now in abeyance, mainly because of resistance from the labor unions. We wonder whether this represents an important change in policy, or whether the sale of shares in these enterprises, to which Mr. Kiriwat refers, is meant to substitute for privatization.

Returning to the 1989 financial outlook, we agree with the staff that it is not yet clear if the tighter credit and higher interest rate stance assumed by the authorities will prove sufficient to contain credit demand. Our first preference would be for removal of interest rate ceilings, which might be introduced in the context of a broadening of financial market instruments. Finally, we are pleased to note that the central bank did not have to provide extraordinary financial support to the

banking system in the form of soft loans or capital funds last year--a positive sign, given the past history of troubles in the banking system.

Despite the movement into deficit of the current account of the balance of payments last years, the medium-term outlook for the external accounts appears quite favorable. Still, the recent spillover of excess demand into imports, and new evidence of likely stronger demand pressures over the medium term, suggest, on the one hand, the need for continuing attention to demand restraint. On the other hand, evidence that import growth has been concentrated mainly in capital goods and industrial inputs is a mitigating factor. The level of official reserves, Thailand's good external credit rating, the rapid rate of Thai export growth, Thailand's low debt ratios, and, most of all, the authorities' record of prudence in managing Thailand's external debt, are also comforting. In addition, the growth of foreign direct investment is a positive factor, although we continue to believe that limits on foreign equity participation and the lack of patent protection constitute impediments to such capital inflows and to the diffusion of technology.

The major strengthening of Thailand's external position from the real effective depreciation of the baht through 1987 seems still to be having its effect. Therefore, we agree with the staff that there appears to be no reason for further nominal depreciation of the rate. This can continue to be the case if Thailand maintains control over its domestic cost and price movements. While there has been some upward movement in domestic costs and prices, it does not appear to have been a serious problem so far.

Mr. Prader made the following statement:

We are under an obligation to the staff for the excellent analytical background they have provided to help the Board understand the complex but enormously encouraging case of Thailand. Stimulated by prudent fiscal policies aimed at revitalizing business confidence and by a benign regional external environment, the Thai economy has performed remarkably well since 1985. Like others, I think Thailand could serve as a role model for other developing countries. With such satisfactory circumstances, Mr. Enoch's suggestion that Thailand move to Article VIII status seems reasonable.

Three major factors are responsible for Thailand's success; the first is fiscal policy. Even though Thailand has a planned economy and the incentives provided through the Board of Investment have a large effect on investment decisions, growth strategy is centered on private initiative. This is because

Thailand's fiscal policy is almost unique, in directing the Government's capital investment expenditures to the support of certain kinds of private investment decisions after they are made. Instead of beginning an initiative in infrastructure--for example, a railroad and port facilities--and hoping that private investment will thus be encouraged to build enterprises to use that infrastructure, the Government has a consistent policy of supporting, with construction of the needed facilities, private sector investments in new enterprises after the private sector has taken the lead. This approach avoids the crowding out of new private enterprise investments resulting from prior excessive government borrowing to fund infrastructure projects, and permits the Government to direct a share of private investment to the tradable goods sectors as well. The strict taxation of speculation, such as real estate transactions, helps to discourage the inefficient allocation of resources.

Second, Thailand's vigilant exchange rate management has enabled it to take advantage of the regional external environment. Thailand was able to gain an advantage from the unannounced integration of the economies of the region by virtue of its consistently competitive exchange rate and growing labor force.

Third, although the commitments that have been made to service external debt during the adjustment are--in effect--pledges to shift rapidly from nontradable to tradable goods, and to accept the resulting medium-term inflationary pressures, those effects are offset in Thailand's case by increased amounts of foreign direct investment. In other words, a timely influx of foreign direct investment to the tradable goods sector has meant that supply shortages in the nontradable goods sector, which might have come about owing to the reallocation of resources that would be required for better export performance, were avoided.

We share the staff's concern about some signs of overheating in the economy--inflation increased from 2.5 percent in 1987 to 5 percent in 1988--and the fact that keeping the public savings ratio on its current track will require a considerable slowdown in the growth of domestic consumption. Realignment of interest rates or abolition of interest rate ceilings, and discouragement of short-term capital inflows, would be major steps in this direction. Encouragement of longer-term financial instruments, which we understand from Mr. Kiriwat's statement is being considered by the authorities, would be a welcome measure.

In the fiscal policy area, we share the authorities' caution about overspending on infrastructure. Recent private sector interest in infrastructure investments, such as port facilities and industrial water supply, should be encouraged and

extended. An increase in general interest rates might create a climate that would make more attractive the purchase of shares in financially sound public enterprises with appropriately adjusted tariffs, at a time when the privatization of public enterprises is being resisted by the labor unions.

Thailand's medium-term outlook depends on regional developments and its domestic policy stance. Given the continuation of current trends in regional exchange rates, any absent and unexpected revival of protectionism in its major markets, Thailand's admirable growth should be sustainable in the medium term. Thailand is a good example of how dynamic forces can be harnessed and directed by skillful and prudent management.

Mr. Al-Assaf made the following statement:

I would like to commend the Thai authorities for their remarkable achievements in managing their economy. I am in broad agreement with the staff report, and concur with the view that the economy is basically sound and well positioned to continue on its present, impressive growth path over the medium term.

