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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 87/175

10:00 a.m., December 18, 1987

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

Executive Directors	Alternate Executive Directors
A. Abdallah	
Dai Q.	Jiang H.
C. H. Dallara	M. K. Bush
J. de Groote	L. Hubloue, Temporary
	E. V. Feldman
M. Finaish	
G. Grosche	B. Goos
J. E. Ismael	J. Reddy
A. Kafka	
	C. Enoch
M. Massé	D. McCormack
	C. V. Santos
Y. A. Nimatallah	I. A. Al-Assaf
G. Ortiz	
	M. Fogelholm
H. Ploix	D. Marcel
G. A. Posthumus	G. P. J. Hogeweg
C. R. Rye	C.-Y. Lim
G. Salehkhou	O. Kabbaj
	L. E. N. Fernando
K. Yamazaki	S. Yoshikuni
S. Zecchini	

C. Brachet, Acting Secretary
R. Gaster, Assistant

Also Present

Central Banking Department: D. R. Khatkhate. European Department: M. Russo, Director; O. P. Brekk. Exchange and Trade Relations Department: L. A. Whittome, Counsellor and Director; J. T. Boorman, Deputy Director; A. Basu, J. Berengaut, D. Burton, A. Chopra, G. G. Johnson, S. Kanesa-Thasan, D. Lee, C. Puckahtikom, P. J. Quirk. External Relations Department: C. S. Gardner, Deputy Director; D. D. Driscoll. Fiscal Affairs Department: V. Tanzi, Director; A. A. Tait, Deputy Director; E.-A. Conrad, V. P. Gandhi, P. S. Heller. IMF Institute: Wong C.-H. Legal Department: A. O. Liuksila, J. V. Surr. Middle Eastern Department: M. D. Knight, M. Yaqub. Research Department: E. Hernández-Catá, M. S. Kumar, G. R. Le Fort. Treasurer's Department: D. V. Pritchett. Western Hemisphere Department: S. T. Beza, Director; M. Caiola, Deputy Director; G. Yadav. Bureau of Statistics: J. B. McLenaghan, Deputy Director. Personal Assistant to the Managing Director: H. G. O. Simpson. Advisors to Executive Directors: M. B. Chatah, G. D. Hodgson, K.-H. Kleine, P. D. Péroz, G. Pineau, D. C. Templeman, A. Vasudevan, J. E. Zeas. Assistants to Executive Directors: N. Adachi, E. C. Demaestri, S. K. Fayyad, M. A. Hammoudi, C. L. Haynes, G. K. Hodges, S. King, K. Kpetigo, M. A. Kyhlberg, V. K. Malhotra, D. V. Nhien, C. Noriega, W. K. Parmena, L. M. Piantini, S. Rebecchini, A. Rieffel, S. Rouai, D. Saha, G. Schurr, E. L. Walker, R. Wenzel, I. Zaidi.

1. MONITORING OF STRUCTURAL ADJUSTMENT IN FUND-SUPPORTED ADJUSTMENT PROGRAMS

The Executive Directors considered a staff paper on the monitoring of structural adjustment in Fund-supported adjustment programs (EBS/87/240, 11/20/87; and Cor. 1, 12/28/87), together with a paper containing background material (EBS/87/254, 12/3/87), and a departmental memorandum on approaches to trade liberalization in developing countries (DM/87/4, 12/3/87).

Mr. Hubloue made the following statement:

The compatibility of structural and growth-oriented reform policies with the legal prescriptions concerning the revolving character of the Fund's resources still seems to be a source of concern to some, but I do not take that position. On the contrary, structural reforms are often more capable of ensuring the revolving application of Fund resources than traditional demand-management policies, because the former's balance of payments results are more durable and because their positive effect on a country's growth performance facilitates the servicing and reimbursement of foreign debts. The overriding need to safeguard the revolving character of Fund resources should also be reflected in our guidelines on conditionality. The need for the Fund to pay due regard to members' social and political objectives--Guideline 4--should be assessed and interpreted in the light of the equally important need to address the real causes of members' balance of payments problems, including any structural or systemic rigidities which prevent members from combining growth with external viability. As to Guideline 9, I suggest, once again, that the language describing the scope of performance criteria be expanded to include "such structural or systemic variables as are essential to the effectiveness of a member's program because of their impact on the viability of the balance of payments position in the medium term."

