

INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 87/168

10:00 a.m., December 11, 1987

M. Camdessus, Chairman

Executive Directors

A. Abdallah
Dai Q.
C. H. Dallara
J. de Groote
A. Donoso
M. Finaish
G. Grosche
J. E. Ismael

T. P. Lankester
M. Massé
Mwakani Samba
Y. A. Nimatallah
G. Ortiz
J. Ovi
H. Ploix
G. A. Posthumus
C. R. Rye

A. K. Sengupta
K. Yamazaki
S. Zecchini

Alternate Executive Directors

Jiang H.
M. K. Bush

J. Reddy
J. Hospedales
C. Enoch

C. V. Santos
I. A. Al-Assaf

M. Fogelholm
D. Marcel
G. P. J. Hogeweg
C.-Y. Lim
A. M. Hammoudi, Temporary
L. E. N. Fernando
M. Sugita
N. Kyriazidis

L. Van Houtven, Secretary and Counsellor
S. L. Yeager, Assistant

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Also Present

IBRD: E. Grilli, Office of Senior Vice President - Operations. African Department: E. A. Calamitsis, Deputy Director; N. Abu-zobaa, P. A. Acquah, J. Artus. Asian Department: W. M. Tilakaratna. European Department: E. O. C. Brehmer, J. J. M. Kremers. Exchange and Trade Relations Department: L. A. Whittome, Counsellor and Director; J. T. Boorman, Deputy Director; S. J. Anjaria, M. W. Bell, S. B. Brown, B. Christensen, H. Hino, H. B. Junz, S. Kanesa-Thasan, M. Nowak, R. L. Sheehy. External Relations Department: R. J. Bhatia, P. C. Hole. Fiscal Affairs Department: V. Tanzi, Director; A. A. Tait, Deputy Director. Legal Department: F. P. Gianviti, General Counsel; W. E. Holder, Deputy General Counsel; R. H. Munzberg. Middle Eastern Department: M. D. Knight, M. Yaqub. Research Department: I. Otani, I. Ul-Haque. Secretary's Department: C. Brachet, Deputy Secretary. Treasurer's Department: T. Leddy, Deputy Treasurer; D. Williams, Deputy Treasurer; J. E. Blalock, K. Boese, G. M. Fitzpatrick, D. Gupta, D. V. Pritchett, G. Wittich. Western Hemisphere Department: S. T. Beza, Director; J. Ferrán, Deputy Director. Personal Assistant to the Managing Director: H. G. O. Simpson. Advisors to Executive Directors: A. A. Agah, P. E. Archibong, M. B. Chatah, A. G. A. Faria, Khong K. N., A. Ouanes, P. D. Péroz, G. Pineau, N. Toé, A. Vasudevan. Assistants to Executive Directors: N. Adachi, J. R. N. Almeida, H. S. Binay, R. Comotto, F. Di Mauro, W. N. Engert, S. K. Fayyad, V. J. Fernández, M. Hepp, G. K. Hodges, L. Hubloue, S. King, V. K. Malhotra, T. Morita, C. Noriega, J. K. Orleans-Lindsay, W. K. Parmena, S. Rebecchini, A. Rieffel, V. Rousset, G. Schurr, B. Tamami, C. C. A. van den Berg, R. Wenzel.

1. STRUCTURAL ADJUSTMENT FACILITY - ENHANCEMENT OF RESOURCES -
PROPOSED FINANCIAL AND OPERATIONAL ARRANGEMENTS

The Executive Directors considered staff papers on operational arrangements governing the enhancement of the structural adjustment facility (EBS/87/245, 11/25/87; and Cor. 1, 12/3/87) and on legal documentation to give effect to the proposed enhancement (EBS/87/253, 12/2/87; and Sup. 1, 12/9/87). They also had before them staff papers discussed previously in Executive Board Informal Sessions 87/5 and 87/6 (11/13/87) and Informal Sessions 87/7 and 87/8 (11/20/87), on proposed financial arrangements (EBS/87/228, 10/29/87; and Sup. 1, 11/11/87), and on considerations relating to access and monitoring procedures under the enhanced facility (EBS/87/230, 11/9/87; and Cor. 1, 11/16/87).

The Deputy Director of the Exchange and Trade Relations Department remarked that discussions had recently been held with some potential contributors to the enhancement of the structural adjustment facility, notably, with the Saudi Arabian authorities, who were considering possible bilateral lending in association with the enhanced facility. The modalities of that lending had not been decided, and it was therefore not fully reflected in the draft Instrument. For example, Section III, paragraph 4(b) referred to the effect of parallel lending on calls on commitments to the Trust. Modifications to that paragraph and a few others, as necessary following the conclusion of discussions on bilateral lending, would be brought to the Board for consideration.

Mr. Nimatallah remarked that that procedure would be agreeable to his authorities. He wondered whether, in the event of a delay in concluding discussions between his authorities and the Fund staff, the provisions for parallel lending could be adopted as an Annex to the Instrument, so that the operations of the facility could commence as soon as possible.

The staff representative from the Legal Department commented that the procedure to be followed depended on the substance of further discussions on parallel bilateral lending. It was hoped that the modalities could be incorporated in the Instrument, but they would first have to be considered by the Executive Directors.

Mr. Abdallah made the following statement:

As beneficiaries of the enhanced structural adjustment facility, my authorities are grateful to management, lenders to the Trust, and the staff, who together have helped to translate the Managing Director's appeal into reality within a very short period. In this connection, we sincerely urge all other potential lenders who have so far not responded to do so by the end of this month so that the enhanced facility will commence in January with adequate resources. Let me also take this opportunity, on behalf of my authorities, to thank China for abstaining from the use of this facility so that it can further assist other eligible developing countries.

It is by now obvious that orderly adjustment in the low-income countries cannot take place without growth. When the debt crisis began in the early 1980s, it was widely believed in creditor countries and some multilateral financial institutions that adjustment could be achieved through a policy of austerity. The record of several years of adjustment shows that programs based on austerity have succeeded in improving the current account position of indebted countries, mainly through a reduction in imports accompanied by a fall in the share of investment in GDP. Clearly, such an outcome is not conducive to economic stability as adjustment programs, to be successful, must be strongly growth oriented. It was this new awareness that led to the creation of the structural adjustment facility. Its purpose was to expand the Fund's traditional approach to adjustment, with a conscious effort to make growth an integral part of the adjustment matrix. The enhanced facility cannot but be seen as a further manifestation of the Fund's commitment to proceed in this direction. To be sure, there is no given input of policy mix that can be associated with a unique outcome of economic growth. But this is not the issue. The crucial point is that for a large majority of developing countries, there can be no such thing as undue oversteering of the pursuit of growth targets. I must therefore emphasize, as I did in the informal sessions of November 20, 1987, that my authorities attach the highest priority to the formulation of programs geared, at a minimum, to arresting the decline in per capita income in their countries.

We frankly see no strong reason for a major departure from the structure and operational modalities of the existing structural adjustment facility. While noting staff justification for maintaining two parallel facilities at least until mid-1988, since eligible countries had been given to understand that they had access to the existing facility until that time, I feel that the enhanced facility, which will enter into effect in January 1988, could retain essentially the same structure without added complexities and conditionality. I note the staff's categorical assertion that users will under no circumstances be eligible to draw simultaneously on the resources of the existing facility and the enhanced facility. Presenting eligible members with such mutually exclusive options only reinforces our impression that too much emphasis is being given to the financial considerations underlying the two facilities at the expense of the essential purpose for which the structural adjustment facility was established. Whether it is the enhanced facility or the existing facility, the purpose is to finance midterm structural adjustment in low-income countries. If this is the case, then the issue is not to choose one or the other arrangement but to see how the total pool of available concessional resources can be utilized most constructively. Accordingly, we feel strongly that it would be a mistake to construe programs under the existing structural adjustment facility arrangements as ineffective simply

because they do not carry the same conditionality and monitoring procedures as those proposed under the enhanced facility. We therefore call for the simplification of the structure of the enhanced facility to keep it in line with the existing facility. This will considerably facilitate the transition to the advantage of many eligible countries willing to undertake feasible structural adjustment programs. However, if somewhat higher conditionality under the enhanced facility is considered necessary by the majority of the Board to underscore the strength of the adjustment program as a basis for access to more resources, then following the cutoff date for the existing facility and the resulting transfer of the undisbursed resources of the Special Disbursement Account to the enhanced facility, borrowing by members under the enhanced facility, in proportion to their eligible claims to Special Disbursement Account resources, should continue to bear the same conditionality as under the existing facility. In that case the two facilities could be effectively maintained and countries could be permitted to draw simultaneously under both facilities until the expiration of the existing structural adjustment facility. Thereafter, the enhanced structural adjustment facility might be envisaged as a facility with a lower tranche representing the entitlement and conditionality under the original facility and an upper tranche with relatively more but not excessive conditionality.

All of us fully realize that the solution to the deep-rooted economic problems facing our countries lies in adopting strong comprehensive structural adjustment programs. Many low-income countries in Africa have been and are implementing comprehensive adjustment programs and have, in fact, made substantial progress in reducing financial imbalances. The question, therefore, is not the need for conditionality and adjustment but rather the need for appropriateness and realism, to avoid the formulation of overambitious programs with complex features and monitoring procedures that will only undermine the political sustainability of adjustment and create further credibility problems for the authorities as well as the Fund. When dealing with structural adjustment programs supported by arrangements, the Fund must make an effort to extricate itself from the standard stand-by concepts and procedures because the problems of growth through structural adjustment, to which programs supported by the facility are addressed, do not lend themselves neatly to the fine tuning that might otherwise be appropriate for an adjustment strategy relying on the short-term manipulation of financial variables.

The proposed structure of the enhanced facility is complex in terms of the quarterly benchmarks, midyear reviews, performance criteria, semiannual disbursements, and prior actions. We are convinced that what the existing facility needed to achieve its objectives was the addition of resources, and not the intensification of complexities and conditionality. While we understand

the creditors' concern that the resources they provide should be safeguarded to secure their repayment, it is important to stress that the real safeguard is the resumption of growth and improvement in the payments capacity of users of the facility, as well as the guarantees provided by the Trust. This is a matter of genuine concern to both the creditors and the users and, indeed, that is why we need a modus operandi which meets a broader consensus. In this connection, it is noted that at the informal session on November 20, 1987 all potential users of the enhanced facility expressed reservations on the proposed complex procedures and excessive conditionality. It might be useful therefore to highlight the areas where simplification could render the enhanced structural adjustment facility more useful in assisting my authorities in pursuit of their objectives.

In view of the conditions in low-income countries with regard to data base and personnel resources, we recommend that benchmarks should be limited to key supply-side variables monitored on a semiannual basis because programs supported under the facility are more geared to growth than is the case with traditional adjustment programs. I believe that this is the same concern which prompted U.S. Treasury Secretary Baker to propose replacing the quarterly performance criteria under Fund programs with semiannual growth-oriented variables with the aim of reducing the focus on short-term targets and increasing the emphasis on structural policies for growth and stability. The nonobservance of midyear benchmarks would serve as early warning signals to the authorities that the program required prompt reinforcement in order to attain the annual targets. We do not agree that midyear benchmarks should be turned into performance criteria to trigger semiannual disbursements nor do we support quarterly benchmarks.

We strongly recommend annual disbursements under the enhanced facility as under the existing facility. While I have some reservations about a midyear review as it adds to the complexity of operational procedures, its association with semiannual disbursements, in effect, converts all semiannual benchmarks into performance criteria, a potential outcome which greatly concerns my authorities. It has been noted that failure to complete the midyear review in 3-4 months will result in the interruption of the midyear disbursement, something which is likely to occur in many programs and sometimes more than once for the same program. In fact, this means that annual programs will have to be regarded as off track and be renegotiated each time a midyear review is thus delayed. This is not conducive to building a momentum for sustained growth, and it can only serve to undermine the facility's potential for fostering the programs' objectives. Indeed, most of my authorities will find considerable problems with this complex monitoring procedure. One of them has stated that "the intensive supervision outlined, including

half-yearly reviews, will be disproportionately expensive in staff time and liable to cause much ill feeling." Even the flexibility in program extension proposed by the staff to address this problem may not be practical unless the drawdown period can be extended well beyond mid-1992.

We recognize that prior actions should not be ruled out completely as they may be warranted by circumstances. However, it should be stressed that programs supported by the enhanced facility are for tackling structural problems, which take time, and, therefore, prior actions may be called for only in exceptional cases. The insistence on too many prior actions as a condition for programs under the enhanced facility would discourage many eligible countries from benefiting from the facility and therefore render it less useful.

Because of the difference in financing needs of individual countries, which vary considerably in relation to their quotas, we find merit in the recommendation for differential access for the enhanced facility. However, we note the recommendation that within the proposed access limit of 250 percent of quota--and a maximum of 350 percent in a few highly exceptional cases--the overall average will be about 150 percent of quota. While we fully acknowledge that "we need to be careful to protect the availability of resources at appropriate levels for all eligible countries that may qualify for support," judging by the experience under the existing facility, many eligible members may not avail themselves of the facility at the same time. In view of this and the large financing needs of these countries, and noting that these limits apply over three years, we would strongly urge an overall average access of at least 60 percent of quota annually. We also agree that front-loading of disbursements will be called for because structural measures will need substantial financial support at the early stage of implementation before desired results become visible. We, therefore, propose front-loading in the first year up to 40 percent of the total loan for all borrowers, while higher levels would be allowed in exceptional circumstances. The pattern of the second and third-year phasing could be determined at the time of the first annual review of the enhanced facility.

As projected by the staff, even after the injection of enhanced resources in the period 1988-90, some financing gaps may still remain, which could be filled with increased concessional assistance from bilateral and multilateral sources and from other Fund facilities. In this connection, I would like to emphasize that governments of eligible countries expect the resources of the enhanced facility to be in addition to normal flows from bilateral and multilateral sources and do not expect the structural adjustment facility to substitute for their access to other Fund facilities.