It is important, however, to reduce the risk of overheating by maintaining an adequate level of public investment. The infrastructure, in particular, has not kept pace with the level of general economic activity. Although the tensions and bottlenecks that seem to be emerging as a result have not yet had any marked effect on price performance, they clearly indicate that action on the infrastructure should not be delayed. It is encouraging to note that the authorities are aware of this problem.

There is also the need to maintain a sufficient level of domestic savings, and, in particular, private savings. This is important in order to avoid an excessive degree of dependence on foreign savings. The Thai economy, of course, has had no difficulty in attracting such savings, which attests to the favorable judgment of the international financial community on the soundness of the economy. Nonetheless, adverse developments in the world economy could eventually restrict such flows and affect the authorities' margin for maneuver.

While the economy of Thailand is characterized by a high degree of overall efficiency, as demonstrated by its growth performance in a context of overall price stability, a weak spot in the system appears to be its financial sector. Financial sector reform is an area in which more effort is needed, and I encourage the authorities to promote the necessary modernization and strengthen financial institutions.

On exchange rate policy, while I agree with the staff's assessment that no further depreciation of the baht is required at this time, I would also note that in light of the strong domestic demand, the large trade deficit, and reliance on autonomous external capital flows, even a moderate appreciation of the exchange rate can have unusually sharp effects on the evolution of the external accounts. This is an area which the authorities should keep under close watch. Once again, I would like to commend the Thai authorities for their impressive management of the economy.

Mr. Fogelholm stated that he concurred with the staff's appraisal and had nothing to add to the analysis. However, he concurred with Mr. Enoch's remarks regarding the acceptance of the obligations of Article VIII, Sections 2, 3 and 4 of the Articles of Agreement by Thailand. Also, against the background of Thailand's impressive economic performance and the authorities' excellent track record, he wondered whether Thailand could be moved onto the bicyclic consultation procedure, and whether that issue had been raised with the authorities.

The staff representative from the Asian Department said that the ceiling on banks' open foreign exchange position had been imposed initially for prudential reasons. In practice, the ceiling had also played a role in monetary control, particularly during swings in the liquidity situation in the domestic market. Presumably, banks could bring in as much foreign exchange as they wished and cover it forward, but in fact such covering facilities had not been available at all the desired maturities. Therefore, as the domestic liquidity position had tightened in 1988, the Bank of Thailand had come under increasing pressure to raise the ceiling so that the banks could maintain a larger open foreign exchange position--which, in turn, would have had an effect on reserve money and credit expansion. Although there were means--other than adjustments in the ceiling--by which the Bank of Thailand could offset unwanted foreign inflows, it was not certain whether they could be implemented as quickly as might be necessary. The experience of other countries in the region had also shown that when foreign exchange inflows were very large, it was difficult to sterilize them completely.

Although a limited type of deposit insurance scheme was in place in Thailand, a wider ranging system might be advisable, the staff representative went on. That recommendation had been made during the 1987 Article IV consultation discussions when a member of the Central Banking Department had participated in the mission in order to review in some depth recent developments in the financial sector. The current deposit insurance scheme covered only some deposits at some institutions. The staff believed that a more generalized scheme would permit a more orderly handling of financial institutions in difficulty, as it appeared that the Bank of Thailand was under pressure to support troubled institutions instead of closing them. The Bank's flexibility in handling those situations was circumscribed to some extent because there was no comprehensive

mechanism for insuring depositors. Of course, the staff and the authorities recognized the drawbacks of generalized deposit insurance schemes.

The authorities were concerned about increasing the domestic value added of production, particularly of exported goods, the staff representative went on. In response to market forces and the surge in exports, there had been sizable increases in investment in intermediate inputs, petrochemicals, automobile parts, and television tubes, for example, which were to come on stream in 1989. That trend had been assisted somewhat by the incentives offered by the Board of Investment. There was also currently some discussion of investment in capital goods industries.

The staff had advocated that interest rates be raised both to restrain credit growth and increase savings, the staff representative remarked. However, experience in other countries suggested that the level of private savings was not very responsive to higher interest rates. The impact of the introduction of new financial instruments on the level of savings was also difficult to measure. Nevertheless, given the pressing need for increasing savings in Thailand--not least for investment in infrastructure--everything should be tried. On the related issue of the stickiness of interest rates, there was no completely satisfactory explanation of that phenomenon in Thailand, although the imperfect competition in the banking sector was widely thought to be an important factor. Such stickiness of interest rates was not unusual in developing countries.

The staff agreed that a higher level of growth in the manufacturing sector vis-à-vis the agricultural sector was likely to lead to a greater level of savings, because the marginal propensity to save was greater in the organized sector, the staff representative noted. That also explained why the private savings ratio was expected to increase over the medium term.

Participation by the private sector in investment in infrastructure was an important trend in Thailand, the staff representative went on, but it still represented only a small part of the whole. As Mr. Fernando had pointed out, however, many infrastructure projects were not suitable for private sector participation, because the returns that were external to the projects were greater than the internal returns. If interest rates were to increase, then presumably those projects most sensitive to the level of internal returns and investment by the private sector would be most affected. Of course, not all infrastructure projects would be left to the private sector, and it appeared that the returns on those projects most likely to be supported by private investment would be high enough so that an increase in interest rates would not have a major effect on them.