This proposal to update and amend the guidelines does not aim merely at a cosmetic adjustment of our formal decision. It aims instead to give the staff the legal authority and the obligation to negotiate future Fund arrangements on the basis of all the relevant policy actions deemed essential to restore balance of payments viability in the medium term. The staff should express the resulting judgments in the form of performance criteria which are unambiguously linked to the required policy changes. Although the Fund's interest in structural adjustment has increased dramatically in recent years, in many cases the traditional credit and fiscal ceilings are still the only binding elements of Fund programs; other structurally oriented policies--such as the reform of financial and subsidy systems, or the reform of public enterprises--become binding only through their effects on the credit and public deficit ceilings. This situation should be changed so that structural reforms can be judged on their own merits and monitored in terms of their overall effects on the member's medium-term viability. It is in the light of these overall effects that Secretary Baker's proposals for growth-oriented arrangements take on their full importance; these proposals have my strongest support.

I do not suggest that structural reforms should displace the reduction of domestic demand pressures from the core of Fund arrangements in all cases. The staff is correct to suggest that the scope of the reforms to be undertaken by a member and the policy areas involved need to be determined on a case-by-case basis, and that the need for reform may be less pressing in countries which have shown the ability to adapt their policies flexibly to the pursuit of macroeconomic objectives. Nonetheless, cases also exist in which the rigidities in the economic system are so well entrenched that only a priori actions on those structural rigidities can pave the way for flexible economic decisions in the future.

On policy design, the staff has drawn an important distinction between reforms aimed at replacing government intervention systems with market-based structures, and reforms which are limited to the improvement of government intervention. This distinction is especially relevant in cases involving systemic reforms. The Fund's policy of leaving the choice between these fundamentally different approaches to the member's discretion is of course an important confirmation of the Fund's neutral stance with respect to the member's most essential economic and political objectives. While this neutrality should be preserved under all circumstances, the Fund should not hesitate to support the process with programs which clearly outline the sequence and timing of all steps to be taken to complete the chosen reform process successfully.

The monitoring of structural reforms should start on the occasion of the Fund's regular Article IV consultations. Prior knowledge of each country's specific situation and distortions is a sine qua non for monitoring the reform process, and the Fund should invest the staff work necessary to acquire that knowledge. A more systematic use of structural indicators can contribute significantly to this learning process, and improve our analytical knowledge of the interactions between structural parameters and the balance of payments. Besides the existing efforts thus far in this area, I would encourage the staff to explore the extension of the indicator approach to the monitoring of public enterprise performance and price subsidies--two areas where reforms are usually urgently needed and where quantified assessments should not be too difficult to obtain.

The Fund's technical assistance functions should be more systematically integrated into the monitoring of structural reforms. The staff has stressed that many structural distortions in countries' financial systems--and I would say in their fiscal systems as well--are in the last analysis due to the lack of sufficient expertise to administer sound and flexible systems. Lack of expertise has also been revealed as a major factor in countries' mixed results with World Bank structural adjustment loans. The Fund has two departments with special expertise in these areas, and their activities should be more systematically associated with each stage of the Fund's involvement in the monitoring of structural adjustment.

Alternative reform processes require alternative monitoring techniques. I support the staff's general proposition that changes in the administration of government interventions in the economy can usefully be monitored by means of intermediate indicators such as the behavior of key prices, while bolder systemic reforms should preferably be monitored on the basis of a detailed sequence of decisions to be taken at each step of the reform process. In the latter case, decisive action at the outset of the program will normally be desirable, to announce the launching of the reform process. Whether subsequent steps should be formulated as performance criteria, or, alternatively, monitored in the context of program reviews, is perhaps more a matter of presentation than of substance; after all, a program review can be given the legal status of a performance criterion. What really matters is for the review to be sufficiently binding to trigger an objective assessment of whether the progress which has been made in critical areas is sufficient to justify the continuation of Fund disbursements under the program.