We were encouraged by the staff proposals on securing access to the resources of the enhanced facility for members with overdue obligations to the Fund, as long as they had adopted strong comprehensive adjustment programs. In the light of these proposals and the understanding expressed by Directors, as reflected in the Chairman's summing up of the informal session on November 20, 1987, we now expect management and the staff to formulate more focused proposals on this matter to be brought to the Board. In this connection, I have noted that the staff paper on the forthcoming six-monthly review of overdue obligations has not addressed this issue, and we therefore request that a supplement on the matter be prepared to enable the Executive Board to come to a decision on this subject at the time of that review. One possibility that was mentioned is the use of policy framework papers to solicit exceptional donor support. I fully agree on the important role that these papers can play in aid coordination. However, I would like to underscore two points. First, the policy framework paper should remain a document of the national government as was originally intended, and it is essential therefore that national authorities have the major role in its preparation with technical assistance from the Fund and the Bank. Second, while the importance of donor assistance cannot be overemphasized, it is advisable not to complicate the already complex process further by requiring the participation of all potential donors as partners in the preparation of the policy framework paper.

The discussion in the last informal session indicated that several creditors shared our view with regard to the cutoff date for access to the enhanced facility which now stands at May 1989, to the effect that this cutoff date needs to be extended to accommodate those whose program preparation would not be ready for approval.

I have noted the point raised by the staff on page 4 of EBS/87/245 to the effect that, if the Board adopts semiannual disbursements based on the completion of midyear reviews, then with a mid-1992 completion of disbursements, the extension of the cutoff access date beyond May 1989 leaves little room for subsequent program extensions. This clearly strengthens our case for annual, rather than semiannual, disbursements based on the completion of midyear reviews. However, should the majority not support our recommendation, our alternative suggestion would be that the borrower's subsequent disbursements should be increased sufficiently to absorb the disbursement forgone due to program interruption. If this occurs during the final phase of the program, we would urge the Fund to negotiate with creditors the extension of the drawdown period beyond 1992. I should also stress here that the problems facing countries eligible to use the facility are not likely to disappear over a three-year period--the envisaged lifetime of the enhanced facility. In that

light, we strongly urge the Fund and creditors to consider, at an appropriate time, the extension of the facility to assist eligible countries to complete their adjustment.

Let me now make a few brief comments regarding the Reserve, the Subsidy Account, charges to overdue obligations, and rescheduling of Trust loan repayments.

While establishment of a Reserve in the Trust is rightly intended to give the creditors an additional sense of security, the main protection, as emphasized by the staff, will be the quality and strength of the adjustment programs to be supported by these resources, together with the guarantee given by the Fund as a Trustee in the proposed decision. Moreover, I fully endorse the proposals for funding the Reserve. My authorities' only concern about the funds flowing into the Reserve is that they should continue to be made available as originally intended.

On the Subsidy Account, I fully agree that considerable uncertainty will remain as to the funds that will be required to subsidize interest rates and ensure the effective rate of 0.5 percent per annum. I would therefore support the proposed decision to empower borrowing by the Subsidy Account. In any case, the frequent Board reviews of this issue during the period of the enhanced facility should provide the Fund with the opportunity to decide what action to take in the light of developments, including the possibility of seeking further contributions.

While I can understand the reasoning behind the proposed decision regarding charges on overdue obligations to the Trust, so far as obligations to the existing facility and the 1976 Trust Fund are concerned, our view is that the present level of charges should continue as there has been no change in the cost of the funds which originally financed those obligations.

On the question of rescheduling Trust loan repayments, if repayment on the due date would result in serious hardship to the member, we strongly call for the inclusion of this provision in the decision on the enhanced facility. Such possibilities are indeed present since we are dealing with the lowest-income countries with highly unpredictable balance of payments, depending, as they do, on changing world market situations.

In the light of our views, while we definitely welcome the establishment of the enhanced facility and accordingly support the proposed decision to that effect, we have reservations on those proposed decisions which will make the enhanced facility more complex and intensify its conditionality. Let me highlight the important ones.

We support the draft decision in Attachment A of EBS/87/253 to the extent that it establishes the enhanced facility: however, we have already stated our position regarding the relationship between the existing facility and the enhanced structural adjustment facility.

We do not support parts (2) and (3) of the proposed decision, Attachment B, which would require that disbursements be in semiannual installments after completion of the midyear review. We strongly advocate annual disbursements.

We support the proposed decision in Attachment C establishing the Enhanced Structural Adjustment Facility Trust. However, in accordance with my earlier remarks regarding the cutoff date of May 1989, I hope that appropriate modifications will be made to the stipulated period appearing in Annex to Attachment C, Section II, paragraph 1(d). In the same Annex, paragraph 2(d), it is stipulated that the annual amounts committed to a member shall not be reduced unless balance of payments developments are substantially more favorable. As we pointed out earlier, we do not agree that a commitment should be reduced under any circumstances, otherwise the confidence and certainty needed for the authorities to embark on the implementation of a strong program might be eroded. In fact, I recall that it was generally agreed in the last informal session that, rather than formally reducing the commitment under such circumstances, the member would be informally requested to abstain from drawing. We would, therefore, request that this part of paragraph 2(d) be deleted.

In view of the request for creditors' flexibility on the drawdown period to be extended beyond June 1992, we feel that the proposed decision in Annex to Attachment C, Section II, paragraph 3(b), restricting the disbursement period, should be deleted.

We support the proposed decision in Attachment D.

Mr. Lankester made the following statement:

My authorities recognize the special plight of debt-distressed countries, particularly in sub-Saharan Africa. Many of these economies are simply too impoverished to be able to maintain, or in some cases resume, external debt service payments without exceptional assistance from the international financial community. The need to offer constructive solutions prompted the Chancellor of the Exchequer to propose that exceptional rescheduling of official debt within the Paris Club should be made available on extended and concessional terms to low-income countries seeking to pursue strong adjustment efforts. In addition, this chair has strongly supported the proposals to

increase cofinancing associated with World Bank programs and the Managing Director's initiative to triple the resources of the structural adjustment facility.

The staff proposals on the enhanced facility are well conceived. The staff is to be congratulated on its thoroughly professional and expeditious work in realizing the framework for the Managing Director's proposal. My chair offered fairly detailed comments on various aspects of these proposals in the informal sessions of the Board. In this statement, I seek to restate our general support and to add emphasis to the importance of certain aspects, particularly in the light of comments raised by other chairs in the informal sessions. I am content that this discussion should satisfy the requirement for a review of the existing facility and that we should address access under the third year of existing arrangements by September 1988.

On the objectives of the enhanced facility, I welcome the staff recognition of debt as a key element in balance of payments financing needs, particularly as elaborated on pages 5 and 6 of EBS/87/230. My authorities would be keen to pursue an even more structured approach, but we recognize the multidimensional nature of the problem facing the poorest debt-distressed countries and the consequent need for some case-by-case flexibility in determining access. At this stage, I would only seek to argue that the staff, in explaining the access proposed for individual members, should include and clearly articulate the importance given in each case to selected and comparable indicators of debt service. We are not pursuing a mechanistic link or rigid formula but would argue that transparency in staff recommendations is an essential requirement for the Board to operate effectively in all matters. I should emphasize also that, in addition to debt factors, my authorities strongly support the objective of focusing the enhanced facility on those members undertaking adjustment programs of a strength and quality that justify such additional concessional financing.

I think it is important to be absolutely clear from the start that the enhanced facility should not be used artificially and unsustainably to try to achieve preset growth targets. The results of the staff's simulations given in Appendix I of EBS/87/230 should not be seen as targets: they are only theoretical indications. The enhanced facility is designed to promote a medium-term strategy of structural adjustment complemented by policies to restore macroeconomic stability. Only a mutually supporting approach of this sort can offer a realistic possibility of sustainable growth and balanced development. However, as experience has amply demonstrated, the success of medium-term adjustment programs requires rigorous implementation. It is crucial, therefore, that the conditionality applied under the enhanced facility must address the reality of the economic

problems confronting members. Specifically, it must be tailored to achieving necessary medium-term balance of payments viability within the time frame of programs or, in exceptional cases, to achieving substantial progress in that direction. Enlarged resources under the structural adjustment facility will be available for only a limited time. At the end of a program supported by the enhanced facility, therefore, a member must have adjusted back to a position which is sustainable on the basis of the normal financing that can realistically be expected over the medium term. This objective is particularly important, in view of the need to ensure the security of claims on the Trust, which means that assured repayment is the irreducible minimum. However, the ability to repay without undue strain is not a narrow objective; it will be a clear measure of the broader success of the enhanced facility.

Of course, the enhanced structural adjustment facility should achieve more than just repayment. I therefore welcome the intention of the staff to seek more ambitious adjustment, and attach particular importance to the objectives set out in page 6 of EBS/87/230--the substantial relaxation of external restrictions, the clearance of arrears, and the normalization of relations with creditors. These are, of course, essential objectives for all Fund assistance.

The staff's proposals to direct a substantial element of enhanced structural adjustment facility financing toward the buildup of reserves is particularly welcome. The thinness of members' reserve cover has made a number of Fund-supported programs rather fragile. It is important, however, that augmented reserves are used appropriately, and it is desirable that levels are broadly maintained over the medium term. Application of the various "preventive" measures developed by the staff will be very helpful, and I note the recent successes that have been achieved with the use of the SDR in assisting members' reserve management. I would suggest that some measure of an adequate reserve level be incorporated in an indicator of performance under the enhanced facility. We would caution against the temptation to trade a higher reserve target for some temporary boost to growth.

On the relationship between the existing facility and the enhanced facility, the staff does itself an injustice in suggesting that its proposals are unduly complex: certainly, these are no more complex than the situation they must address, including the need to honor the Fund's commitment on maintaining access to the existing facility. It would, of course, be neater to have a single facility or to use the enlarged facility to provide an upper tranche or second window to the existing facility but, all things considered, I doubt that these alternatives are in fact feasible; the staff's proposal is probably the simplest.

On the proposed cut-off date of May 1989 for the existing facility, my authorities would not seek to stand against any consensus among contributors for some extension; but, as a first choice, we are inclined to stick with the proposed date, in order to encourage conversion from the existing facility to the enhanced facility as soon as possible and to minimize the scope for unfairly maximizing total access from the two facilities.

For the same reason, I have some reservations about the proposed right to cancel an arrangement under the enhanced facility and move back to the existing facility, notwithstanding the fact that this would only be allowed before the cut-off date. In practice, this possibility may not be important; but, it would do no harm to regularize the situation by precluding reversion to the existing facility. I would also like to endorse the staff proposal that the cancellation of an arrangement under the existing facility before the end of a program year in order to convert to an arrangement under the enhanced facility should be exceptional, and must be reflected in a suitable adjustment of additional access.

On eligibility and qualification for the enhanced facility, I wish to take this opportunity to extend my appreciation to China for its generosity in deciding to abstain from drawing on the enhanced facility. Like other Directors, I believe it would be reprehensible if this exemplary act were to be used to disqualify China from other sources of concessional assistance.

As for access and phasing, my authorities regard differential access as an essential element of the enhanced facility, given their concerns to support low-income, debt-distressed countries undertaking adequate adjustment programs. It is difficult to believe that uniform access would have commanded the same support from contributors.

I have no difficulty with the staff proposals for cumulative access limits of 250/300 percent of quota, provided these are used as limits and are not interpreted as entitlements. In this respect, there are good arguments for having a single limit of 250 percent, without quantifying the margin of exceptional access. A multiplicity of limits--not least the suggestion of a 250/300/350 percent system--is not desirable, as it grades access with a precision that might tend to encourage expectations of entitlement. I cannot support a 350 percent super ceiling to be activated only by suggestion of the Executive Board: the recommendations of management and the staff would seem to be the most efficient starting point for Board decisions. Moreover, given that exceptional should mean just one or two cases, I wonder whether a definition of highly exceptional access is not redundant. A 250/350 percent system may not be a desirable alternative, as the 350 percent ceiling might unduly inflate

expectations in cases of exceptional access. Subject to the staff's proposed limit on front-loading--which is an important safeguard--further annual limits would appear neither necessary nor helpful. All proposed access limits must, of course, be conditional on commensurate financing actually being available to the enhanced facility at the time they are set.

I welcome the staff's proposal for annual reviews of individual maximum access limits. I can accept the suggestion that a reduction in the access indicated in the second and third years of an arrangement under the enhanced facility should only be considered where there is a substantial improvement in a member's external position, and would endorse Mr. Nimatallah's suggestion that members should be encouraged to withdraw voluntarily.

This chair has expressed concern previously at the suggestion that general resources might be used in conjunction with the resources of the enhanced facility. Given that the purpose of the enhanced facility is to meet low-income members' needs for concessional resources, qualification to use the facility's resources would suggest prima facie that the member is not in a position to use the Fund's general resources. Perhaps, there will be some cases where it is appropriate for a member to have access to both the structural adjustment facility and general resources, but we will want to look at such cases extremely carefully and would regard such combinations as exceptional. General resources should not be used just to fill financing gaps: such usage should be unnecessary in view of the enlargement of the structural adjustment facility. Where use of general resources is proposed for members eligible to use the existing facility, the time frame of the adjustment program being supported must reflect the terms and costs of the general resources involved.

The degree and direction of conditionality suggested by the framework proposed for the enhanced facility by the staff is strongly endorsed by my authorities. Not only is adequate conditionality an incentive in the best interests of adjusting members, but it is the most fundamental safeguard for creditors. As I have noted earlier, the conditionality applied under the enhanced facility--and, indeed, with respect to use of all Fund resources--must normally be commensurate with the need to achieve medium-term balance of payments viability within the program period.

I must emphasize that prior actions should not be regarded as exceptional. They are fully justified by the availability of disbursements at the very start of programs. Specification of such measures should depend on the scale of the member's problems and its previous record of implementation. Prior actions should

be mandatory where there is any degree of front-loading in disbursement. The test of prior action will be a vital safeguard for the security of the Trust.

On monitoring, my authorities welcome the staff proposal for semiannual disbursement and midyear reviews with the use of a few quarterly financial benchmarks as monitoring aids and some semibenchmarks as performance criteria. Greater specification of structural benchmarks and the use of such indicators in the outlying years of an arrangement under the enhanced facility are also very welcome. I attach particular importance to the idea of a midyear review; this will provide an important degree of flexibility in monitoring, and will resolve some of the problems that have been experienced with the existing facility in synchronizing program and fiscal years. I can broadly agree with the staff's suggestion that reviews be bypassed for small arrangements under the enhanced facility and where there is negligible uncertainty about the achievement of program targets, but this provision must be used very prudently. It is to be hoped that serious divergences from quarterly benchmarks will trigger urgent consultations with a view to putting programs supported by the enhanced facility back on track so as to avoid interruption at the stage of midyear reviews or annual renewals.