Domestic bond issues by state enterprises had been relatively small because the bond market in Thailand lagged behind the development of the real sector, and perhaps also of the financing needs of Thai companies, the staff representative observed. Another problem behind the low level of domestic bond issuances was that official reserves had until recently been relatively low, and the investment of state enterprises tended to

have a large import component. Consequently, a consideration in determining borrowing by state enterprises was how to secure the foreign exchange that was needed for the type of investments they made.

Because Thailand was not eligible for loans from the International Development Association (IDA), the advantages of increased World Bank financing of projects were not obvious, and were not materially greater than what Thailand could obtain from commercial sources of finance or foreign direct investment, to which Thailand had ready access, the staff representative noted.

Underlying the assumption of relatively rapid export growth over the medium term was the assumption that the real effective exchange rate would be stable, the staff representative explained. Also, although the growth in world markets would slow somewhat from that experienced during 1988, it was still expected to be relatively strong in the medium term. Based on past empirical relationships, exports responded fairly strongly to world market growth. The projections for rapid export growth were also reinforced, in the staff's view, by the robust investment in the export sector that had taken place over the previous few years and that was expected to continue through 1990. Thus, the risks to export growth were likely to be all on the demand side, because there was little capacity constraint to export growth.

On a related issue, the Thai authorities had begun to assess the impact of the announced cuts in privileges under the Generalized System of Preferences of the United States, the staff representative went on, and at present the effects were expected to be small. The status of eight products, accounting for about 25 percent of Thailand's exports to the United States in 1987, would change. However, an offsetting factor was that Thailand was likely to benefit from the elimination of preferences under the Generalized System of Preferences for a number of Asian countries that competed directly with Thailand in export markets.

Tariff reform would reduce tax revenues, as one Director had observed, but such a reduction could be offset by changes in other taxes, particularly consumption taxes, the staff representative commented. In fact, that aspect had been emphasized by the staff in the discussions on the introduction of a value-added tax. A value-added tax would be a relatively flexible tax, should additional revenues be needed. On the matter of exemptions from the value-added tax, the details of the tax had not yet been finalized, and the authorities were aware of the arguments against the exemptions.

The focus of privatization efforts had changed, the staff representative stated. The authorities had previously concentrated on shifting state enterprises into private hands, but were currently focusing on increasing private sector participation--in providing infrastructure, in particular. For example, private sector participation in constructing a rapid transit system for Bangkok, in road building, and in providing water for industrial uses was under consideration. The change in focus

did not represent a backtracking on privatization efforts. Rather, it was a forward-looking approach that placed the emphasis on increasing the role of the private sector in those sectors of the economy that had traditionally been reserved for the public sector. Private sector participation was viewed as having been quite successful in ports administration and in supplementing the public sector bus and rail network. The authorities were also considering encouraging state enterprises to become listed on the stock exchange.

Acceptance of the obligations of Article VIII, Sections 2, 3, and 4 of the Articles of Agreement by Thailand had been discussed with the Thai authorities, the staff representative noted. Thailand maintained an exchange system free of restrictions on payments and transfers for current international transactions. The staff had pointed out that Article XIV status had thus ceased to have any practical benefits for Thailand. However, it was the view of the authorities that formally accepting the obligations of Article VIII would be administratively difficult and would require parliamentary approval, and that waiting for a better time to do so would be advisable.

The question of moving Thailand onto the bicyclic consultation procedure had not been raised with the Thai authorities, the staff representative concluded. There were a number of considerations behind the staff's decision not to advocate a switch to that procedure, including the fact that Thailand had had a stand-by arrangement as recently as 1986, with repurchases falling due through the early 1990s. Also, although Thailand had successfully controlled the growth of its external debt, with a debt of over $20 billion, it was still a significant debtor. Finally, although the staff was projecting that Thailand's medium-term external position would remain manageable, the current account deficit was rising rapidly, so that implementation of the appropriate policies to contain the deficit to manageable levels would be critical. Therefore, switching to the bicyclic consultation procedure at the present juncture would send the wrong signals about the Fund's concern over the policy adjustments that would be needed to maintain a viable external position.

Mr. Kiriwat stated that the Thai authorities agreed with Directors that the growth of domestic demand needed to be curbed. To that end, interest rates had been increased sharply over the preceding three or four weeks without actions to mitigate them by the central bank. Coupled with the low rate of inflation--about 4 percent--the real rate of interest at present ranged between 6-10 percent, which the authorities believed should prove sufficient to slow the economy down and restrain domestic consumption. The authorities realized the importance of keeping watch over domestic demand.

On the fiscal side, the budget for 1989/90 would not have the effect of increasing domestic demand, Mr. Kiriwat noted.

Despite the resistance of the labor unions, the Cabinet had intended to list all five major public enterprises on the stock exchange,

Mr. Kiriwat continued. The process of completing the listing would be finished soon. That decision was a significant step in the gradual process of privatization that the authorities were following. The Cabinet had also decided recently to grant concessions for the construction of two major strategic highways included in the National Economic Plan to the private sector--an unprecedented and significant step. The Cabinet had made it clear that such further measures would be forthcoming, and that their implementation should be expedited.