The speed and timing aspects are of the highest importance for the monitoring of structural reforms, especially in relation to the demand-management aspects of the program. One argument stressed during the discussion on December 16, 1987 by Mr. Rebecchini concerns the different time spans for the implementation of structural and demand policies. Another important argument is raised on page 6 of EBS/87/240, where it is mentioned that liberalization measures can initially pose a serious threat to the financial stabilization imposed by traditional demand management, and it is suggested that systemic reform measures might consequently have to be postponed until the domestic finances have been stabilized. I doubt the merits of such an approach, which perpetuates distortions in favor of short-term stabilization and increases the risk that the need for reform will be less clearly perceived once the financial situation has temporarily been brought under control. Structural reforms should never be postponed, but should be accompanied by a more flexible monitoring of the program's demand-management components. In any event, further research on the interactions between the structural and demand components of Fund arrangements still seems needed, as these two components cannot be designed or monitored as independent blocks of a single program.

I support the proposals for reactivating the extended Fund facility, because this facility was specifically created to address payment imbalances relating to structural maladjustments and because it already broadens the scope of performance criteria by linking Fund disbursements to the implementation of policies which are necessary for achieving the program's objectives. I am confident that a more formal and systematic application of these principles will eliminate many of the weaknesses of earlier extended arrangements, and I look forward to further discussion of the issue.

Mr. Reddy made the following statement:

Generally, reform packages should not be too ambitious, as overambitious programs are bound to fail. The programs should therefore be realistic, based on attainable targets and objectives. In designing structural adjustment programs, we must not lose sight of the administrative difficulties of the member in implementing the programs, and the importance of simplicity in program design cannot therefore be overemphasized.

One question concerns the specific areas of structural reform to be addressed in Fund-supported programs. That will have to be determined on a case-by-case basis, taking into account the specific circumstances of the country and the nature and extent of distortions. I agree with the staff that we should not prejudge the areas of reform to be included in the program, but experience suggests that four areas should be approached with caution. First, we should be careful in calling for the elimination of consumer subsidies intended to protect the poorest sections of the community, as these subsidies have significant social and political implications. Second, caution is warranted in seeking the elimination of agricultural subsidies, which could be a useful instrument for providing incentives in some developing countries. Agricultural subsidies tend to be more prevalent in industrial countries when, in fact, they are better justified in developing countries. Third, we must be cautious in asking developing countries to reduce import tariffs at a very early stage of their development, when the export sector has not gained enough strength and when the balance of payments position remains fragile. The intensification of protectionism in industrial countries creates additional uncertainties for developing countries' exports, and great caution should therefore be exercised in asking developing countries to lower their tariffs prematurely in the context of Fund-supported programs. Fourth, we need to avoid promoting excessive diversion of resources to the export sector, which could lead to the neglect of domestic production, especially food production for local consumption, and possibly serious social consequences.

Not every type of structural reform will lend itself to precise quantification. Thus, while structural indicators might serve a useful purpose, a mechanical application of such indicators should be avoided: a substantial element of judgment should be applied in using indicators on a case-by-case basis. I agree with the staff that the identification and solution of structural problems can be undertaken even without the assistance of sophisticated indicators, and that this should be done wherever possible.

The staff should take a pragmatic approach to program design on a case-by-case basis. Some economies, and quite often certain sectors within individual economies, are more attuned to market-oriented solutions for improving incentives than others, where a regulatory approach may be more appropriate. On occasion, it may even be possible to use a blend of the two approaches to get the best results. The staff will have to make a judgment in each case as to the most efficient and politically feasible approach.

Prior actions, performance criteria, and reviews have a role to play in the choice of monitoring techniques, but it is not desirable to devise firm rules about the types of reforms that should be monitored by one technique or another. A variety of factors would have to be taken into account, particularly the time required for the preparation and implementation of certain types of reforms. I would, however, like to see the program kept as simple as possible and performance criteria restricted to a relatively few benchmarks. In addition, great care should be taken in the use of prior actions. Some reforms take time to formulate, while others, once formulated, will have to be implemented over an extended period, and prior actions will clearly be inappropriate in the latter cases. In addition, we should not insist on prior action if there are potential social and political problems associated with it, provided that the member is willing to give a firm commitment to carry out the reforms in installments during the program period. Insistence on prior actions can sometimes lead to complete disengagement of a member, which may not be very productive. It is more important for a member to be brought within the ambit of the program, and for agreement to be reached on a phased program of reforms over the entire program period, so that the reform process gets under way without causing any serious social or political difficulties. In such cases, the actual disbursement will have to take account of progress in the implementation of the program.

There has now been sufficient satisfactory experience in the area of Fund-World Bank collaboration on preparing the policy framework papers for the implementation of the structural adjustment facility. The staff can usefully build upon this experience, and can perhaps improve somewhat the coordination of timing and monitoring.