I can support the staff's proposal for an annual review of the enhanced facility.

On the treatment of members in arrears, the use of the enhanced facility by members in arrears to the Fund raises difficulties for my authorities, not least because of the need to assure contributors of the future security of claims on the Trust. At this stage, I believe our primary objective must be to launch the enhanced facility without further delay, and I therefore endorse the suggestion of the Managing Director that the issue of access for members in arrears should be addressed within the context of the six-monthly review of overdue obligations to the Fund. This review would provide an appropriate opportunity for the systematic consideration of the arrears problems.

We do not favor the suggestion that some provision could be made in the enhanced facility for rescheduling. The fact that temporary borrowing will finance the enlargement of the facility, rather than a permanent endowment from resources such as gold-sale profits, is an obvious limitation. I would also not be keen to erode the endowment of the Special Disbursement Account by tapping it for subsidy payments for rescheduled borrowing under the enhanced facility; and higher interest charges for borrowers forced to seek rescheduling seems inappropriate. The general preference of my authorities is that, where a member with obligations to the Fund--or in this case, the Enhanced

Structural Adjustment Facility Trust--encounters repayment difficulties, it should refinance its obligations within a new Fund-supported program of adjustment. No subsidy should be paid on overdue obligations to the enhanced facility: this would unfairly deprive borrowers remaining current in their repayments of a share of their subsidy, or would have to be financed from Special Disbursement Account capital.

My authorities endorse the staff's proposals on the interest rates to be charged on overdue payments to the Trust. We can support the preparation of policy framework papers for members in arrears and feel that the proposal to include lead donors in the preparation of policy framework papers for such members is an appropriate and desirable development of this instrument.

As negotiations with other potential contributors are at an advanced stage, I will limit my comments on financing of the enhanced facility to a few points.

First, while capital contributions should legitimately receive market-related rates of interest, it is inappropriate for any lending by creditor members to the Fund, in its own right or as Trustee, to be charged at a fully commercial rate. Previous rates of return on lending to the Fund--based on three-month, six-month, and five-year SDR-weighted domestic interest rates--have proved generally acceptable to date, and we are unconvinced that any enhancement or risk premium is justifiable.

Second, my authorities recognize that some members might have institutional difficulties in denominating their lending in SDRs and, in principle, would wish to accommodate arrangements necessary to overcome such problems, especially if it is possible to avoid the Trust having to undertake hedging operations. The proposals in Supplement 1 to EBS/87/253 could be helpful. A final decision, however, must depend on the likely cost of the covered interest rate. Whatever the outcome, it will be necessary to ensure that the rate of interest on lending under the enhanced facility reflects fully the cost of financing against the available subsidy contributions: a rate of 0.5 percent per annum is the objective of the facility, but first it will be necessary to be sure that the resources of the Subsidy Account are adequate.

Third, we would question the proposal that a transferee of claims on the Trust should only receive the three-month SDR-weighted interest rate given that the transferor could be receiving a higher rate of interest. It would seem more equitable if the transferee was to receive from the transferor the same remuneration as the latter receives from the Trust whenever this was higher than the three-month SDR interest rate. Alternatively, the rate of return should be negotiable between transferor and transferee.

Fourth, I wish to express the strong hope that every member of the Fund who is not a likely beneficiary of the enhanced facility will make every effort to participate in making some contribution to the facility. It is important that, for a scheme of exceptional international assistance, support should be forthcoming from beyond the usual circle of creditors. I also hope that members of the Fund who feel unable at the present time to contribute to the enhanced facility will make a commitment as and when they are able to do so.

The draft decisions, including the Trust Instrument, proposed by the staff appear broadly acceptable. However, I would suggest that the proposed Amendment of the Regulations for the Administration of the Structural Adjustment Facility would be more faithful to staff proposals if it were to read, between subparagraphs (2)(i) and (2)(ii), "and normally" rather than just "or." Similarly, paragraph 1 of Section I: General Provisions of the proposed Instrument to Establish the Enhanced Structural Adjustment Facility Trust understates the purposes of the facility. The more ambitious adjustment advertised for the enhanced facility suggests that programs should aim "to achieve medium-term balance of payments viability, usually within the program period, as a basis for fostering sustainable growth."

Finally, let me repeat my appreciation of the Managing Director's initiative in launching the enlargement of the structural adjustment facility and of the staff's efforts in realizing this proposal. I think we have all been impressed with the skill and energy demonstrated by management and staff. The result is very encouraging, and I believe it can justify the exceptional response made by the contributing members. It will be necessary now to translate these good intentions into reality. I do not underestimate the practical difficulties for members undertaking adjustment under programs supported by the enhanced facility, and such commitments should not be made lightly or without broadly based domestic support. However, I urge low-income members to use the window of opportunity represented by the enhanced facility. A commitment to undertake the more ambitious adjustment which will be facilitated by the significant additional financing offered under the facility is the only realistic solution to overcoming incipient economic weakness, particularly where this is accentuated by an unsustainable debt burden. In view of the urgency of low-income members' problems, I welcome the fact that we seem to be on target for inaugurating the facility on January 1, 1988--in which case, there may be more reason than usual to wish each other a prosperous New Year.

Extending his remarks, Mr. Lankester commented that his authorities strongly supported the general framework of the enhanced facility as proposed by the staff. In the circumstances, it was unlikely that the

framework could have been significantly simplified. The additional funds to be made available through the enhanced facility presented a unique opportunity for low-income, debt-distressed countries to restore some sanity to their external accounts and a renewed momentum to their development efforts. It was imperative that the money be well spent, and therefore he strongly supported the proposed degree of conditionality.

For similar reasons, the proposals for semiannual disbursements, midyear reviews, and other monitoring proposals were entirely appropriate, Mr. Lankester continued. He also strongly favored the concept of differential access, namely, giving special access to those low-income countries that were especially debt distressed, provided that they were undertaking adequate adjustment programs.

He had reservations about the access of members in arrears to the facility, Mr. Lankester commented. He did not agree with Mr. Abdallah that a consensus had been reached at the discussion on November 20 that members in arrears should, in principle, have access to the facility. He agreed with the Chairman that the Board should return to that question in the context of the six-monthly review of overdue obligations. He also agreed that efforts should be aimed at a firm starting date of January 1, 1988 for the facility's operations with an interest rate on loans of 0.5 percent, even if subsidy offers by that date were not sufficient to warrant so low an interest rate. If an adequate amount of subsidy was not eventually forthcoming, Directors should agree that the interest rate would be raised following a review of the facility's operations in June 1988. However, there was absolutely no possibility that the United Kingdom would make any additional subsidy contribution.

The United Kingdom would provide an interest subsidy to the enhanced facility in an amount sufficient, at present interest and exchange rates, to subsidize loans up to SDR 1 billion, Mr. Lankester remarked. That offer was made on the assumption that appropriate contributions would be made by other major countries and that differential favorable access would be given to those countries in greatest need, especially the heavily indebted countries in sub-Saharan Africa. The offer maintained the U.K. position of giving priority to those countries in greatest need and willing to undertake appropriate structural adjustment. The contribution was also viewed as complementary to the Chancellor's initiative for official debt relief. Finally, the contribution would be entirely additional to the United Kingdom's existing planned aid program.

Mr. Mwakani made the following statement:

At this final stage of the process for establishing the enhanced structural adjustment facility, I wish to express our appreciation to management and the staff for their handling of this matter. They have accomplished a remarkable job in a short period of time, and eligible countries in my constituency appreciate their unremitting efforts, the more so, since the initiative for tripling the resources of the structural adjustment

facility will supply the long overdue additional resources that were expected at the time of the establishment of the facility. Also, eligible countries in my constituency appreciate the efforts of those member countries who, despite their own financial difficulties, have found ways to make possible the enhancement of the structural adjustment facility. The countries in my constituency wish to reiterate their gratitude to China for not availing itself of the resources of the enhanced facility.

Since the staff papers on the operational arrangements and on the legal documentation reflect in many respects the general consensus reached at our two informal sessions, I will refrain from repeating our position expressed on the various issues and instead concentrate my remarks on the remaining outstanding issues pertaining to first, the procedures for access and monitoring, and second, the financial arrangements. I shall then propose some amendments to the draft decisions.

First, on the remaining outstanding issues pertaining to procedures for access and monitoring, at the last informal session on November 20, a number of Executive Directors, including myself, found the earlier proposed cutoff date of May 1989 too short and suggested some flexibility to accommodate borrowing countries. I can, therefore, agree that the cutoff date should be set at November 1989 as proposed by the staff. However, for this extension to provide a meaningful flexibility, it would be necessary to extend the cut-off date for disbursements under the enhanced facility. In addition, without a corresponding extension of the cut-off date for disbursements by the Trust, there will be no scope for delays that might occur in concluding mid-term reviews or subsequent annual arrangements in certain cases and as a result, access would be reduced. Such a reduction of access would be detrimental to the implementation of a member country's adjustment program since, in all likelihood, the original access would have been calculated on the basis of a given financing requirement and the strength of the program. I would strongly suggest that for these cases, adjustment should be made to the amount of subsequent disbursements to allow the country to benefit from the full amount of the resources committed under the three-year program.

With regard to access limits, we find the proposed limits-- 150 percent on average, with upper limits of 250 percent and 350 percent of quota--reasonable in view of the limited amount of the facility's resources and we support these limits. However, since the upper limits of 250 percent and 350 percent of quota would apply only in a limited number of cases and in a few highly exceptional cases, respectively, it would be preferable to define beforehand the relevant criteria for these cases. While the balance of payments needs of a member country can easily be expressed in terms of its quota, the determination of the strength of its adjustment program will involve a high degree of judgment.

On phasing, I should say that it is regrettable that my authorities' preference for one annual disbursement upon Board approval of an annual arrangement, as stated during the November 20 informal session, was not retained. Short of the annual disbursement, they find acceptable the staff's proposal that disbursements in the first year should reach 40 percent of the total size of the loan.

Concerning the relationship between the existing facility and the enhanced facility, I am satisfied with the clarification given by the staff. It is important to make a clear distinction between the two facilities so as to preserve the special features of the existing facility and also preserve eligible members' right to avail themselves of the existing facility's resources under the present regulations if they so choose. We are of the view that members using the enhanced facility should be entitled to receive up to 63.5 percent of their quota--representing their share of Special Disbursement Account resources--under the regulations governing the existing facility.

As to the commitment of access, we have difficulties with the staff suggestion that access should be reduced at the time of approval of an annual arrangement or that midyear disbursement should be wholly or partially forgone under circumstances where balance of payments developments proved more favorable than originally anticipated. Despite the perceived improvement in a member's balance of payments position, the attainment of the growth objective would certainly require the maintenance of the loan commitment at the level deemed adequate to satisfy the growth target of the program.

On issues related to the financial arrangements, as I noted at the informal session on November 13, 1987, the Reserve of the Trust should go a long way toward meeting the concerns expressed by lenders. Therefore, I do not think it necessary to take further steps to provide security to lenders' claims.

Concerning the liquidity of claims on the Trust, the staff envisages a temporary suspension of calls by any lender without regard to participation in mutual arrangements for transfers of claims. While we are not opposed to the efforts to ensure the liquidity of claims, we are concerned about the implication of such a suspension of calls on the Trust's obligations toward borrowers, especially where front-loading is required. Similarly, we have difficulties with the provision for temporary encashments of claims by the Trust as it will impair the Trust's ability to provide security to lenders' claims.

On the treatment of overdue obligations in respect of the existing facility and the 1976 Trust Fund, we do not see any compelling reason to alter the treatment of these overdue

obligations. The present level of special charges on the overdue obligations to the existing facility and to the 1976 Trust Fund represent a compromise, and in the absence of significant changes affecting the cost of the Special Disbursement Account and structural adjustment facility resources, we do not think it is appropriate to reopen the debate on this issue.

With regard to the suggested provision for rescheduling obligations to the Trust, we strongly support its inclusion in the Trust Instrument and would agree with the staff's proposal that "the rescheduled amount continue to be subject to the subsidized interest rate and that any cost of the subsidy be borne effectively by the Special Disbursement Account."

As to the interest rates on loans to the Trust, we fully share the staff's view that the enhancement of the structural adjustment facility is an official operation undertaken in the spirit of international cooperation and as such, market-oriented interest rates should not be envisaged. The need to obtain financing that will permit the onlending of funds to borrowers at an effective interest rate of 0.5 percent cannot be overemphasized. It is unfortunate that because some contributors may lend to the Trust at market rates, assurance could not be given to borrowers that interest rates on the Trust loans will remain at 0.5 percent. As we stated at the November 13 informal session, this situation will create uncertainties and complexities regarding the operations of the Trust. It will be of critical importance for the simplification of the operations of the Trust that contributors lend either to the Trust at 0.5 percent or provide donations to achieve an effective interest rate of 0.5 percent.

On the period for notice of call, it is important that we stick to the five business days' notice for call as suggested in EBS/87/228 to avoid penalizing borrowing countries with undue delays between the date of Board approval of an arrangement and the date of release of funds to the country.

On the proposed decisions, the decision in Attachment A needs to be redrafted with a view to bringing out clearly the distinction between the existing facility and the enhanced facility. As is, paragraph 1 gives the impression that the enhanced facility replaces the existing facility.

With regard to the Amendment of the Regulations for the Administration of the Structural Adjustment Facility, such an amendment will not be necessary if the suggestion that the portion of Special Disbursement Account resources to which countries using the enhanced facility are entitled be disbursed under the regulations governing the existing facility is agreeable to the Board.

On the establishment of the enhanced facility, we support the proposed decision in Attachment C. However, we have a number of amendments to the different sections of the Instrument establishing the Trust. First, in Section II, paragraph 1(b), the reference to paragraph 14 of the Regulations for the Administration of the Structural Adjustment Facility should be dropped and the conditions for assistance under the enhanced facility spelled out clearly. We agree that the commitment period should be extended to November 30, 1989. In line with my comments on commitment of access, the last sentence of paragraph 2(d) of this Section should be deleted and an additional provision that "access to the Fund's resources under other policies of the Fund will remain available in accordance with the terms of those policies" should be included. We strongly support the inclusion of the provisions of paragraph 4(c) in the Trust Instrument. Second, with regard to the borrowing for the Loan Account, paragraph 4(c) of Section III should be deleted, since we are not in favor of temporary suspension of calls by lenders not participating in mutual arrangements for transfers of claims. Third, concerning Section IV on the Subsidy Account, we support the maintenance of the last sentence of paragraph 4.