If Thailand was to grow rapidly in the succeeding four or five years, securing an adequate level of domestic savings would be crucial, Mr. Kiriwat observed. Private savings currently accounted for only 17 percent of GDP, and the authorities were determined to increase it to 20 percent over the following three years. The authorities thus believed that all the necessary mechanisms for the mobilization of savings should be put in place rapidly. In that respect, the design stage for the financial infrastructure had been completed. The authorities hoped that the process of implementation could be speeded, so that the entire financial infrastructure would be in place by the end of 1989.

The authorities believed that with the implementation of the proper financial infrastructure, the introduction of financial instruments, and high real interest rates, domestic savings could be increased, Mr. Kiriwat went on. That in itself would help to contain the current account deficit to 4 percent of GDP--a figure which the authorities took seriously. External stability had proved to be a cornerstone of economic management in Thailand, and had served the country well in the past, so the possibility of slippages in the deficit target would not be entertained.

The possibility of accepting the obligations of Article VIII, Sections 2, 3, and 4 of the Articles of Agreement had in fact been discussed by the authorities, Mr. Kiriwat pointed out; the problems connected with such a move were legal, not practical. If Thailand were to accept the obligations of Article VIII, several clauses in the exchange control laws would have to be amended, which meant that the laws would have to be taken up by the Parliament. There were many items in those laws themselves--which had not been amended in 40 years--that might have to be revised and amended as well. With the help of the Fund's staff the authorities were reviewing the exchange control laws as a whole. When the review was completed, the question of accepting the obligations of Article VIII and the revised exchange control laws would be taken up together, first by the Cabinet, and then by the Parliament. The chances for success would be greater if those two matters were considered as a whole by the Parliament.

The authorities had not lost sight of the fact that income imbalances still existed in Thailand, Mr. Kiriwat remarked, and they realized that ways and means should be found to disperse equitably the benefits of growth to the entire population. However, the authorities did not believe that the Government should be the motivating force behind such a development. Rather, the intention was to create the opportunities for the

private sector--both financial and nonfinancial--to move into the rural areas and, by providing the infrastructure, to fulfill the aim of a wider dispersal of national wealth.

One Director had observed that, despite the high rate of growth of exports, the valued added of exports should be increased in order to deal with the increase in imports, Mr. Kiriwat recalled. To that end, Thailand had declared an open trade policy--in a small way--with the countries of Indochina. Serious negotiations were currently under way for a free exchange of goods between Thailand and the Lao People's Democratic Republic, to secure raw materials from the Lao People's Democratic Republic for export and to further the development of joint ventures. The Thai authorities were aware of the weaknesses in the structure of exports and imports.

The Thai authorities considered that the Article IV consultation discussions with the Fund staff were special occasions, Mr. Kiriwat concluded. They presented an opportunity for a lively exchange of views and stimulating debates on matters of economic policy, and had shaped in no small way the economic policies that were responsible for the success Thailand was enjoying at present.

The Acting Chairman made the following summing up:

> Executive Directors noted with satisfaction the exceptionally strong performance of the Thai economy during 1988, and the excellent prospects for 1989. They noted the contribution of export diversification and improved international competitiveness to the rapid growth, and emphasized the fact that sound macroeconomic policies had allowed the economy to benefit fully from the recent favorable international environment. While the recovery had been led by exports, the contribution of domestic demand had risen sharply in 1988, reflecting not only the continued strength of private investment, but also a recovery in the growth of private consumption. There were now signs of overheating, even though inflation remained moderate. Directors stressed that the main immediate challenge for the authorities was to assure the smooth transition from the present boom to a sustainable path of growth. Directors welcomed the authorities' efforts to ensure that high growth is reflected in rising standards of living for all segments of the population, and all regions.
>
> Directors were of the view that the recent increase in the external current account deficit was manageable, inasmuch as the rise in imports stemmed from a higher level of private investment, direct foreign investment was large, and Thailand's debt profile remained strong. Nevertheless, the widening of the deficit was considered to be a symptom of unsustainably rapid

growth, and it rendered the external position vulnerable to foreign disturbances. Thus, Directors emphasized the need to rein in the growth of domestic demand.

Directors commended the authorities' efforts to restrain domestic demand in 1988, and supported continued restraint in 1989. They welcomed the revised budget projections for 1988/89, which indicated a stronger fiscal position than initially projected. They urged the authorities to aim at a budget surplus relative to GDP at least as large as that in 1987/88. Directors added that a prudent fiscal policy should be supported by adequate restraint of domestic credit creation, and concern was expressed regarding the recent surge in private sector credit demand. Directors also questioned whether, with many interest rates now at their official ceilings, credit policy could be fully effective in restraining demand. Speakers generally held the view that ceilings on interest rates should be raised or removed. With regard to exchange rate policy, Directors broadly agreed with the staff's recommendation that while exchange rate policy should remain flexible, no further depreciation of the baht in real effective terms was needed at present.