On the issues of surveillance, I support the proposal to improve the appraisal of structural aspects of members' economies as part of Article IV consultations. To this end, consideration might be given to the inclusion of World Bank staff on Article IV consultation missions.

Technical assistance will be of crucial importance, in both formulating and implementing structural adjustment arrangements. High priority should therefore be given to providing technical assistance to all countries eligible for arrangements under the structural adjustment facility.

Finally, on the guidelines on conditionality, Guideline 4 remains appropriate.

Mr. Ortiz made the following statement:

Today's discussion focuses on a difficult and sensitive topic--the extent to which the Fund should be involved in structural policies, and the extent to which this involvement should be reflected in program design. This question, which obviously must be raised before entering into the details of monitoring, gives rise to a number of difficult issues.

If the Fund is to move in the direction of growth-oriented programs, there must be a recognition that structural policies ought to play a greater role in program design. However, as several Directors noted during the discussion on December 16 (EBM/87/173 and EBM/87/174), the Fund is--and should remain--a monetary institution, and should therefore not seek to take on the functions of a development bank. The question here is whether a growth orientation for Fund-supported programs is compatible with the monetary character of the Fund. It would appear that there are still some doubts in this respect. This implies, in turn, that we should begin by elucidating our definition of growth programs.

The discussion on December 16 showed that there is no consensus regarding the direction in which the Fund should move. If--as some said--growth is merely a fashionable password or a convenient catchword to add some appeal to traditional Fund-supported programs and thus make them somewhat more marketable, then the focus on structural reforms will probably remain at that same rhetorical level. There is also the idea--often voiced in the Board--that the growth orientation of Fund programs should essentially consist of adding "microconditionality" to the existing array of more traditional conditionality applied to macroeconomic variables, while everything else--including the financing and the time horizon of the adjustment program--remains the same. This is clearly the worst of both worlds.

Focus on structural reforms should be a function of the Fund's commitment to designing programs in which economic growth is one of the key objectives. While growth cannot be guaranteed, a government's ability to fine tune economic growth is not a precondition for the setting of growth targets in Fund-supported programs. After all, governments are also usually unable to fine tune the balance of payments, but this does not preclude us from setting reserve targets.

The growth orientation of Fund-supported programs must imply a movement away from the strict interpretation implied by the availability of resources approach. Otherwise, the new growth-oriented programs will be indistinguishable from the traditional ones. In the context of growth exercises, it will be necessary to determine the external financing requirements, along with the domestic savings necessary to attain realistic growth rates. In this context, an appropriate diagnosis of structural problems, and of the reforms which are considered essential to overcome important obstacles to economic growth, should be accomplished. If the required external resources greatly exceed those readily available, or if the country has utilized its debt capacity to the maximum--defined as the point after which additions to foreign debt may hinder rather than foster growth--the Fund should be candid, and should either attempt to catalyze additional concessional resources whenever possible, or determine the amount of debt reduction necessary for the resumption of economic growth under a Fund-supported program.

In this area, the enhanced structural adjustment facility offers a unique opportunity to deal more effectively with the problems of low-income countries, aiding them to resume economic growth; this would be the case if debt relief on concessional terms is forthcoming in tandem with enhanced structural adjustment facility resources from official creditors, in line with the U.K. and French proposals.

Growth exercises should be applied, at a minimum, to gauge the consequences for economic growth of any proposed program, even if it is of the more traditional type. In the presence of a balance of payments disequilibrium, countries could be given a choice between adopting a more traditional program aimed at correcting the short-term disequilibrium mostly through demand-management measures, or adopting a more comprehensive and far-reaching growth-oriented program in which structural measures--which fall within the sphere of competence of the Fund--could be given a more prominent role, perhaps in the context of a reformed extended arrangement. Of course, the timing and financing of such an extended program would have carefully worked out so as to establish adequate conditions for growth.

The Fund should not attempt to identify precisely the circumstances and ways of incorporating structural reform in its programs, or to comment in an abstract sense about, inter alia, prior actions and reviews--which have to be tailored on a case-by-case basis.