We support the proposed decision in Attachment D on the Transfer and Retransfer of Resources from the Special Disbursement Account to the Trust and back to the Special Disbursement Account.

To conclude, during our informal session on considerations relating to access and monitoring, Executive Directors representing potential users of the enhanced facility found the monitoring and disbursement procedures complex, unnecessarily tightening the conditionality, and imposing an undue burden on both the authorities and Fund staff. My authorities have noted the assurance given in the Chairman's concluding remarks at that session that in the operations of the enhanced facility, administrative and bureaucratic complexities will be avoided. I would suggest that reference be made to this assurance in the summing up of today's discussion.

Extending his remarks, Mr. Mwakani stated that he could go along with the proposed amendment to Section III, paragraph 5(c) of the Trust Instrument. He could also support the additions to Section V of the Trust Instrument as proposed in the supplement to EBS/87/253.

Mr. Ovi, reporting on the status of contributions to the enhanced facility by members of his constituency, remarked that he had recently received from the Minister of Finance for Sweden a firm commitment for a subsidy grant of SKr 600 million, or approximately SDR 75 million, over a four-year period. Swedish legislation did not allow for a capital contribution to an enhanced facility.

In all Nordic countries, grants had to be funded from development budgets, which usually required broad parliamentary approval of expenditures, Mr. Ovi observed. In Norway, the Government was still discussing a commitment to the enhanced facility, but it was unlikely that a decision would be taken before the beginning of January 1988. It had been suggested that the central bank should release SDR 90 million for a capital contribution to the enhanced facility ahead of the decision on the grant element.

He had previously explained the problems encountered by Denmark and Finland in their effort to mobilize resources for the enhanced facility, Mr. Ovi recalled. In both instances, central banks usually participated in cooperation with a development institution, and grants automatically followed. At present, however, the central banks were not satisfied with the modalities for the enhancement of the structural adjustment facility, particularly with respect to the security of claims on the Trust, and they could therefore not commit exchange reserves for that purpose. In Norway, the authorities were looking to other institutions to provide the grant element independently; that time-consuming process might not be completed by year-end. For Finland, a capital contribution was expected, but a subsidy grant was unlikely.

He wished to assure prospective borrowers from the enhanced facility, particularly those countries represented by Mr. Abdallah and Mr. Mawakani, that the difficulties and delays encountered by his authorities were unusual and in no way represented a lack of commitment to the enhancement on the part of his countries or their monetary authorities, Mr. Ovi remarked. The resolution of those difficulties was, at present, beyond the control of his authorities, who were following with great interest the Board's discussion on the modalities of the enhancement, particularly with respect to the security and liquidity of claims on the Trust.

Commenting on the latest staff proposals, Mr. Ovi made the following statement:

On access, the proposed framework for enhanced lending goes a long way toward meeting our concerns that lending to countries eligible to use the facility should be primarily in the form of structural adjustment loans, although I should like some clarification as regards the meaning of "in accordance with existing guidelines."

On monitoring, we are still somewhat concerned about the proposal to use performance criteria instead of benchmarks or possibly midyear reviews in a number of cases. We agree that conditionality under the enhanced facility needs to be tightened. Still, some clarification is needed regarding those instances where performance criteria should be used instead of midyear reviews. In our opinion, performance criteria should be used primarily for countries facing severe adjustment problems, namely, along the guidelines outlined for the use of prior actions.

We can agree to a prolongation of the drawdown period on loan commitments to the Trust until mid-1992.

The staff raises the question whether, in case of serious delays, access should be reduced on a permanent basis or result in additional disbursement periods. As the delays may not always be fully attributable to the individual country, at least some possibility for carryover should be allowed for.

On access limits, previous Board discussions have led to a suggestion for somewhat greater differentiation among countries. The new proposal for maximum access up to 350 percent of quota seems acceptable. However, I should like the staff to confirm that the increased access for these countries will not result in a cutback of access for other countries. The proposed text is so different from the previous text that some doubt arises as to its actual meaning. We also see a need for a possible scaling down of access, particularly when it is high in relation to quotas, in the event that sufficient grants should not be forthcoming.

I can go along with the staff's proposals on remaining problems concerning access and monitoring.

On financial issues, in the judgment of several of my central banks, the staff proposals do not provide sufficient security for them to contribute to the enhanced facility. Also, the central bank that has agreed to participate would like to see some strengthening in this area.

On liquidity, the basic element is the establishment of compensatory access to the resources of the General Account. While I understand the staff's explanation regarding the safeguards and conditionality associated with members' access to the Fund's general resources arising from needs based on developments in their reserves, it is not clear whether a decision needs to be taken on this matter or whether this interpretation of the Articles would be sufficient. I should like to hear staff comment on this point.

After careful consideration, all of my central banks have decided, in the event of their participation, that they would not want to become "electing lenders." The system of elected lending is complicated, and only in exceptional circumstances do they see a case for an exchange of claims. Instead, they would prefer to make the possibility of temporary suspension of calls available to all contributors.

We shall not oppose the encashment of claims by the Trust, but are not attracted by this proposal.

On charges on overdue obligations, we could accept the use of the SDR interest rate in all cases.

On access to members in arrears to the Fund, we continue strongly to hold the view that there should be no deviation from past policies in this regard.

The question of denomination is a difficult one. I note that at least one contributor would rather lend in its own currency. The staff has suggested a way around this problem. Still, the issue of costs remains, and I am not convinced that the Trust should carry this--so far open-ended--burden. However, the question of denomination has several dimensions. For one of my countries, Sweden, the budgetary contribution has--almost by necessity--been fixed in domestic currency. I realize that, in principle, this creates some uncertainty rather similar to the above mentioned case, but a good argument can be made for treating the denominations of grants more leniently than capital contributions. I should like to hear staff comment on that point.

Finally, on the issues of a more market-related interest rate or the addition of a risk premium, my authorities agree strongly with the views expressed by staff. If such ideas should garner support, it would be the responsibility of the lender to contribute additional subsidies.

Clearly, many of the preceding comments also apply to the draft decisions. However, outstanding issues are clarified by the draft texts, and I shall touch on a few of these.

The staff paper on legal documentation for the enhancement starts with "a short description" of the documents. I understand that this text, specifically that part relating to the nature of the Fund's commitment, does not in any way constitute a "commentary" in the legal sense. Thus, it should not guide later interpretations of the decisions.

On the interest rate to be charged on loans from the Trust, if grants did not meet expectations, which variable affecting loans should be changed? In the paper, it is clear that the interest rate will have to be increased. For my authorities, maintaining the targeted interest rate of 0.5 percent is one of the most distinctive elements of the enhancement of the facility, and we should endeavor to find the necessary grants to achieve this rate. We certainly do not rule out a later increase, which might become unavoidable. Therefore, to leave sufficient room for maneuver, provision should be made for a possible change in access limits, rather than having to raise interest rates automatically.

Finally, although it is clear from the text that there will, in practice, be limited scope for borrowing by the Trustee from the Subsidy Account, as a matter of principle, we should indicate that such borrowing could take place from official sources only.

Mr. Hospedales remarked that his authorities supported the draft decisions and the draft Instrument to give effect to the enhancement of the structural adjustment facility as set out by the staff. The speed of response by donors and the staff to the technical challenges posed by the Managing Director's bold and imaginative initiative to focus sharply on the problems of low-income countries facing exceptional difficulties, particularly those countries that were heavily indebted, represented an exemplary approach to international economic cooperation. Mr. Lankester's remarks on behalf of his authorities merited the highest commendation, in particular because the resources being pledged would be additional to existing aid programs. He was also encouraged by the commitments by members of Mr. Ovi's constituency.

He was also broadly satisfied with the staff's proposals on those issues which had not been entirely resolved during the informal discussions, Mr. Hospedales continued. The recommended potential access up to a maximum of 350 percent of quota in exceptional circumstances would be instrumental in enhancing the use of the facility's resources. He would insist on such a scale of access for those low-income countries where the magnitude of needed structural adjustment was large and the amount of external arrears to be settled was sizable. In that connection, he could also endorse the proposed flexible response to the need for front-loading for some members eligible to use the facility; an initial disbursement of up to 40 percent of the total loan was a step in the right direction.

He continued to be in general agreement with the staff proposals with respect to the financial framework for lending under the Trust and associated borrowing and subsidy arrangements, which were intended essentially to permit lending by the enhanced facility on terms comparable to those under the existing facility, Mr. Hospedales commented. To that end, the staff proposals on the rescheduling of obligations to the Trust and their suggestions on interest rates were broadly acceptable. A number of remaining problems, including some on security and liquidity issues and the modalities of lending, could be settled by the staff and relevant donors so that the enhanced facility could begin operations as originally envisaged.

Mrs. Ploix made the following statement:

Today's discussion is a decisive step in the implementation of the enhanced structural adjustment facility. France attaches great importance to this initiative and is pleased that thanks to the staff's dedication and efforts, it is likely to succeed in the near future.

France's contribution will be made available through resources provided by a parastatal financial institution. The corresponding subsidy will be financed through budgetary resources.

On the security and liquidity of claims on the Trust, we agree with the thrust of the proposals. However, we would like the staff to be more specific about the nature of the Fund's guarantee with respect to repayments of the Trust's obligations in paragraph 2 of the draft decision on the establishment of the enhanced facility, especially as regards the possibility for the Fund to sell gold. Also, would it be possible to also include a reference to other reserves in the draft decision?

To strengthen security, we should still keep in mind the protection of reserves. In this regard, my authorities are reluctant to reschedule obligations to the Trust. While it is true that the Regulations governing the structural adjustment facility include such a possibility, the existing facility and the enhanced facility are not completely analogous, as their funding comes from different sources. Any rescheduling of a loan extended by the Trust would imply a use of the Reserve and could thus impair the ability of the Trust to meet its obligations. I would also stress that great caution should be exercised in using reserves on encashment of claims by the Trust.

France will not be participating in the "electing lender" scheme.

With regard to the interest rate on overdue payments to the Trust, we agree with the proposal to raise the interest rate to the SDR rate. However, we are not in favor of applying the same treatment to overdue obligations with respect to the existing facility. That issue has already been settled, and there is no reason to reopen it. Furthermore, in view of the different origin of the two facilities' resources, such a change would not be justified.

We are in broad agreement with the access limits suggested by the staff. However, as regards differentiated access, a more structured approach, including the use of criteria, is more advisable. In our view, three access limits could be established: the first--between 63.5 percent and 100 percent--without specific criteria; the second--up to 250 percent--set aside for the most indebted countries or those heavily dependent on one or two export commodities, for example, products accounting for 50 percent of exports; and, the third--up to 350 percent--for those countries meeting both criteria. In any event, my authorities prefer access policies that take full account of criteria regarding both indebtedness and dependence on only one or two export commodities. On phasing, we can go along with a certain degree of front-loading; an amount of 50 percent of the total loan is feasible.

We agree that the cutoff date for loan commitments should be November 1989.

We can also support the proposals concerning monitoring, but we have some reservations about the treatment of benchmarks as performance criteria. The reformulation of conditionality should not result in a program design similar to that for stand-by arrangements. Indeed, given the specific goals of the structural adjustment facility, the rationale for conditionality differs from that for stand-by arrangements; conditionality under the enhanced facility must be tailored mainly to the structural aspects of growth-oriented adjustment. Furthermore, all countries should remain eligible to use the Fund's general resources, that is, under a stand-by arrangement.

My authorities regret that the staff rules out this additionality, as such a position will prevent many countries from receiving Fund financial assistance. We are concerned by this possible disengagement; it is important that the Fund should continue to provide financial assistance to all of its members through all of its available facilities.

In sum, we can support all the draft decisions except for those on which I have expressed reservations.

Mr. Ortiz made the following statement:

I would like to reiterate the basic principles guiding the authorities of some of the countries in my constituency when considering their financial contribution to the enhancement of the structural adjustment facility.

My authorities consider the enhanced facility as an instrument to provide low-income countries with more adequate resources in support of strong growth-oriented programs. On this point, I would emphasize our support for Mr. Abdallah's statement that "there cannot be such a thing as undue overstressing of the pursuit of growth targets." The additional resources made available under the new facility should ease the balance of payments constraint, allowing for increases of essential imports geared toward new productive investment and essential structural reforms aimed at increasing economic efficiency--a necessary condition for sustained growth and poverty alleviation. From our perspective, this initiative should be implemented in a broader, comprehensive framework dealing with the deep structural growth problems of low-income countries. The initiative should thus be put forth simultaneously with the Chancellor's proposals regarding the treatment of official debt for countries eligible to use the existing facility, and with additional concessional financing

from official creditors. Financing under the facility must be additional to--and not a substitute for--new assistance from official bilateral creditors.

With these considerations in mind, my Spanish authorities have indicated that they will contribute to the enhanced facility in an appropriate order of magnitude. They have not yet determined a final figure, and they are studying different modalities. But they have responded positively to the initiative, and they will in the course of the next few days come up with a final figure. My Mexican authorities have also indicated that they would be willing to make a contribution to the Trust at the targeted rate of interest, but only in the context of a broadly based regional effort toward international cooperation.

Regarding monitoring, the basic structure of the existing facility should be applied to the new facility. In particular, we support the role of the policy framework paper and consider a three-year program period to be an adequate time frame. The eligibility and qualification requirements should be the same as those for the existing facility.

Conditionality should not be stricter under the enhanced facility than under the existing facility. I have sympathy for many of Mr. Abdallah's comments regarding the use of quarterly benchmarks, performance criteria, prior actions, and midyear reviews. In particular, prior actions should not be considered a norm, and although midyear reviews may be acceptable as a monitoring device, like Mr. Abdallah, we see a danger of transforming benchmarks into performance criteria to trigger semiannual disbursements. We should be careful not to let excessive conditionality defeat the purpose of this new facility.

Access to the enhanced facility by members with overdue obligations is a difficult problem. Like Mr. Lankester, we are willing to support the Managing Director's suggestion that that issue should be addressed within the context of the six-monthly review of overdue obligations.