For the medium-term, the large increase in investment in infrastructure that would be required to sustain growth was noted, and it was observed that the increasing role of the private sector in providing infrastructure should help ensure the efficiency of investment. Directors emphasized the need to raise domestic savings in order to finance investment without undue recourse to foreign savings. For the public sector, this would require continued vigilance over current expenditures, further efforts to improve enterprise profitability, and to accelerate privatization. For the private sector, Directors supported the Government's intention to broaden the range and enhance the attractiveness of long-term savings instruments. A shift to more market-oriented interest rates should also contribute to an increase in private savings.

Directors noted that structural policies that ensured the efficiency of private sector activities were of the utmost importance. They welcomed the Government's plan to introduce a value-added tax (VAT) in January 1990, and the hope was expressed that coverage of the VAT would be broad. They strongly supported the Government's interest in pursuing tariff reform to lower and narrow the rates of effective protection. They urged the Government to review investment incentives and to ease foreign investment regulations. Directors noted that the authorities had effectively addressed problems that had emerged in some financial institutions in recent years, but urged a continuation of efforts to strengthen the means for dealing with

weak financial institutions. Thailand was again encouraged to accept the obligations of Article VIII status in the Fund.

It is expected that the next Article IV consultation with Thailand will be held on the standard 12-month cycle.

7. ST. VINCENT AND THE GRENADINES - 1988 ARTICLE IV CONSULTATION

The Executive Directors considered the staff report for the 1988 Article IV consultation with St. Vincent and the Grenadines (SM/89/16, 1/27/89). They also had before them a background paper on recent economic developments in St. Vincent and the Grenadines (SM/89/25, 2/6/89).

Mr. Engert made the following statement:

Since the 1987 Article IV consultation, the economy of St. Vincent and the Grenadines has continued to perform well. The economy has grown briskly, at about 5 1/2-6 percent a year. At the same time, inflation has been low, under 2 percent a year. An important contribution to this favorable performance has been prudent macroeconomic management. In addition, important contributions have been made by the efforts to improve the productivity of the economy, particularly in the agricultural and construction sectors. However, unemployment remains high, and is a pressing concern of the authorities.

On the external front, the current account of the balance of payments declined sharply in 1986/87 and in 1987/88 owing substantially to the effects of adverse weather on the production and export of bananas--the key agricultural crop. However, this deterioration was offset by increased capital inflows, and the overall balance of payments again recorded a surplus in 1987/88. Moreover, debt and debt service measurements continue to be low.

On balance, recent economic developments have been impressive, with relatively high unemployment the outstanding difficulty.

The authorities' development strategy continues to be one of fostering private sector initiative through the provision of needed infrastructure and through the prudent management of economic policy. While the staffs of the Fund and the World Bank feel that the Public Sector Investment Program (PSIP) is appropriate, there are valid concerns about implementation capacity, which the authorities share. In response, they have undertaken a wage reclassification scheme to address key personnel shortages in departments responsible for the implementation

of public investment, and have offered fiscal incentives to encourage private sector imports of capital equipment needed to support the PSIP.

The staff report raises concerns regarding the development strategy, including the dependence on banana production and the risk of a possible reduction of preferential access to the U.K. banana market after 1992. The staff also notes that manufacturing development has been hindered by cumbersome administrative procedures for approval and licensing of projects.

For the reasons noted in the staff report, the authorities believe that bananas are likely to remain St. Vincent's principal agricultural export over the medium term. A relevant consideration here as well is the possibility of greater access to the European market in the event of an EC-wide quota. However, my authorities agree that it could be useful to develop a strategy to improve the competitiveness of Vincentian bananas by focusing on the containment of costs, improving quality and yields, and possibly through regional efforts to reduce external marketing costs.

With respect to the concerns that have been raised about the manufacturing sector, a new investment law which will address administrative bottlenecks is being prepared. The authorities feel that the resulting new procedures should make an important contribution to expediting approval and licensing of projects.

The authorities continue to assess the prospects for increased tropical fruit cultivation for the North American market. As the staff report notes, an encouraging sign in this regard is the confirmation by the U.S. Food and Drug Administration that Vincentian tropical fruits are free of fruit fly infestation, and can therefore enter the U.S. market. The authorities also continue to develop the potential in St. Vincent and the Grenadines for up-market tourism.

The staff correctly notes that the fiscal balance has been weakened by increases in personal income tax exemptions, customs duty exemptions and an increase in the public sector wage bill. The authorities believe that the change in the personal income tax was justified in order to reduce the burden of taxation, which was viewed as a disincentive to private initiative and work. The customs duty exemptions also were seen as necessary in order to attract the heavy equipment imports needed to support the PSIP.

The selective wage increases were necessary to improve the management of the public sector and the implementation of the PSIP. At the same time, the authorities are keenly aware of the

need for sound fiscal management, as the record demonstrates. Thus, in an effort to contain the public sector wage bill, the authorities intend to fill only essential vacancies over the near term.

Notwithstanding the recent increases, the fiscal deficit has remained quite small. Looking ahead, the projections prepared by the staff show the fiscal deficit declining by 1990/91, and significant public sector savings. Moreover, it seems likely that the fiscal deficits would be covered by available concessional financing in connection with the investment program, thus removing any risk of domestic bank financing. Finally, the authorities intend to persevere with their efforts to improve tax administration and collection.