Let me conclude with the following observations. First, as the staff paper notes, structural policies often touch on areas in which the authorities have specific social and political objectives. While it is appropriate for the Fund to point out the possible inefficiencies that such policies may generate, it is clearly outside the scope of Fund activity to insist on reforms outside its sphere of competence. There are also clear overlaps with the activities of the World Bank--a key issue not seriously addressed in the paper, except to say that cooperation is proceeding so well that any potential problems will be resolved. Second, if, as became clear during the discussion on December 16, we should be humble about claiming to understand the interrelation between economic instruments and objectives--in both financal programming and growth models--this is even more the case when dealing with issues of structural reform. We are unsure of the effects of reforms--which vary from country to country in the fiscal, trade, and prices areas--but we are even less sure of the appropriate sequencing of the reforms.

In any event, the renewed emphasis on structural policies should not lead to a further proliferation of performance criteria. On the basis of the argument that the monitoring of such policies is essential for balance of payments viability, the number of performance criteria could be extended indefinitely, since every variable is connected in a general equilibrium system. In these circumstances, one should be extremely careful in setting specific and rigid agendas for policy reform and in attempting to specify detailed macroeconomic conditionality.

Finally, for all these reasons, considerable political commitment from the authorities is essential, especially in programs that contemplate a substantial degree of structural reform.

Mr. Kafka made the following statement:

Even assuming that structural reform is a legitimate subject for the Fund, it does not follow that all Fund-supported programs need to contain elements of structural reform, even those elements which clearly fall within the field of the Fund's competence. If a member wishes to adopt a program without elements of structural reform, I can see no general justification--either under our Guidelines, especially Guideline 4, or otherwise--why the Fund should insist on including such elements. Certainly, the basic principle of Article V, Section 3(a) can be compatible with the correction of payments problems even if the method adopted is less than optimal from the growth point of view, as it could well be in the absence of structural reform. Possibly, but by no means necessarily, the maturity and volume of Fund resources required for a program with structural reforms could be shorter or smaller, respectively, than for one without such reforms.

In determining the degree to which it is legitimate for the Fund to insist on including structural reform elements in a program, the problem of symmetry cannot be overlooked. In an interdependent world, the effectiveness of a given country's structural reform policy, like that of its macroeconomic adjustment policies, depends very much on the policies of other countries. Where balance of payments viability over a reasonable period is not negated, programs without structural reforms cannot be justifiably refused--particularly when the welfare or output yield of structural reform measures adopted by the program country is reduced by the absence of complementary structural reform measures in partner countries. I am not denying that unilateral measures can be helpful; they may, nevertheless, be too costly politically if their yield is small, and they may have a negative economic yield over time because the political problems created by the initial measures provoke resistance to effective follow-up measures. As a practical matter, one need only refer to the recent statement of the Institute of International Economics to see how inadequate even macropolicy complementarity--between developed and developing countries--is today. If the Fund had substantial influence over the major countries, it could promote structural reforms in its programs more decisively; but the fact is that the Fund lacks such influence.

Even when a country wants structural reforms, the Fund should be careful--not negative--about including them in its programs. The experience of the Fund--and the World Bank--in this area is, after all, limited. As the December 16 discussion showed, there is considerable doubt about our understanding of the effects of structural policies--even more than about the effects of macroeconomic policies. In addition, structural reform requires a much closer involvement in national decision making than do macroeconomic policies, and we must eschew even the impression or suspicion that we want to govern our program countries from Washington. This consideration is particularly important since we have recently had a frightening proliferation of macroeconomic performance clauses; simply adding microeconomic ones would be extreme folly. In fact, the proliferation of performance clauses makes effective government impracticable, and we should start restricting the number of macroeconomic clauses before we start adding structural ones; I am convinced that we would not lose significant ground. We need not operate with our program countries on the basis of distrust. One of the reasons why the World Bank is--at this stage--still less unpopular in the developing world than the Fund is simply its different approach to program monitoring.

How then should we formulate and monitor the structural part of our programs when such a part is desirable? The staff seems inclined more toward prior action or review clauses than toward performance clauses, since the latter require a particularly high degree of specificity. At first sight, this seems sensible; yet there are obvious limitations to prior actions. There are, for instance, sequencing problems--some of the most difficult problems to determine.