The Trust should not be exposed to undue risks by allocating its resources to a few countries. A combination of high access determined on the basis of large debt ratios, together with the suggestion that front-loading may be needed to discharge arrears, could imply a concentration of risk in a few heavily indebted countries. If appropriate rescheduling arrangements along the lines of the proposals made by the Chancellor are implemented in tandem with the disbursement of resources under the facility, programs would have a much better chance of attaining their ultimate objectives. The resources of the facility should not be utilized to discharge arrears and, in particular, they should not be used to pay arrears to official creditors. This could

create a moral hazard problem. Moreover, the primary objective of these resources should aim at financing productive investment. In this sense, we have some reservations concerning the notion that the new facility should be targeted more specifically to debt-distressed countries; a number of other economic indicators should be utilized to assess access.

Although we would prefer uniformity of access, we could go along with the proposed access limits on the basis of well-balanced economic criteria. We could also accept the proposed phasing of resources. Finally, we are flexible regarding cutoff dates and could go along with November 1989.

Regarding the security of claims on the Trust, we agree with the view that the strength of the member's program for growth is the best safeguard. We also consider the sources and amounts of funding for the Reserve as broadly appropriate. Although my authorities appreciate the Fund's intention to consider fully and in good faith all reasonable initiatives to assure full payment to lenders in the event that the amounts included in the Reserve turn out to be insufficient to cover arrears, they would request a specific mention of the possibility of gold sales in the decision. We also support the principle of broad proportionality of calls on lenders.

The liquidity provisions still fall somewhat short of the needs and requirements of monetary authorities. In this regard, several points should be stressed. First, lenders should be able to suspend commitments temporarily for short periods of time without having to justify such suspension to the Fund, whether or not they are participating in a "mutual arrangement." Second, we still have some doubts about the effectiveness of swap arrangements for "electing lenders," since it is unlikely that major creditors will elect to participate. Third, we support the provisions related to temporary encashments, and deem a reversal clause acceptable. Fourth, we regard the use of the Fund's ordinary resources as the most promising avenue to the provision of adequate liquidity for claims on the Trust. This, again, is not accurately reflected in the decision. Finally, we support a ten-day period for notice on calls to make a disbursement.

On other issues, we are, in principle, against subjecting overdue obligations to the Trust to market-related interest rates. Therefore, we disagree with any change in this direction with respect to the existing facility. On rescheduling, we agree with the view expressed by Mrs. Ploix. Although any rescheduling of repayments to the Trust will imply a use of the resources of the proposed Reserve, we are in favor of leaving the door open to the possibility of rescheduling.

Mr. Nimatallah, commenting on access of countries with overdue obligations to the enhanced facility, remarked that the problem of arrears was an important one and was likely to persist for some time. Rescheduling of overdue obligations was not possible in the context of the Fund's normal operations, and the problems facing countries in arrears were, in many cases, beyond their control. It might be possible to utilize the enhanced facility to help alleviate the arrears problem without necessarily changing the basic rules of the Fund. That possibility should be left open pending an in-depth examination of the issue with a view not only to facilitating the adjustment process of those countries but also normalizing their relations with the Fund as well as with other creditors.

The Chairman observed that the six-monthly report on overdue obligations to the Fund was tentatively scheduled for Board consideration in January. Nonetheless, he wished to stress that the enhanced facility was not intended to address the problem of arrears to the Fund. Indeed, in negotiations with potential contributors it was clear that any such intention, or perception of such intention, would be detrimental to the entire purpose of the enhancement, namely, to provide an instrument to assist the structural adjustment efforts of the poorest countries. He urged Directors to make that point clear in discussions with their authorities. In that connection, he would also recommend to countries in arrears to the Fund that they should put their house in order so that they might take advantage of the unique opportunity that the enhanced facility offered to facilitate their adjustment efforts.

Mr. Grosche made the following statement:

We have made a great deal of progress since the Managing Director launched his initiative for an enhancement of the structural adjustment facility. I am broadly satisfied with the staff's proposals, and I can generally support the draft decisions.

It is important, however, that in formulating details we pay attention to the need to retain sufficient flexibility for management and the staff in their negotiations with potential lenders. In particular, the issues of denomination, hedging, and the interest on loans should be addressed so as not to interfere with possible solutions. We wish, for example, to be able to denominate our capital contribution of up to SDR 700 million in SDRs, but we do not yet know whether and how that can be done. The matter has to be discussed in the forthcoming negotiations. In this context, I support the solutions proposed in the supplement to EBS/87/253.

On a few issues that need some further clarification, I fully agree with the objective of charging a rate of interest on Trust loans of only 0.5 percent. My authorities consider, however, that the extent of subsidization should be decided on the basis of the financing available to the Subsidy Account. The

Fund cannot commit itself to any specific interest rate in a legal sense, and I recognize that the draft decisions take this into consideration. I wonder, however, whether it is at all necessary to include a reference to a specific interest rate objective in the decision establishing the enhanced facility. In our view, it would suffice to include a general reference to the Subsidy Account and to leave the decision on the interest rate to the Board, which will then have to make the decision on the basis of the financing available. We would therefore propose that Section II, paragraph 4 of the Trust Instrument be amended accordingly. Section III, paragraph 5 could be deleted.

On the cutoff date, I share the view of the staff that flexibility would be necessary. Nevertheless, I would suggest that at this point we should keep to the staff's original proposal and set the cutoff date at May 1989, which would give the Fund sufficient time for the disbursement of loans before the end of the drawdown period. If more time is needed to conclude discussions with recipient countries regarding, for example, the policy framework papers, an extension of the cutoff date up to November 1989 could be considered, perhaps in the context of a review of the enhanced facility.

I support the staff's proposal for cumulative access limits of 250 percent and 300 percent of quota, provided they are used as limits and not as entitlements. Like Mr. Lankester, I do not believe that the establishment of a 350 percent ceiling for highly exceptional cases is necessary or even appropriate.

As for the relationship between the existing facility and the enhanced facility, I do not see a need for providing an option for choosing between an arrangement under the enhanced facility or one under the existing facility. I wonder whether the staff could comment on the rationale underlying such a provision.

My authorities attach great importance to the security and liquidity of claims on the Trust. While agreeing with the establishment of a Reserve within the Trust, I have reservations on some proposals which could weaken the security and liquidity of claims. In particular, my authorities do not favor the suggestions to permit a temporary suspension of calls by any lender and to provide for temporary encashments of claims on the Trust by some lenders. Also, we cannot freely support the suggestion that provision could be made for rescheduling under the enhanced facility. The Trust must be assured of timely repayments of loans, and thus adjustment programs supported by the enhanced facility must aim at restoring balance of payments viability within a time period commensurate with the maturity of loans from the Trust. In my view, provisions for rescheduling could adversely affect the willingness of potential lenders to participate in the enhancement of the facility.

I would like to reconfirm our support for the basic structure of the enhanced facility, its objectives, and monitoring procedures. The prime objective of the enhanced facility should be to support macroeconomic and structural reforms, thereby laying the foundations for a viable balance of payments and sustained growth. I therefore do not share Mr. Abdallah's view that the enhanced facility should focus on growth targets. Sustained growth in countries eligible to use the facility cannot be restored by just channeling more financing to them. After all, that policy contributed to the internal and external imbalances facing many of these countries today. We therefore need strong adjustment programs, and it is fair to expect a strong commitment to adjustment on the part of the beneficiaries under the facility, not only because we are concerned with the security of loans but mainly because it is in the best interest of these countries. In this regard, I can only express a certain disappointment about Mr. Abdallah's rejection of key features of the proposed Instrument, such as performance criteria in exceptional cases and semiannual disbursements. We should bear in mind that on the part of contributors, the special effort on the part of contributors--whose taxpayers' money is going to be spent--calls for special efforts on the part of recipients to see to it that the money is well spent.

Mr. de Groote made the following statement:

Austria will make a reserve loan of SDR 60 million at an interest rate of 0.5 percent--a below-market rate that implies a subsidy of about SDR 24 million. Turkey will make a loan in an amount that will be duly proportional to other members' commitments and which, in any case, will not exceed SDR 35 million, on terms and conditions to be discussed with the Fund at a later stage. Belgium is ready to contribute an amount of not more than SDR 120 million in consideration of the clear intention of the Fund to take all necessary measures, including gold sales, to ensure the liquidity and solvency of the Trust, and to give lending members the benefit of an additional unconditional and renewable drawing facility in case of reserve need. The readiness of my Belgian authorities to contribute is conditional on the Board's formal agreement to these guarantees for lenders' claims on the Trust.

On the outstanding operational issues and legal documentation, the staff has continued, with exceptional diligence, to eliminate most of the technical concerns raised during previous Board discussions and has proposed solutions that should be acceptable to almost all of us.

I support the staff's proposal to extend the cutoff date for the approval of arrangements to November 1989 in order to give

members time to prepare the comprehensive adjustment programs and policy orientations which the enhancement is intended to support. However, it is illogical to grant this flexibility with respect to the cutoff date only in exchange, as it were, for the total loss of any flexibility whatever once the arrangements have become operational. I therefore agree with Mr. Abdallah on the need for at least some scope to accommodate delays in completing midterm reviews or subsequent annual arrangements without risk to members' access to their final disbursements under the enhanced arrangement. I therefore propose that the drawdown period should also be extended from June 1992 to at least the end of 1992.

While I have no major difficulty with the proposed access ceilings, I would appreciate some clarification on the precise implications of the 250 percent limit for members' access to the facility's resources. An earlier discussion of this issue left the clear impression that the enhanced facility would, in principle, allow eligible countries to cover their large residual financing needs up to this 250 percent limit. Does the staff's present insistence that access up to 250 percent should only be permitted in a limited number of cases, and that the facility's resources are not intended to fill residual financing gaps, represent a change in its position?

On other operational issues, we continue to support the staff's earlier proposal that overdue obligations to the Trust, to the existing facility, and to the 1976 Trust Fund should carry charges at a uniform interest rate equal to the SDR rate.

We see little merit in including in the Trust Instrument a rescheduling provision along the lines of the Regulations for administering the structural adjustment facility. Such a provision is not only difficult to reconcile with timely repayment to lenders, but the new facility, because of its sources of financing, is completely different from the original facility. The enhanced facility therefore does not contain any latitude for flexible reimbursement arrangements with members.

We support the staff's interest rate proposals for loans to the Trust and have no problem with the suggested period of five business days' notice on calls on loans to the Trust. We also welcome the solution now being elaborated to accommodate the misgivings of the member who has been especially concerned about the exchange rate risk attached to an SDR-denominated loan. While I look forward to the staff's final conclusions on this issue, assuming normal functioning of the money markets, the remuneration of the member's loan at the SDR interest rate should generally cover any funding and hedging costs.

Mr. Nimatallah remarked that the Board should be careful in finalizing the legal arrangements for the enhanced facility, so as to minimize the need for amendments.

On the proposed financial arrangements, he had no difficulty with the steps articulated by the staff, Mr. Nimatallah continued. He understood that the modalities for the third source of financing, namely, parallel financing, would be developed and articulated soon, in light of further discussions between the Fund and potential parallel lenders.

On access limits, he welcomed the flexibility introduced by the staff and fully agreed with the revised guidelines for access, Mr. Nimatallah commented. A maximum access limit of 350 percent of quota would facilitate the resolution of some difficult problems facing debt-distressed, low-income countries.

On phasing, it would also be desirable to introduce some flexibility, Mr. Nimatallah considered. Some front-loading in the first year of the annual arrangement might be desirable, and indeed, necessary in those instances where a substantial reduction or even a liquidation of payments arrears was required. The proposed pattern of phasing, which would allow for disbursement of up to 40 percent of the total loan in the first year, seemed appropriate as a general guideline, so long as the interpretation of that guideline paid due regard to the strength of the adjustment program and the specific needs of the adjusting country. Furthermore, within each yearly arrangement, some front-loading of the annual disbursements would be desirable to allow as much flexibility as possible to enable the Fund to respond to the needs of debt-distressed, low-income countries in an effective and timely fashion.

He could go along with the proposed cutoff date of November 1989 and the extension of the drawdown period to June 1992, Mr. Nimatallah remarked. However, in cases where programs were in progress and an extension beyond the end of the drawdown period was required, some flexibility should be introduced to permit the completion of committed disbursements. He recognized that the Instrument provided for a possible extension of the drawdown period, to be worked out between the parties concerned, but he did not see a similar mechanism with respect to the operational arrangements. For example, there could be an exceptional extension in the drawdown period, but not necessarily in the repayment period to creditors.

The Chairman remarked that flexibility was indeed an important feature of the enhanced facility. However, flexibility should be directly related to the quality of the program: the higher the quality of the program, the greater the degree of flexibility.

Mr. Sengupta made the following statement:

I have spoken extensively on this subject at our informal sessions, and will limit myself to a few outstanding issues on operational arrangements and legal documentation.

We welcome the staff's suggestion that the cutoff date for the enhanced facility should be November 1989, because it would provide more flexibility to the borrowing countries. If there are delays in concluding arrangements or midyear reviews, they should be dealt with in a flexible manner, without any automatic reduction in access or adjustment to the amounts of subsequent disbursements.

On the relationship between the existing facility and the enhanced facility, we can go along with the staff proposals. We also support the idea of differentiated access under the enhanced facility. On the front-loading of disbursements in the first annual arrangement, our authorities feel that 40 percent of the total loan would be inadequate; a higher initial amount may be necessary to promote smoother adjustment with a higher initial addition to reserves.

We have noted the clarification on the transfer and retransfer of funds between the Special Disbursement Account and the Trust and welcome that the proposed decision defines and circumscribes the scope of such transfers.

We do not favor the encashment of claims on the Trust by utilizing amounts available in the Reserve. This is not an appropriate measure for addressing liquidity problems, which can be adequately met by recourse to existing Fund facilities. It would be undesirable to impair the Reserve for this purpose.

On the question of the rate of interest on overdue obligations to the existing facility and to the 1976 Trust Fund, we do not see any reason for a change in the decision on special charges, which was taken after long discussions in 1985. Since the amounts disbursed under the structural adjustment facility and as Trust Fund loans can be identified, there should be no difficulty in proceeding with the existing decisions on overdue obligations with respect to these loans.