In the monetary sector, there has been a steady increase in the banking system's liquidity position. While deposit rates have declined in response, banks have not reduced lending rates correspondingly. In addition, the amount of private sector borrowing for productive purposes has been disappointing. However, the authorities are reluctant to take measures--such as removing completely the tax on deposits--without assurances that such steps would result in improved borrowing terms.

With respect to competitiveness, although real wages seem to have increased significantly, the authorities believe that real wage increases have generally been matched by productivity gains. Furthermore, the real effective exchange rate has decreased considerably from the 1985 peak, and the projections of the balance of payments prepared by the staff suggest that competitiveness is not a concern. Thus, the authorities believe that the current exchange rate is adequate for the time being.

The question of moving from the present 18-month consultation cycle to a 24-month cycle was raised during the recent consultation. However, as explained in the staff report, the authorities would prefer to remain on the 18-month cycle, which they believe has served them well.

The authorities would like to thank the staff for the important contribution that their work has made to economic analysis and policy discussions in St. Vincent and the Grenadines.

Mr. Piantini made the following statement:

The authorities of St. Vincent and the Grenadines should be strongly commended for another successful year in managing their economy. Since 1983, GDP has grown at an average annual rate of 6 percent, in an environment of stable prices. The public

sector is now generating a surplus, as is the balance of payments, and the debt service ratio is marginal. We are in general agreement with the staff appraisal.

Given the importance of fiscal policy to the growth process in St. Vincent and the Grenadines, we share the staff view that some revenue enhancement is appropriate. The authorities will be well advised to consider the staff recommendation for increasing indirect taxes. Additionally, the high unemployment rate and the short supply of jobs might make it necessary for the authorities to provide more support for educational training in order to strengthen human resources, which is so important for enhancing the country's development options.

The authorities are appropriately concerned with the lack of private sector dynamism. Given the small size of the private sector in St. Vincent and the Grenadines, there is a need for more imaginative actions. Despite the increase in bank liquidity, real lending interest rates are still high; therefore, more aggressive lending programs should be implemented through state financial institutions so as to help reduce market rates. This, combined with tax incentives, a streamlining of bureaucratic procedures, and the completion of factory shells, should encourage private investment in the short term. In this context, we welcome the tax exemptions for hotel activities and the reduction of corporate income tax rates on profits from exports that were implemented by the authorities in 1988.

The economy of St. Vincent and the Grenadines, while healthy in the medium term, is still quite vulnerable to external shocks. In this regard, we welcome the public investment program aimed at broadening the productive base of the economy, and also the agreement that was reached by the members of the Caribbean Community (CARICOM) for unifying tariffs on most commodities imported from third countries, which should help to increase efficiency in the allocation of resources. Nevertheless, we would like to caution the authorities that continuation of high wage increases could impair the economy's external competitiveness. Finally, the authorities might give more consideration to developing the country's tourism potential.

Mr. Jarvis made the following statement:

Since the Board's last review 18 months ago (EBM/87/98, 7/6/87), the economy of St. Vincent and the Grenadines has continued to perform well. GDP has grown by over 5 percent, and inflation continues to remain below 2 percent. This is an impressive achievement, and is due to a large extent to the authorities' skill in managing public sector finances.

That said, there are one or two aspects of economic developments in the last couple of years which cause me some concern. The first is the continuation of substantial unemployment, on which I note there are still no statistics, and I would be interested in the staff's assessment of the true extent of the problem. Also, what is the relationship between unemployment and real wages? One would have expected that the recent increases in real wages would have increased unemployment, but there are also some indications that there is a problem with unwillingness to work, or unwillingness to work in the formal economy, because wages are actually too low. The staff report is not entirely clear on this point, and I would be grateful for elaboration.

While fiscal policy appears to be sound, I note the staff's comment that the position has been bolstered by the surplus of the National Insurance Scheme. This surplus cannot be expected to continue indefinitely, and the authorities should not become overreliant on it.

Turning to external policy, I note that the current account deficit increased to 15 percent of GDP in 1987/88, and that there was a substantial increase in imports. Could the staff say a little more about this, and also give the Board some idea about what proportion of the increase in imports is related to the construction of the Cumberland Hydroelectric Power Station? I am also a little concerned that external debt is projected to increase from $37.9 million in 1987/88 to $52 million by 1990/91. Once again, could the staff explain the underlying assumptions?

Prospects for exports of bananas will be particularly important in determining St. Vincent's medium-term prospects. As the staff report points out, the policy of allowing preferential access to traditional suppliers of bananas will ultimately be reviewed by the European Communities. Clearly, the importance of fruit exports to economies like that of St. Vincent will need to be considered carefully in this review.

In the long run, however, it is important that St. Vincent not allow itself to become overly dependent on exports of bananas to Europe, especially as their value to St. Vincent is subject to substantial fluctuations when the exchange rate between the U.S. dollar and European currencies changes. For this reason, we would continue to emphasize the importance of diversification. Clearly, the opportunities for this are limited at present, but perhaps more could be done to encourage it in the future. I would be interested in any comments which the staff has on this.