Review clauses are probably preferable for both structural and macroeconomic policies. I assume that when the staff speaks of structural review clauses, those are the only performance clauses, not a supplement to other qualitative or quantitative performance clauses. We have missed the opportunity to use review clauses in a similar--alternative--mode in the case of macroeconomic policies. Yet, it would also be a mistake to underrate the problems of review clauses as an alternative to other performance clauses. Review clauses require a high degree of trust between program countries and the international agency concerned, and Fund policy has increasingly been based more on distrust than on trust--which is reflected in the attitude of our members. A way out of the dilemma, pending the re-establishment of mutual trust, may well be review clauses based on indicative limits, combined with review periods longer than those usually adopted.

The tracking of structural aspects of member countries' programs during Article IV consultations can only be helpful. In many cases in which I could not justify the inclusion of structural reforms as performance clauses or prior actions or matters to be considered under review, I would have no hesitation in supporting their consideration in the course of Article IV consultations.

As in the case of macroeconomic policies, we should consider the extent to which contingency clauses should be provided for in the context of structural policies. It is quite possible that exogenous developments could impinge strongly on certain variables that affect the structural reforms to which a country has committed itself in the expectation that the values of these variables would remain within tolerable limits. An example of such a reform might be a freezing of interest rates. In these cases, it would be desirable if it was understood at the outset that the indicative limits would be stretched if certain developments--outside the control of the program country--occurred.

There are areas of structural reform where World Bank experience may be very helpful to the Fund, and vice versa. Nevertheless, for the time being, we should not subvert the separate existence and tasks of the two institutions by imposing on them an excessive intimacy in cooperation. The accepted strictures against cross-conditionality are a case in point.

Mr. Fernando made the following statement:

During our recent discussion on growth exercises, we agreed that uncertainties relating to behavioral relations and to exogenous variables would be large in programs that explicitly recognize growth as an objective in addition to balance of payments adjustment. In that context, it was recognized that transaction mechanisms would have to be determined more closely before we can recommend any set of structural policies with confidence. Policy prescriptions should also fit the circumstances of the country concerned, and should not be developed in a mechanical way.

These are very important conclusions, although they could, in purely operational terms, imply the need for an increase in the time required to design a program of adjustment with growth. Meanwhile, structural policies would be incorporated into most programs on intuitive grounds, but would be justified by using the word growth as a catchword or password, without necessarily targeting it. I doubt whether there will be any tangible modifications in either program design or conditionality in the near future.

Although many Directors have emphasized the need for growth-oriented adjustment to support wide-ranging and often specific structural policies, the staff does not seem to share this view completely. The staff argues that in considering the approach of the Fund to the question of structural reform, the basic concern is how such reforms relate to the objective of achieving balance of payments viability over the medium term. The paper also states that Fund-supported programs have frequently addressed impediments to the efficient functioning of the external sector through attention to, inter alia, exchange rate policy and the pricing of tradable goods. The view is expressed that such reforms "may also lead to stronger growth of income and output." But the staff wants to retain its option of introducing structural policies on grounds other than strict external adjustment; hence the argument that while emphasis should be on reforms that influence the external sector directly, "there is no a priori basis for general exclusion of particular areas of reform. Rather, the specific areas to be addressed will need to be determined on a case-by-case basis in light of the country's circumstances, taking account of both the magnitude of the distortions involved and the extent to which they bear on external viability, as well as other considerations, such as whether the World Bank is playing a complementary role in assisting the country in its structural reforms" (EBS/87/240). Such policies could therefore be based on any consideration, sublime or not so sublime, including growth and the role of World Bank. Does this defense of structural reforms imply a specific role for commercial banks in the adjustment process, at least in the case of highly indebted countries?

I do not completely agree with the staff's view of the Fund's role in promoting policies that bring about structural changes. The staff view implies that policies could be recommended on an a priori basis, without putting in place a proper linkage of policies and effects. This I do not accept.

There is another reason why we should not go too far in recommending wide-ranging structural measures. Structural reforms are--at least so long as financial programming is the main basis of program design--not consistent with the present guidelines on conditionality. In fact, nowhere in the guidelines do the words "structural" or "growth" occur. The staff recognizes this, but states that structural adjustment "clearly may go to the heart of the domestic, social, and political objectives of members, referred to in Guideline 4." There is however a lack of conviction in this presentation. The record of the Board discussions in 1979 on the guidelines on conditionality does not generate a feeling that structural adjustment was given serious attention. It was definitely not in mind when the guidelines concerning monitoring, prior actions, performance criteria and reviews were devised. And under Guideline 10, there is serious doubt whether the present practice of examining structural policies during the reviews as a regular feature in most programs is consistent with the guideline, which requires that only "an essential feature" of a program, a feature which cannot be a performance criterion, could be reviewed in "exceptional cases."