The staff has raised some important issues with respect to the problem of rescheduling obligations to the Trust. I am not sure that there is a consensus on a provision for rescheduling under the enhanced facility, but if such provision was included, the cost of subsidizing the rescheduled portion of the loan should not be met from the resources of the Special Disbursement Account, because that would imply a permanent depletion of those resources.

With respect to the proposal for the second disbursement, on the fulfillment of an either/or condition, as given in the Amendment of the Regulation for the Administration of the Structural Adjustment Facility, I suppose that the performance criteria are intended to be specified only where there is no midyear review. The intention should not be to have both, if we agree that the

basic structure of the existing facility would be retained for the enhanced facility. I agree with Mr. Abdallah's views on these points, particularly with regard to conditionality.

The draft Instrument provides that before approving a three-year arrangement, the Trust should be satisfied that the member is making a "substantial effort" to strengthen its balance of payments position, while the corresponding provision for the existing facility states that the member has to make a "reasonable effort" to strengthen its balance of payments position. The expression "substantial effort" in the draft Trust Instrument has not been defined, whereas "reasonable effort" under the existing facility has been carefully defined to mean that the member has presented to the Fund a three-year adjustment program and the first of three annual programs setting forth the objectives and policies for the year. The term "substantial effort" should not, in my opinion, be left undefined. If the intention is to imply "prior action," then it should be pointed out that the Chairman's summing up of the discussion on November 20 indicated that "some Directors believe that prior actions would be appropriate where strong policy responses are required, while others have argued that the use of prior actions should be strictly limited." We would therefore suggest that the terminology for the existing facility should be used in the proposed Instrument for establishing the Trust.

More generally, with respect to the operation of the facility, excessive emphasis on the security of claims on the Trust should not lead to excessive conditionality, as that would not be consistent with the purposes of the enhanced facility. Moreover, the specific needs and implementation capacity of the borrowing members would need to be given greater emphasis in program design. Finally, the enhancement of the facility's resources should ensure genuine additionality to the normal availability of concessional flows to low-income developing countries.

My Indian authorities support the increased flow of resources to developing countries and, in this context, extend their support for the enhanced facility. However, they would stress that there should be a parity of treatment among all poor countries, as a matter of principle. The staff papers and draft decisions fully recognize the eligibility of all poor countries, including India, which meet the objective criteria for assistance. As stated in our intervention on the occasion of the review of experience with the structural adjustment facility in June (EBM/87/93, 6/19/87), although India's requirement for concessional finance has increased in the 1980s, such assistance has steeply declined in real terms. India received only about \$2 per capita in net official development assistance, and its debt profile has been deteriorating. Currently, the authorities are tackling

the problems associated with an unprecedented drought, as was recognized during the 1987 Article IV consultation discussion (EBM/87/120, 8/7/87). The balance of payments position, however, is expected to recover despite some stress owing to the drought, mainly because of the sound economic policies that the Government has followed over the years. We intend to continue to follow such policies, and therefore it is unlikely that India will borrow from the enhanced facility. However, we would note that although the present indications are that India does not expect to borrow from the facility, if the balance of payments position changes fundamentally, the question of borrowing from the enhanced facility could be considered at that time.

The Chairman remarked that, as Mr. Sengupta had emphasized, India would, of course, remain eligible to use the existing facility as well as the enhanced facility. India was a poor country facing great economic difficulties, and if an unexpected crisis arose, a request by India to use the facility would be examined with sympathy.

In that light, he welcomed India's intention not to seek recourse to the enhanced facility in the foreseeable future, the Chairman continued. He was also confident that the authorities would continue to pursue prudent financial policies that would enable India to solve its problems. However, he wished to make it clear that India's position with respect to the facility--as well as China's--should in no way result in any diminution of concessional flows from other sources.

Mr. Yamazaki stressed his authorities' commitment to, and support for, the enhancement of the structural adjustment facility. Although he could broadly endorse the staff's proposals, his authorities had not completed their deliberations on possible arrangements for contributing to the Trust. Therefore, at the present stage, he had reservations with respect to the proposed decision on establishment of the enhanced structural adjustment facility Trust.

As far as the operations of the Trust were concerned, he could generally support the proposed decision, Mr. Yamazaki continued. However, a guideline for the Trust's lending operations was probably needed. For example, although the proposed decision required potential borrowers to make substantial efforts to strengthen their balance of payments position before concluding an arrangement under the enhanced facility, the proposed decision did not present a guideline for that requirement, whereas the Regulations for the administration of the existing facility included a guideline for a similar requirement for the use of its resources.

He wished to reaffirm his understanding that paragraph 2 of the proposed decision on the establishment of the Trust meant that the Fund would consider all initiatives, including the sale of gold, Mr. Yamazaki added. Finally, he wished to underscore the importance which his authorities attached to the timely inauguration of the facility's operations.

Mr. Zecchini made the following statement:

In October 1987 the Board agreed that no decision would be taken on the legal arrangements for the enhancement of the structural adjustment facility unless the Board had been informed about the preliminary commitments of each donor and lender well in advance. This procedure is indeed appropriate, and we would prefer that the Board abides by it. Consequently, the Board should postpone any decision on these matters and have only a preliminary exchange of views on the texts of the decisions. Once the Chairman is in a position to circulate a paper outlining the terms of the participation of each contributor and enough time has passed to allow members to examine this paper, then the Board can proceed to a formal consideration of the proposed texts. In line with this approach, we can express only preliminary views on the proposed financial arrangements, while our position on legal considerations will be taken when all of the necessary information is available.

As to the cutoff date, the extension of access from May 31, 1989 to November 1989 has to be viewed in the light of the probability that all major contributors, including the largest shareholder of the Fund, will join this facility at some stage of the access period. If this is the case, there is enough justification for agreeing on the extension. Otherwise, we do not see sufficient reason for it. In this respect, the May deadline usefully meets the objective of prompting beneficiary countries to hasten the restructuring of their economies.

As to the access limits, the proposed solution allows a judicious flexibility. On the timing of disbursements, the norm should be uniform distribution. Front-loading of disbursements has to be considered as exceptional and possible only if adequate resources are available. The possibility of reducing access in the event of favorable developments in the balance of payments has to be considered with great caution since it might have the perverse effect of penalizing the diligent country or of discouraging the achievement of a rapid external adjustment.

With respect to the security of claims on the Trust, we must insist on the subordination of other payments to the Special Disbursement Account to repayments of these claims and for an addition to the language of the draft Instrument, which I will specify later. As to the provisions aimed at assuring the liquidity of claims, the latter have to be negotiable and freely transferable independently from the participation of lenders in the scheme of "electing lenders." The credit certificates have to be negotiable among Fund members. We also support the proposal for permitting a temporary suspension of calls by the lender and for a temporary, short-term encashment of claims.

At the same time there can be no question that the claims have to be denominated in SDRs and that no rescheduling of maturities can be allowed, even if sufficient resources are available in the Reserve. Any rescheduling would amount to unfair discrimination among both lenders and beneficiaries. Overdue obligations to the Trust cannot benefit from any concessionality but should be charged the highest interest rate between the SDR interest rate and the actual cost of borrowed funds to the Trust. On the method of determining the market interest rate on the loans, we can accept in principle the staff proposal for making reference to the SDR interest rate. In this respect, we understand that the issue of the use of a risk premium or a more market-oriented rate is a delicate one if some countries provide only the principal and others only the interest subsidy. In the absence of full knowledge about this crucial possibility, the question of the use of the market rate cannot be considered as already settled.

I have few preliminary suggestions for amendments to the legal documentation. However, the full extent of our proposed amendments will be presented at the time of the final Board discussion of this matter.

In the decision on the Amendment of the Regulations for administering the enhanced facility, paragraph 1(3), it should be specified that the period of the three-year commitment shall be extended up to mid-1992, otherwise we could be faced with an unwarranted extension of this period. In paragraph 2 of the decision establishing the Trust, reference should be made to the possibility of using or mobilizing the Fund's gold to protect lenders' claims. Moreover, the Fund should assure not only full, but also "swift," repayment to lenders in case of arrears.

In Section I of the draft Instrument, we should clarify that the objective of the programs is to strengthen the balance of payments position not only substantially but also durably. The notion of durability should be incorporated.

In Section III, paragraph 4(c) of the draft Instrument, the word "broad" should be eliminated, since uniform proportionality has to be the norm.

In Section IV, paragraph 4, of the draft Instrument, the words "in such order as it may determine" should be eliminated, since proportionality should also be applied here. The bracketed statement should be deleted, as rescheduling should not be allowed. In paragraph 5(a)(i), the words "to the extent possible" should be deleted, since the objective for the subsidy should remain a reduction of the interest rate to the level prevailing under the existing facility. Without this objective and by

enlarging the differences between the existing facility and the enhanced facility, we run the risk of creating a strange hybrid rather than enhancing the structural adjustment facility.

Our final position, with reference also to those parts of the draft decisions which were not mentioned, will be presented when we know all of the terms of participation for each contributing country, but without in any way detracting from our strong commitment to support the enhanced facility. Our commitment was specified in the amount of lending, in the subsidy granted, and in the other conditions at the informal discussions of the Board on this matter, and is considered by us as irreversible.

The Chairman remarked that while no decision would be taken at the present meeting, and in that sense the discussion was a preliminary one, it was nevertheless important to finalize the arrangements for the enhancement of the facility by the end of the year as had been urged at the Economic Summit in June. He continued to hope that the new facility could enter into operation on January 1, 1988.

Mr. Dai made the following statement:

I believe that the Board is now united in its wish to expedite the legislative process so that enhancement of the structural adjustment facility can be implemented on schedule.

I would like to clarify our views on some outstanding issues that were not resolved during the Board's informal discussion on the subject. I agree with the proposal to set the cutoff date at November 1989. I can also go along with the proposed guidelines on access limits. As for front-loading, I can agree to the proposal for disbursements in the first year up to 40 percent of the total loan, if we cannot go any higher.

As for the financial arrangements, I agree with the staff's view that temporary suspension of calls by any lender should be permitted only in very limited cases and that there should be a genuine liquidity need. With regard to the rate of interest on overdue obligations to the existing facility and to the 1976 Trust Fund, I see no need to change the rate of charge. I believe that a provision for rescheduling similar to that in the Regulation for the existing facility should be included in the Trust Instrument. Although I can go along with the proposal that the Subsidy Account can borrow under certain circumstances, in principle, lenders should be called upon to provide the subsidies required.

More generally, the enhanced facility is aimed at increasing the availability of resources, rather than intensifying the conditionality attached to the use of such resources. The discussion on the review of experience with the structural adjustment

facility in June led to the conclusion that conditionality under the existing facility should not be further tightened nor should its procedures be made more complex. Nevertheless, the proposals for the enhanced facility not only tighten conditionality but also greatly increase the work load of both the staff and the Board. The concerns expressed by Mr. Abdallah regarding this intensified conditionality are quite convincing. I am very much concerned that the increased complexity of the new facility and the tightened conditionality might discourage potential borrowers from drawing on its resources. Most of the problems of these countries are structural in nature, and it would be impractical to expect their adjustment and reform efforts to achieve results in a shorter period of time than would be necessary, for example, to redress a temporary balance of payments imbalance. In reality, both time and patience are needed as far as structural adjustment and growth issues are concerned.

I fully understand lenders' concern about the security of their claims on the Trust. We must not lose sight of the fact that the enhanced facility was an official action growing out of a spirit of international goodwill and cooperation. We hope that all eligible member countries will benefit from this facility and that neither its method of operation, or terms and conditions will impede its use. After all, if a large number of eligible members find it difficult to avail themselves of the facility, how can we fully achieve our original objective for its establishment? I therefore hope we can be flexible with respect to its implementation.

An alternative would be for the staff to monitor each program's performance and, upon evidence of a program going off track, a mission could be dispatched promptly to the member country to provide suggestions and technical assistance. If the program is found to be generally on track, a report could then be sent to the Board for its information and for decision on a lapse of time basis; no further action would be necessary. Such a procedure could reduce some of the work load of both the staff and the Board and would also be less burdensome to the recipient countries.

In sum, I can generally go along with the proposed decisions, except for those reservations expressed on sections of the Amendment to the Regulations for the Administration of the Structural Adjustment Facility that will intensify conditionality.

Mr. Massé made the following statement:

Since I have presented my authorities' views on most of the issues concerning the enhancement in our earlier informal discussions, I will address only the additional aspects raised by the staff papers.

With respect to access and monitoring, my authorities would agree that in order to provide maximum flexibility to borrowing members, the cutoff date could be set at November 1989. As regards access limits, we continue to feel that the expectation of an average loan of about 150 percent of quota is reasonable, and that access near, or at, 250 percent of quota should occur only in a limited number of cases. In addition, my authorities would be willing to consider a maximum access limit of 350 percent, but only in a few exceptional cases. With respect to phasing, we continue to feel that an even distribution of financing over three years is reasonable, although in exceptional cases, we would be willing to consider some front-loading, with disbursements up to 40 percent of the arrangement in the first year.

As for financial arrangements, my authorities do not wish to be an "electing lender." Provision for a temporary suspension of calls could be helpful, and some limited provision for temporary encashments could also be useful. Overdue obligations to the existing facility and to the 1976 Trust Fund should be subject to the same rate of charge as that for the proposed Trust--namely, the SDR interest rate. My authorities do not consider it appropriate to envisage the possibility of any rescheduling of loans made by the Trust. Consequently, they would not favor the inclusion of such a provision for the enhanced facility.

My authorities find that the interest rates suggested by the staff are acceptable, and they would also agree that an additional risk premium is not necessary. We accept that denomination of loans to the Trust in domestic currencies could unduly complicate the operations of the facility, and my authorities would not wish to press this issue. My authorities also find the provision for calls, and the exceptional provisions relating to the timing of interest payments and of disbursements of Trust loans, and calls on lenders to be broadly acceptable.

As regards the legal documentation, the draft decisions seem to be generally quite correct to us, subject to the qualifications that I have noted.

This chair appreciates the Chinese authorities' decision not to draw on the enhanced facility--an undertaking which I fully agree should not undermine China's access to other concessional resources. In that connection, I strongly endorse the Chairman's remarks on India. We recognize India's eligibility to use the resources of the existing facility and the enhanced facility; there should be no discrimination among borrowers having low per capita incomes and extreme balance of payments difficulties.