The fact that the authorities seem to be having considerable difficulty in attracting private sector investment to St. Vincent emerges clearly from the staff's papers. There are some things which the authorities can do in that regard. For example, the dispute regarding compensation for the site of the Diamond estate should be resolved as soon as possible. Since the company involved in the dispute with the Government is itself in the public sector, this should not be impossible. Also, streamlining authorization procedures for new investment applications will clearly be important, and I welcome the authorities' recent moves in this direction. More generally, I would agree with the staff that the authorities' strategy of concentrating on the provision of infrastructure and relying on the private sector to undertake employment-generating activities is the correct one. However, even allowing for the administrative and physical bottlenecks referred to in the report, it is surprising that private sector investment is so low. I would be interested in any comments by either the staff or Mr. Engert.

I have expressed a number of concerns about developments in St. Vincent's economy. However, I would not wish to sound unduly negative. St. Vincent has enjoyed an excellent record of economic growth, and the authorities' financial management has been impressive. I note that the authorities have expressed a preference for remaining on the 18-month cycle. Since this involves less staff resources than the bicyclic consultation procedure--because there are no interim consultations--this seems appropriate. Indeed, it is an example which others might wish to follow.

Mr. Hogeweg stated that he recalled that the staff report had said that there was little scope for monetary and exchange rate policy in St. Vincent and the Grenadines because the country was a member of the Eastern Caribbean Central Bank. That seriously underestimated the work of the common central bank, which conducted such policies, although on behalf of not only St. Vincent and the Grenadines. In fact, an advantage of such a common central bank was that it was truly independent of government, and therefore might be in a stronger position to conduct monetary policy.

The staff's contention that the present level of the exchange rate appeared adequate in light of the real effective depreciation that had taken place since 1985 turned the argument on its head, Mr. Hogeweg observed. The fact that the authorities had weathered well the period when the anchor for their common currency went up by following prudent fiscal and financial policies which kept inflation low and protected the economy's competitiveness should be appreciated.

The large margin which existed between lending and deposit rates appeared to be very detrimental for St. Vincent and the Grenadines, Mr. Hogeweg concluded. The margin was too large to be explained by the

tax on deposits. He would appreciate some elaboration as to why competition in the banking system was so low, and what could be done about it.

Mr. Fogelholm stated that he was aware, like Mr. Jarvis, that in some cases the bicyclic consultation procedure might involve an increased use of staff resources. However, he understood that there were some countries that were on a true 24-month cycle, with no interim consultation in between. Perhaps that alternative might be explored for St. Vincent and the Grenadines.

The staff representative from the Western Hemisphere Department stated that although there was currently a small job training program in place funded by the U.S. Agency for International Development (USAID), the experience of the Vincentian authorities had been that the domestic manufacturers were not very interested in it. The shortage of skills was not in itself a constraint on employment, because the manufacturers preferred to give their employees on-the-job training themselves.

St. Vincent and the Grenadines suffered from a number of disadvantages that hindered its potential for tourism development, the staff representative continued. Very high levels of investment would be required in tourism infrastructure, such as airport facilities, the development of connections between St. Vincent and other Caribbean islands, and hotels. Undertaking the investment that would be required to make St. Vincent competitive in tourism with Barbados--the nearest alternative market--would mean a large expansion in external debt, which the authorities were reluctant to contract. The existing program of small airport construction would not relieve the constraints on tourism development.

No survey of unemployment had yet been made in which the authorities had any confidence, the staff representative went on. Statistics for unemployment of between 20 percent and 40 percent of the labor force had been brought forward, but the authorities did not adhere to any hard figure in that regard. Although real wages had risen, it appeared that the rise was currently moderating, with beneficial effects on unemployment. However, a related factor in the unemployment situation that was not captured in the statistics appeared to be the fact that Vincentian expatriates employed abroad remitted significant amounts of resources for the support of their relatives back home--certainly to a far larger extent than could be discerned from the balance of payments statistics. That support tended to affect the willingness to work. In that regard, it might be said that wages were too low, but the problem would persist as long as about 100,000 Vincentian expatriates working abroad remitted resources home.

The authorities were not particularly concerned about the surpluses that had been accumulating in the National Insurance Scheme, the staff representative remarked; however, in the staff's view, the surpluses

should not act as a disincentive to the authorities to mobilize additional revenues domestically. Those surpluses should not be relied upon to finance public capital investment for much longer.

Although the current account deficit had widened over the previous two years, the staff expected it to be reversed, the staff representative stated. Banana exports, which had declined over that period, were expected to recover. Also, imports had increased because of capital investment associated with the Cumberland Hydroelectric Power Station, which was close to completion. Thus, the level of imports was expected to moderate.

External debt was projected to increase in line with the commitments to the Public Sector Investment Program (PSIP), which was fully funded up to 1990, the staff representative continued. It was expected that the level of external debt would grow in line with the disbursement rate--which in the recent past had been 65-70 percent.

There was indeed a problem of financing of private sector investment, the staff representative commented. The commercial banks' liquidity had risen partly because the banks were reluctant to lend to the private sector on a medium-term basis. According to the banks, there was a scarcity of well-prepared bankable projects. To deal with that situation, the authorities were considering expanding the role of the development corporation in providing assistance to private investors for project preparation, as well as in increasing its lending to the private sector.