What do these reviews imply after all in the context of stand-by arrangements, when we all know and agree that long lags exist between the implementation of structural policies and their impact on macroeconomic variables? At best, reviews give us--during the period of stand-by arrangements--an idea of whether the suggested structural measures have been put in place at all. Any delays are due to "the circumstances"--social, political, and legislative--of the country concerned, and the Board would have to be mindful of these circumstances and show flexibility. This flexibility is all the more necessary because in devising structural policies, the countries--particularly the low-income developing countries--are rarely consulted about the feasibility of the policies and about their administrative capacity to implement them, even when arrangements are for a relatively longer period. This is borne out by our experience in 1987 in the formulation of policy framework papers, used for providing assistance under the structural adjustment facility, a process in which no qualifying country authority was involved.

I am not opposed to recommending structural policies per se. My difficulty with the present practice of providing policy suggestions is, first, that these suggestions lack a clear analytical basis; second, that they are often not tested empirically with reference to the country concerned or to countries similarly placed; and third, they are not accompanied by adequate flows of external financing.

In Section III of EBS/87/240, the staff proposes that diagnosis and monitoring of structural reforms can be done more precisely by using indicators that measure the magnitude and impact of distortions. The other papers give a host of possible indicators that might be considered. The practicality of this suggestion should be considered against the background of Fund exercises on economic indicators in multilateral surveillance over major industrial countries, where information and relationships are relatively well known. The indicators exercises took more than a year, and there is still no full agreement about the number and the type of indicators that should be used in multilateral surveillance. In many developing countries, qualitative and comprehensive data are often not available, which makes the analysis of historical relationships hazardous. Besides, some of the suggested indicators are of doubtful validity--for instance, real interest rates, dispersion of lending rates across sectors, and cash flow data on a continuing basis for major public enterprises and their nominal tariffs. Are the indicators supposed to indicate the policy measures to be undertaken, or the degree of implementation of the measures, or the link between the measures to any specific set of objectives, or all three? If the indicators are not to be used for addressing structural problems, then they are nothing more than mere data about the structural weaknesses or problems, in which event we need not try such sophisticated techniques as working out real interest rates on the basis of expected inflation rates.

The staff favors specifying in detail the measures to be taken during a specific planning period, and focusing on the important structural reforms. It is, however, difficult to formulate a priori the optimal sequence in which structural reforms should be implemented. It is equally difficult to draw up a detailed plan of reforms to generate speedier adjustment, given inadequate data bases, insufficient certain knowledge about the impact of reforms within a given period, administrative difficulties, and long lags in operation. For these reasons, the Fund's approach to structural reform should be flexible.

I expressed doubts at the outset concerning the introduction of monitoring of structural adjustment in stand-by arrangements in the context of the existing guidelines on conditionality. It is, however, possible to envisage structural policies in extended arrangements that use reviews as a monitoring technique, assuming that the policies underlying these programs are well tested empirically.

On Fund-World Bank collaboration, I have made my views known on previous occasions: cross-conditionality in the name of monitoring and policy framework formulations should be avoided. Nor should this collaboration mean that the policy framework for structural adjustment will be prepared solely by the staff of the Fund and the World Bank; authorities' views should be fully reflected in such a framework.

On surveillance and technical assistance, Article IV consultations provide occasions on which to identify structural problems and to discuss possible lines of action. Technical assistance would need to be provided to countries to build up the data base, to generate information on institutions, and to help to train nationals in policymaking and monitoring.

Finally, empirical evaluations are necessary to compare the structural reforms that have been undertaken in some countries with program objectives, so that suggested measures would have more credibility. Conditionality must not be intensified for its own sake, but should be set appropriately. The danger in being overenthusiastic about the monitoring of structural adjustment is that many programs could fail and require a number of midcourse revisions or waivers. Such possibilities should alert us to the need to be cautious and flexible in recommending and monitoring structural adjustment.