Although not all of the issues related to the enhancement have been resolved, a number of months ago most of us believed that the chances of getting this far were not great, and it is due to the efforts of the Chairman, the staff, and a large number of my colleagues that an extraordinary result has been achieved in a period, which, in terms of international organizations, is quite brief. I would also like to encourage potential contributors to finalize their arrangements, especially since it appears that there remain untapped, and still needed, sources of funds.

In that regard, my authorities are considering a call for a contribution in excess of the amount of SDR 200 million, which had been announced earlier. To prevent any delay in putting the enhanced facility into place, I would plead with Mr. Zecchini to urge his authorities to reconsider their position, so that the facility could commence operations even if all contributions were not finalized within the next few weeks.

Mr. Zecchini, responding to the concern expressed by Mr. Massé, commented that he wished to make it clear that his authorities' position had not been taken in response to specific commitments but rather arose from the general proposition that all major shareholders in the Fund should contribute to the enhanced facility at some stage.

Mr. Donoso remarked that he generally supported the proposed decisions to give effect to the enhancement of the structural adjustment facility. Some members of his constituency were considering a contribution based on a broad regional participation in the enhancement. In particular, Chile had indicated that, subject to the realization of that broad regional participation in the enhancement, it would also contribute an amount proportional to commitments by the other Latin American countries.

Mr. Posthumus remarked that his authorities intended to contribute to the enhanced facility, and they were making all possible efforts to implement that intention. While they had had hesitations about the initiative, they had also supported it once it was taken. The hesitations arose with respect to the role of the Fund and had nothing to do with the need to take urgent measures to assist the poorest and most indebted member countries with the adjustment required to enable those countries to attain structural growth. Clearly, his authorities supported that aim, and the assistance programs which the Netherlands financed, bilaterally, multilaterally, and jointly with the World Bank, on behalf of those countries, were ample proof of that support. The Netherlands had for many years financed official assistance programs which, in terms of GNP, were substantially larger than those of many other donor countries, and had since 1980 amounted to about 1 percent of annual GNP. Substantial budgetary difficulties over the past few years had not changed that policy. Thus, while his authorities' concerns and aims were the same as those of the Fund, it was difficult for them to follow the path of the enhanced facility to reach their objectives, but not because of the lack of resources.

His authorities recognized that an international initiative could not be tailored to fit each donor country's idiosyncracies, Mr. Posthumus continued. The staff had suffered with him when he had tried to put the aims of the Netherlands, the Fund, and the World Bank in one basket. That effort had failed and proved that if one had more aims than instruments, some aims would have to be given up. However, his authorities were working on another approach, namely, grants for interest subsidies only.

He supported the conditionality and monitoring proposed for the enhanced facility, Mr. Posthumus commented. The countries eligible to use the enhanced facility were presented with a unique mechanism to help solve their balance of payments problems. He had reservations about lending to members in arrears to the Fund, but had an open mind.

His authorities were not at the moment considering a capital contribution to the Trust because they considered its liquidity and security to be insufficient to give such contributions a monetary character, and he therefore had few comments on the Trust, Mr. Posthumus observed. However, he objected to pledging the Fund's gold to cover the residual risk. Finally, to have assembled in less than half a year an amount of SDR 6 billion of concessional funds and to have set up the mechanism to channel those resources to the developing countries was indeed a big achievement. He would like to thank the Chairman and the staff for their considerable efforts.

Mr. Finaish made the following statement:

We agree with the staff that flexibility in setting the cutoff date is desirable in order to provide members with sufficient time to undertake the necessary preparations for entering into an arrangement under the enhanced facility. We support the extension of the cutoff date from May 1989 to November 1989. The staff has noted that, because the enlarged resources are committed over a limited period of time, the extension of the cutoff date beyond May 1989 implies little scope for delays in disbursements if an arrangement is approved close to the cutoff date. In this regard, it would be advisable that economic performance be evaluated in a flexible manner so as to avoid undue delays in the completion of midterm reviews or the approval of the next annual arrangement. If timely completion of the review is not possible so that the efforts of the authorities and staff are concentrated on the next annual arrangement, this should not result in a permanent reduction in access for the borrowing member, and adjustments should be made to the amounts of subsequent disbursements.

We accept the staff suggestion that adequate access should be open to as broad a range of eligible members as possible, and access near or at the limit of 250 percent of quota should not be considered a norm. By the same token, access should not be

unduly stringent and should be constrained only by the availability of resources. We also agree that access at a maximum limit of 350 percent should be considered in exceptional cases.

Regarding the criteria for access, the external debt position of the member is clearly a relevant consideration. However, preoccupation with a single variable like the debt ratio could be counterproductive. While differentiated access is appropriate, it should not lead to a concentration of access in a relatively small group of members. We have in the past discussed the issue of protracted balance of payments needs of low-income countries; the Board's conclusions on that issue continue to be relevant for access under the enhanced facility.

In his remarks at the conclusion of the informal discussion on November 20, the Chairman stated that access limits are expected to be increased at the time of the annual reviews. Presumably, an increase in the access limit will also imply an upward adjustment in the actual differentiated access within that limit. It is unclear, however, how such an increase in actual access is to be applied. For example, the second review of access limits will take place soon after the cutoff date. At that time, it is not unlikely that a significant increase in access may be possible, since the number of actual users of the enhanced facility will be known. It is unclear whether those members that started their three-year programs early, and that may have already drawn one half or more of the initial total commitment, will be able to benefit from the increase in access to the same extent as those that started their program shortly before the cutoff date. In our view, it would not be desirable to apply the policy in a manner that penalizes the early comers and thus, at least in theory, gives members a disincentive to embark on a program as soon as possible. Staff comment on this point would be useful.

With regard to the phasing of disbursements, we agree that there should be front-loading of loans. Front-loading is consistent with the profile of the financing requirements of the countries eligible to use the facility, because it is expected that relatively large financing will be required in the initial phases of their adjustment programs. These large financing requirements in the first year of the programs arise not only from the need in some countries to settle overdue external obligations and to build up international reserve holdings, but also and more generally, because the current account deficit is expected to decline gradually over time on account of the lagged adjustments in exports and imports to policy measures such as exchange rate depreciation. Indeed, certain structural adjustment measures, which are frequently incorporated in programs under the facility, such as rationalization of the tariff structure and removal of quantitative import restrictions, are likely to result in an

immediate increase in imports, whereas the improvement in export performance owing to increased efficiency tends to occur with a substantial lag. In view of the up-front financing needs of most members eligible to use the facility, front-loading is clearly desirable, and the primary consideration in this connection should be the rate at which the Fund's borrowing arrangements permit the drawdown of contributors' lending commitments. The staff suggestion regarding the pattern of phasing that results in disbursements in the first year of up to 40 percent of the total loan seems to be on the low side, and if the availability of resources permits a greater degree of front-loading, we would support even larger disbursements for the first year. In any event, the suggestion that front-loading should be considered only in exceptional circumstances does not seem to be fully justified. Front-loading should be applied whenever it is judged to be appropriate, which may well be the case in a relatively large number of programs.

On the relationship between the existing facility and the enhanced facility, we agree that the existing facility should continue to operate in parallel with the enhanced facility and that the proposed review of the existing facility should take place before November 1989. The staff proposals regarding the procedures that would apply to cancellation of an arrangement under one facility and its replacement by an arrangement under the other are acceptable. We also agree with the staff that whereas cancellation of an existing arrangement and replacement by a new three-year arrangement under the enhanced facility would usually take place at the expiration of an annual arrangement, cancellation prior to the expiration of an annual arrangement should be permitted if a country faced a significant change in balance of payments needs.

On the issue of loan commitments, we have difficulty with the suggestion that access should be reduced during the course of the arrangement if balance of payments developments turn out to be more favorable than originally envisaged. We continue to support the view that access should not be reduced as a rule in such circumstances. In many cases, the resources could be utilized to raise the real growth targets and to provide some cushion in the implementation of stronger adjustment measures. In most low-income countries, the external financing needs are such that even a substantial improvement over the balance of payments target would still not justify a reduction in access. Moreover, it is likely that an improvement in the external environment, associated, for example, with stronger demand for imports by industrial countries, will have a positive effect on the external positions of many countries eligible to use the facility during the same period. In such circumstances, a generalized reduction in access may lead to an underutilization of available resources by countries which, despite the improvement

in their balance of payments, continue to need the concessional financing provided by the enhanced facility. In this connection, the staff is correct to emphasize that even after taking into account funding provided under enhanced arrangements, a number of countries would remain in need of additional assistance, some of it on a substantial scale.

Regarding access of members with overdue obligations to the Fund's resources, we have noted the Chairman's statement at the conclusion of the informal discussion on November 20 that the matter will be taken up again in the near future. During that meeting, different suggestions and views were expressed by Directors, and we look forward to a more thorough discussion of this matter by the Board in January.

On financial arrangements, the staff's proposals with respect to the financial framework for loans to eligible members and the associated borrowing and subsidy arrangements provide an adequate degree of liquidity and protection against risk for claims on the Trust. We can endorse the staff proposal that the Subsidy Account should be governed by a separate Instrument. We can also endorse the staff suggestion that a provision for rescheduling comparable to that of the existing facility should be included in the enhanced facility, and the provision should make explicit that a request for rescheduling would not be considered until a determination has been made by the Fund that the Reserve had become sufficient to meet the Trust's remaining obligations. For the reasons mentioned by the staff, we agree that the rescheduled amount should continue to be subject to the subsidized rate and any cost of the subsidy should be borne effectively by the Special Disbursement Account.

Finally, the question of a possible contribution to the enhanced facility is still under consideration in some countries in my constituency. We will inform management and the staff of any new development.

Mr. Dallara made the following statement:

I would like to congratulate management and the staff for the remarkable progress achieved in only half a year in moving toward the full realization of the Managing Director's initiative, which should play an important role in supporting the economic efforts of many low-income countries in the years ahead.

I would also like to extend the appreciation of my authorities for the willingness of so many other Fund members--not only industrial country members but also a number of debtor country members--to contribute to the enhancement of the structural

adjustment facility. This response reflects a recognition that, in current circumstances, some countries are better placed than others to contribute to the enhanced facility.

At the same time, I certainly am aware of the desire shared by many Directors that my own authorities should be in a position to participate. Perhaps I have not stressed enough in earlier discussions that we conducted an exhaustive search of possible nonbudgetary means of participation. In contrast to the legal flexibilities that appear to exist in some other capitals, there is absolutely no off-budget mechanism, involving either the Federal Reserve or any other official agency, through which we could participate in the enhanced facility.

With respect to a possible budgetary contribution, I hope that everyone appreciates the factors which guide our position. In addition to the funding that we are currently seeking for broadly similar purposes for other institutions to support low-income countries, there is the urgent need to reduce the fiscal imbalance which my authorities currently face.

With respect to the positions of other members, we welcome and commend the willingness of the Chinese authorities to forgo the use of the resources of the enhanced facility. We also welcome the comments made by Mr. Sengupta. As Mr. Massé has noted, it is important that we express our sincere appreciation for the willingness of the Indian authorities not to use the enhanced facility at this time. It is equally important to recognize and reaffirm India's eligibility to use the facility in the future if there should be a fundamental change in its external circumstances. This would help ensure nondiscrimination in the use of this facility. The position of the Indian authorities should go some distance in helping to achieve the purposes of this facility.

We generally support the arrangements for the enhanced facility set forth in the staff papers. More specifically, we support the arrangements with respect to security, with one minor qualification. While we have previously advocated a mechanism to ensure that excess amounts in the Reserve would be released as soon as possible, we can accept the proposed language in the staff papers. We understand that this language means that the Reserve would be under continuous review and amounts could be released to the Special Disbursement Account on the basis of a majority of the voting power in the Board.

With regard to the pledge of the Fund's gold and the suggestion that there should be an explicit reference in the decision establishing the Trust to the possible sale of gold, my authorities cannot support the inclusion of such a reference in the decision. U.S. legislation would, in fact, preclude me from

actually supporting the use of gold to satisfy claims on the Trust, and, therefore, my support for the inclusion of such language in the decision might send the wrong signal. At the same time, I should add that this issue relates to a possible event more than a decade in the future. No matter how farsighted my authorities are, there is simply no way that they can predict the circumstances and considerations which would come into play in that distant future.

On other issues, we accept the guidelines on access suggested for the first year of operation, with annual reviews of both the access guidelines and amounts committed to each country. Since there is some ambiguity in the language setting forth access for exceptional cases, we would like to indicate our understanding that the staff proposals would enable access in such cases to be set anywhere between 250 percent and 350 percent of quota, and I would also associate myself with the position of Mr. Lankester that we should not feel ourselves obligated to set definitively an upper limit for exceptional cases.

On front-loading, we recognize the constraint resulting from the fact that loans would be tranching, and we appreciate the risks to lenders associated with excessive front-loading. Nevertheless, we support the basic principle of some front-loading, and we hope that the proposals of the staff would be interpreted flexibly so that the amounts could be determined on a case-by-case basis.

On other operational issues, we noted with interest Mr. Lankester's proposals regarding the reserve objective in program design. While we can support the staff's view on the importance of building reserves, we would note that, in some cases, difficult judgments would have to be made regarding the alternatives of reducing high-cost debt or building reserves. On the cancellation of commitments under the existing facility, we would take a skeptical view of cancellation before the end of an annual arrangement. Regarding interest charged on arrears, our firm view is that the rate of interest on overdue obligations relating to both the existing facility and the enhanced facility should be set at the SDR interest rate. On rescheduling, we support the view of those who would not consider it appropriate to include a provision in the enhanced facility for rescheduling. With respect to loans to the Trust in domestic currency of members, we would hope that the lender could absorb the risk of exchange rate movements to the maximum extent feasible. Finally, on borrowing by the Trust, we had expressed some reservations on this issue earlier, but we are now able to support the limited authority in the proposed draft Instrument.

Mr. Rye stated that three countries in his constituency--Korea, New Zealand, and Australia--had been approached regarding contributions to the enhanced facility. His Korean authorities were understandably taking the view that the matter was one for decision by the new Administration that would take office following the election on December 16. New Zealand had decided that its aid priorities lay within its own South Pacific region, and it was unable to contribute to an expanded facility at present. As for Australia, the Reserve Bank was taking the same view as some other central banks, namely, that the proposed Trust did not offer sufficient security or liquidity to make it an appropriate repository for official reserve assets. Unfortunately, Australia did not have other nonbudgetary sources for a possible capital contribution. A budget contribution raised a number of difficult issues. However, the question whether there might be scope to provide funds, at some future time, for the Subsidy Account was still under consideration by his authorities.