A new investment code was being drafted that would lead to a simplification of the rules for reviewing and approving applications, and would remove some of the delays and administrative bottlenecks that had arisen in the past, the staff representative noted. Responsibility for approving applications would lie with one government unit in the future.

The Eastern Caribbean Central Bank (ECCB) maintained statutory limitations on lending to individual governments, the staff representative observed. The public sector in St. Vincent had not had to borrow from the commercial banks, because most capital spending was financed externally, and the current account savings of the public sector had been substantial--although they had declined recently.

He agreed that the exchange rate was adequate because fiscal policy had been tight, the staff representative noted, but the staff was not unaware of the connection between them. The prudent fiscal policy of the authorities had made possible the appropriate exchange rate which prevailed at present.

The spread between lending and deposit rates had widened because the rate on deposits had fallen in response to the buildup of liquidity, while lending rates had remained sticky, the staff representative concluded. The private sector had become more liquid, the level of deposits

in the banking system had increased, and given the lack of bankable projects, the banks would have been unable to increase their lending significantly, even if lower lending rates had prevailed.

Mr. Engert stated that moving to the bicyclic consultation procedure for St. Vincent and the Grenadines would be significantly more costly in terms of staff resources, because for a country like St. Vincent there was not much difference, in terms of the amount of background work the staff needed to do, between an 18-month cycle and a bicyclic consultation procedure. Also, the bicyclic consultation procedure might overtax an already overburdened public management team in St. Vincent and the Grenadines. For those reasons, moving to the bicyclic procedure was probably not the right step at present.

The intention originally had been to consider moving to the 24-month cycle, given the authorities' good track record and prudent management, Mr. Engert continued, but some potential problems had shown themselves. For example, the banana market was a potential problem, as was the authorities' reliance on the National Insurance Scheme, as well as some uncertainty about external aid. Also, a significant number of loans outstanding to St. Vincent would begin to be amortized in the early 1990s, and the situation would need to be closely monitored. Given those considerations, the authorities believed it advisable to stay on the 18-month cycle, which was consistent with their prudent approach to economic management. The issue could be brought up again at the time of the next Article IV consultation with St. Vincent and the Grenadines, and depending on the developments over the following 18 months, moving to the 24-month cycle might be reconsidered.

The Acting Chairman made the following summing up:

> Executive Directors were in general agreement with the thrust of the staff appraisal.
>
> Directors noted that the overall economic performance had been satisfactory in recent years, pointing to the high rate of GDP growth, the low rate of inflation, and the balance of payments surpluses. Directors attributed many of these developments to the prudent policies that the authorities had followed. Nevertheless, Directors observed that areas of concern remained; unemployment was substantial, the productive base was narrow, the balance of payments remained vulnerable to exogenous developments, and the current account deficit was large in relation to GDP.
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> Against this background, Directors expressed support for the authorities' development strategy of promoting private sector activity, and encouraged them to broaden and diversify the productive base of the economy. They expressed concern, however, about the sluggishness of domestic private investment in manufacturing and tourism activities.

The authorities' commitment to prudent fiscal policies was welcomed, although it was noted that the fiscal position had been weakened in the current year. Directors agreed with the staff's recommendation that the underlying fiscal position be strengthened by increasing consumption taxes and licensing fees, and by raising user charges for public utilities. Directors also urged the authorities not to rely on the surpluses of the National Insurance Scheme. Directors cautioned that wage adjustments should be made within a framework of overall containment of the wage bill.

Directors agreed that the international competitiveness of bananas needed to be improved in anticipation of the possible decline in preferential access to the traditional U.K. market. On the exchange rate, it was noted that the authorities worked in conjunction with other members of the Eastern Caribbean Central Bank; although the adequacy of the exchange rate at present was not questioned, one speaker indicated that it was important to control wages so that competitiveness could be maintained.

Directors recommended that the next Article IV consultation with St. Vincent and the Grenadines be held on the current 18-month cycle.

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/89/24 (2/27/89) and EBM/89/25 (3/1/89).

8. EXECUTIVE BOARD COMMITTEES - NOMINATION

The Executive Board approves the election of the Executive Director nominated by the Acting Managing Director to assume the vacant position on the Committee on Administrative Policies and on the Committee on Interpretations, as set forth in EBD/89/61 (2/24/89).

Adopted February 27, 1989

9. ASSISTANTS TO EXECUTIVE DIRECTORS

The Executive Board approves the appointments of Assistants to an Executive Director as set forth in EBAP/89/51 (2/23/89) and Correction 1 (2/24/89).

Adopted February 28, 1989

10. APPROVAL OF MINUTES

The minutes of Executive Board Meetings 88/130 through 88/132 are approved. (EBD/89/55, 2/21/89)

Adopted February 27, 1989

11. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors as set forth in EBAP/89/52 (2/24/89) and EBAP/89/53 (2/27/89) and by an Advisor to Executive Director as set forth in EBAP/89/52 (2/24/89) is approved.

APPROVED: September 7, 1989

JOSEPH W. LANG, JR.
Acting Secretary