Since his constituency was thus, for the time being at least, standing on the sidelines, it did not seem appropriate for him to comment on the arrangements for the enhanced facility, Mr. Rye continued. However, in line with his remarks at the recent informal sessions, he could support the staff proposals. In particular, the proposed procedures for monitoring and the proposed degree of conditionality were entirely appropriate.

Mr. Hammoudi made the following statement:

Management and the staff have made tremendous progress within a short period toward the establishment, arrangements, and framework for the operation of the enhanced structural adjustment facility. I would like to take this opportunity to express my appreciation to China and India for their decision to abstain from drawing on the enhanced facility. While the concessions extended by several creditors to low-income countries under the enhanced facility are appreciated, we hope that all other potential creditors will also respond to this initiative as soon as possible so that adequate resources will be available by January 1988 for the commencement of the facility's operations.

It is essential that the international community at large shows understanding for the difficult conditions under which most countries eligible to use the facility, particularly those in sub-Saharan Africa, are living. It is important that we avoid imposing further conditionality and complex operational modalities that they would be unable, for obvious reasons, to handle. Thus, I would emphasize that we should refrain from treating this facility as if it were an extended Fund facility, even with some simplification. Under the circumstances, I do not see any convincing reason for a major departure from the structure and operational modalities of the original structural adjustment facility. Even then, I should point out that this chair has

expressed strong reservations about the tightening of conditionality for that facility. Furthermore, I strongly feel that the suggested recommendations relating to conditionality under the enhanced facility are not consistent with the spirit and the letter of either the 1976 Trust Fund or of the existing facility. As Mr. Abdallah has rightly stated, "what the existing facility needed to achieve its objectives was the addition of resources and not the intensification of complexities and conditionalities."

I understand perfectly the concerns of the countries that would provide the necessary resources for the establishment of the facility. However, these concerns should not take precedence over the need to tailor our assistance to the special circumstances and requirements of countries eligible to use the facility. Moreover, the existence of stand-by arrangements has not prevented the emergence of arrears to the Fund. We should therefore show some flexibility toward countries using the enhanced facility, for example, by accepting the staff suggestions to continue disbursements even if the country has overdue obligations and by front-loading disbursements if circumstances warrant.

My first preference is to maintain the essential features of the existing facility, with the understanding that we find its conditionality to be excessive.

In view of the complexities inherent in the proposed structure of the enhanced facility, it appears difficult, if not impossible, for eligible countries to implement the introduction of midyear reviews, quarterly benchmarks, semiannual disbursements, prior actions, and the transformation of some benchmarks into performance criteria. The experience of the Fund shows that excessive and stringent conditionality would force a program to go off track, given the extraordinary difficulties that eligible countries are confronting and the undesirable political consequences expected to arise from frequent monitoring and extended conditionality.

Since our views on the proposed arrangements have already been expressed during the informal meeting of November 20, 1987, and since we strongly support the establishment of the enhanced facility, I would like to associate myself with the views expressed by Mr. Abdallah with regard to other aspects of the proposed decisions.

The Deputy Director of the Exchange and Trade Relations Department recalled that a clarification had been requested regarding the statement in EBS/87/245 that access to other Fund facilities by a member using the resources of the structural adjustment facility would be examined on a

case-by-case basis "in accordance with existing guidelines." The guidelines referred to were straightforward with respect to the conditionality associated with the use of those resources, whether under a stand-by or an extended Fund arrangement, as well as with respect to operational aspects of the various facilities, such as phasing and performance criteria. However, under some of the Fund's facilities, the time frame for repurchases was shorter than that of the structural adjustment facility, and the charges on all other facilities were higher. Those two aspects, in particular, would have to be taken into account in examining the issue of access to other Fund resources. Of course, all members eligible to use the enhanced or existing structural adjustment facility remained eligible to use the resources of other Fund facilities.

The Fund had an important role to play with respect to countries eligible to use the structural adjustment facility, the Deputy Director commented. A substantial volume of resources was being made available to those countries as a result of the initiative to enhance the facility, as well as the World Bank's successful initiative to elicit more cofinancing from donors. Therefore, in framing programs with countries, the Fund would have to examine all available resources with a view to choosing the most appropriate financing package for a country in need of assistance.

It was proposed that there should be performance criteria for the midyear disbursement in all cases, the Deputy Director noted. Monitoring would be conducted on the basis of an appropriate number of quarterly benchmarks used under the existing facility, some of which would be converted into performance criteria for the midyear disbursement. The structural nature of the programs supported by the enhanced facility suggested the need for a review in most instances, because many of the policy reforms to be taken were not easily quantifiable for the purpose of evaluating the success of implementation. For those countries where access was relatively small, the previous record of adjustment was good and the program straightforward, performance criteria alone might be sufficient.

The language of the draft Instrument was not meant to imply that in exceptional cases the maximum cumulative access could automatically be raised from 250 percent to 350 percent of quota, the Deputy Director remarked. There were certain binding constraints on the operations of the enhanced facility, the most critical ones from a financial point of view being a fixed volume of resources available for only a fixed period of time. The proposed access limits reflected the estimated needs of eligible countries over the period of the facility's operation. The actual figures would no doubt change in the light of the availability of other resources and the negotiation of programs with member countries. It was therefore difficult to set rigid rules for access at the present time. The intent of the words "norm" or "average" access at about 150 percent of quota reflected both estimated needs and the availability of resources. The proposed upper access limit of 350 percent of quota in exceptional cases was intended to allow for some flexibility. Access limits would be subject to frequent review by the Board and could be

revised as necessary. In that connection, an upward revision of access limits in the light of the use of resources was not intended to penalize "early comers." Countries were urged to enter into arrangements at an early date in view of the structure of the facility, which focused on three-year programs. If the pattern of use of resources did not materialize as envisaged, the Board could decide, inter alia, to extend the loan commitment period to cover a fourth year.

Extending the cutoff period for loan commitments to November 1989, while maintaining mid-1992 as the cutoff date for commitments by creditors, meant that little flexibility for program slippages would be available for late comers implementing a three-year program, the Deputy Director observed. Thus, the draft Instrument allowed for new agreements to be made with creditors if they wished to extend their commitment period. That aspect of the facility could be reviewed in light of experience. However, it was hoped that few countries would be only beginning programs as late as November 1989.

There was a diversity of views among Directors on the phasing and front-loading of disbursements, the Deputy Director noted. Several Directors preferred a uniform disbursement as the norm, while others suggested a 40 percent limit, and a few proposed limits beyond that level. The staff had proposed a 40 percent limit in view of the constraints posed by a fixed amount of resources and the assumption that those resources would become available in maximum annual amounts of one third of the total commitment by creditors over the three years of the commitment period. In the light of the Board discussion, the draft decision would be revised to provide some flexibility with respect to the front-loading of disbursements.

Responding to a question by Mr. Nimatallah, the Deputy Director remarked that the extension of the repayment period as a result of the extension of the drawdown period was an issue to be explored with the participants.

On the guidelines for lending operations, he wished to confirm that the staff would prepare for management's review a fairly detailed set of guidelines on how programs should operate and what the criteria should be for access under programs, the Deputy Director commented.

On the conditions for assistance, a Director had noted that the draft Instrument provided that a member should be making "a substantial effort" to strengthen its balance of payments position, whereas the Regulations for the administration of the existing facility called for "a reasonable effort," the Deputy Director recalled. That important distinction had been made in deference to the spirit of the decisions establishing the Special Disbursement Account and the use of reflows from the original Trust Fund for the structural adjustment facility--namely, the first credit tranche conditionality that had been applied to the Trust Fund arrangements. The distinction between "reasonable" and "substantial" had been made long ago in an Annual Report to clarify the difference between first credit tranche and upper credit tranche conditionality.

The distinction was made because an arrangement under the enhanced facility differed from an arrangement under the existing facility with respect to monitoring and, to some extent, the type of program it was expected to support. The availability of substantial additional resources meant that countries using those resources could undertake more difficult structural adjustment measures than would be possible with more restricted financing. More concretely, the condition of "substantial effort" reflected the fact that a substantially enlarged volume of resources entailed greater exposure on the part of creditors, and that monitoring to a large extent was intended to ensure that that exposure was protected and that programs were kept on track. Moreover, monitoring was intended to give guidance to the staff and to create a set of firm expectations for the authorities regarding the progress to be achieved, so that programs could unfold in a smooth fashion.

Responding to a question from Mr. Sengupta, the Deputy Director of the Exchange and Trade Relations Department confirmed that "substantial effort" was not intended to imply prior actions in addition to "reasonable effort." In that regard, it was expected that in those instances where the record of adjustment was poor or actions were needed to get the adjustment process started, prior actions might be warranted, and the staff would propose such actions to the Board. Indeed, prior action was an element of flexibility in arrangements.

The staff representative from the Legal Department remarked that the proposed decisions would be revised in the light of the Board discussion, and the understanding reached on any outstanding substantive issues would be reflected in the revised legal documentation to be submitted to the Board.

It had been suggested that some flexibility should be allowed in the proposed decisions so that additional provisions could be added when there was more clarification on some issues, the staff representative recalled. He had one caveat to offer in that respect. The Instrument was a complex one, and it would not be possible to keep all issues open. An issue might have an impact on more than one provision, so that additions could not be made without upsetting the whole structure. The degree of flexibility would thus depend on the substance of the issue.

On voting majorities, a majority of 70 percent of the voting power was needed for amendment of the Regulations for the structural adjustment facility because Article V, Section 12(j) called for a special majority for the adoption of the rules and regulations for the administration of the Special Disbursement Account, the staff representative explained. The adoption of the Trust decision required only a simple majority, because the Trust was an instrument under Article V, Section 2(b), and thus a special majority was not needed. The release of funds from the Reserve involved two provisions: one for release upon liquidation of the Trust, at which time the balances in the Reserve would be transferred to the Special Disbursement Account; and the second for a release of

resources whenever it was determined that the balances in the Reserve exceeded the liabilities of the Trust. In both instances, a simple majority of the voting power would be required.

Access to the Fund's general resources to provide some liquidity to claims on the Trust was discussed in detail in the staff paper on operational arrangements, the staff representative noted. Two aspects of the approach available under the Articles would require a decision by the Board--namely, if the Board desired to exclude purchases from the calculation of the reserve tranche, and if it desired to adopt repurchase periods that were different from the normal repurchase periods described under Article V, Section 7.

On the meaning of the Fund's commitment with respect to the residual risk, he could confirm that "all initiatives" included all courses of action that were or would be available to the Fund, including the sale of gold, the staff representative remarked.

Responding to a question from Mr. Sengupta, the staff representative from the Legal Department commented that there was no anomaly between the requirement of a 70 percent majority of the voting power to amend the Regulations for the structural adjustment facility and the requirement of a simple majority to amend most of the provisions of the Trust Instrument. However, some complexity was involved in that the Trust Instrument contained a reference to the Regulations. Section II.D of the Trust Instrument referred to paragraph 14 of the Regulations: assistance under the Trust Instrument would be provided, in principle, under the same conditions and on the same terms as loans under the structural adjustment facility. Thus, in principle, the provisions on assistance from the structural adjustment facility in the Regulations also applied to the assistance from the Trust. Since amendments to the Regulations required a 70 percent voting majority, the same majority would be required to amend the provisions on Trust loans through an amendment of the Regulations for the structural adjustment facility.

The Deputy Treasurer recalled that a number of Directors had commented that it was important that the Trust's borrowing and lending operations be denominated in SDRs. The staff also attached importance to that point. It was not evident that the Trust could engage in operations to obtain SDR cover for borrowing in currencies, or what the cost of such operations might be. If the Trust were to borrow in local currency, a substantial exchange risk might be imposed on borrowers, or the Reserve might be exposed to exchange risk, thereby impairing its capacity to provide the security that was of great importance to a number of creditors. Thus, the denomination of the Trust's borrowing and lending operations was an important issue.

A distinction could be made between the denomination of loans to the Trust and the denomination of grants for the Subsidy Account, in the sense that grants denominated in local currency would not entail the same problems for the Trust's operations that he had described, the Deputy

Treasurer continued. However, the denomination of grants in local currency did add another element of uncertainty about the adequacy of the grants to achieve the desired interest rate target of 0.5 percent on loans from the Trust. Thus, although there were technical distinctions that could be made between the two types of operations, the possible problems associated with grants in local currency led the staff to hope that grant commitments could be expressed in terms of SDRs.

The Chairman remarked that he also wished to confirm that the reference in the draft decision on the establishment of the Trust to "all such initiatives as might be necessary to assure full payment to lenders" had to be understood to include sales of the Fund's gold.

The Executive Directors agreed to continue their discussion on December 15, 1987.

2. EXECUTIVE DIRECTOR

The Chairman bade farewell to Mr. Sugita upon the conclusion of his service as Alternate Executive Director.

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/87/167 (12/7/87) and EBM/87/168 (12/11/87).

3. RELATIONS WITH GATT - CONSULTATION WITH CONTRACTING PARTIES -
FUND GUIDANCE

The Executive Board approves the recommendation by the Committee on Liaison with the CONTRACTING PARTIES to the GATT with regard to the guidance statement for the Fund representative attending the GATT consultation with Peru on December 15, 1987, as set forth in EBD/87/308, Supplement 1 (12/7/87).

Decision No. 8747-(87/168), adopted
December 10, 1987

4. STAFF COMPENSATION ISSUES - TAX ALLOWANCE - REVIEW AND
MODIFICATION OF AVERAGE DEDUCTION SYSTEM

The Executive Board approves the recommendations with respect to the review and modification of the average deduction system in the light of the 1986 Tax Reform Act as set forth in EBAP/87/238, 11/2/87; Correction 1, 11/6/87; Supplement 1, 11/5/87; Supplement 2, 11/13/87; and Supplement 3, 11/25/87.

Adopted December 9, 1987

5. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors as set forth in EBAP/87/265 (12/4/87), EBAP/87/268 (12/7/87), and EBAP/87/269 (12/9/87) is approved.

APPROVED: July 25, 1988

JOSEPH W. LANG, JR.
Acting Secretary