Mr. Enoch made the following statement:

The staff papers lay out the issues very well, and I can certainly endorse their general findings. I fully agree with the staff view that there are no hard and fast rules on the circumstances in which conditionality should be attached to structural measures. Much will depend upon the situation facing the member concerned, its economic and social objectives, and the nature of the imbalances that it faces. But in general, once policies have been implemented, it is surely essential to have effective monitoring in some form: monitoring should not necessarily be associated with restrictiveness; rather, it rests on the elementary point that all participants in the program--in particular, the country concerned and the Fund--should wish to follow the progress of the program as closely as possible.

There will generally be a continuum of adjustment packages available to the authorities, containing different mixes of the various demand-management and structural adjustment measures open to them, although the relative efficacy of the policies will vary across countries. Within the key objective of ensuring balance of payments viability, different combinations of measures may often have different implications for growth. One of the responsibilities facing the staff in devising programs is to identify these alternatives and to advise the authorities on their respective implications. In some cases, programs may have almost no structural adjustment content, and there is nothing intrinsically wrong with this. Indeed, this may well be the most appropriate course when the major cause of disequilibrium in the economy is excessively loose fiscal and/or monetary policy. In many cases, however, demand-management policies alone may not be sufficient to achieve a viable external position. In these cases, the Fund must inevitably become involved with structural adjustment measures.

On occasion, the Fund has supported adjustment programs which seem to place excessive reliance upon demand-management restraint--deriving, for example, from failure to confront exchange rate issues. Adjustment through excessive demand restraint may improve the balance of payments but in a way that is unlikely to prove sustainable. Even if the authorities stay the course for a while, the pressures for higher growth are likely to mean that the temptation to relax the restrictive policy stance is bound to increase the longer the policy continues. By supporting such a stance, the Fund only reinforces the myth that its programs are inimical to growth.

Perhaps, however, one should not make too much of this problem. In some cases structural and demand-management policies are substitutes, in others independent, and in others complements. Criticizing one or other aspect of such policies--especially in the case of complements--seems unproductive: the Fund basically produces a package of measures which have to be assessed and monitored in their totality.

Although the structural content of adjustment programs will vary from case to case, structural matters in some form are likely to be important in most Fund-supported adjustment programs, as well as--inter alia--in Article IV consultation reports. While no hard and fast rules can be given, it is the external sector which is most directly related to external viability. In this regard, I attach particular importance to trade policies in the Fund's surveillance work. This is a key area from the standpoint of ensuring efficient resource allocation, and it is also clearly central to the Fund's mandate. This is not just an issue for Fund programs. Article IV consultation reports should therefore always contain a detailed description of the country's trade and tariff system.

Structural adjustment on the external side cannot be separated from domestic adjustment measures--reforms of public sector financing and of parastatals, for instance--and the Fund will doubtless continue to emphasize these areas. But while indicators and monitoring may cover domestic adjustment, external viability should remain the center of attention. This, after all, is where the expertise of the Fund, rather than that of the World Bank, has generally rested.

Wherever possible, structural adjustment measures should be included as prior actions, or at least as very early actions. This will help to reinforce the private sector's confidence in the authorities' adjustment program. Prior action will not always be possible, however, and in other cases, structural measures will be better included as performance criteria or as conditions of program reviews. Where structural adjustment measures are of great importance to the successful completion of the program, the relevant understandings need to be specified in considerable detail.

In discussing the structural measures to be included in a program, the staff should also produce a reasonably full description of the background to the understandings concerned. It is, for instance, of little use to be told that the public enterprise sector in a particular country is inefficient, and that understandings have been reached on two particularly important enterprises, if one is not also aware of the size and scope of the other enterprises. It would be helpful, therefore, if the staff could present broad descriptions of the institutional background to key structural areas. Similarly, where the agricultural sector plays a central role in the economy, staff papers should set out the level of producer prices in the country concerned in comparison with prices in world markets and neighboring countries.

In designing and implementing a comprehensive set of structural reform measures, the authorities may well need technical assistance from the Fund. To maximize the return on our limited assistance budget, assistance should be allocated to the areas where it will have the greatest impact in support of comprehensive adjustment programs.

The Fund and the World Bank have different mandates and should continue to concentrate upon these separate areas of expertise. There is little point in the Fund trying to duplicate the World Bank's role, as this would be wasteful and could lead to the two institutions giving conflicting advice, which would clearly be counterproductive. However, even if the Fund and the World Bank retain separate areas of interest, they clearly have common interests in many areas and will have to work closely together. There are some countries where there is at present only limited World Bank involvement; in these countries the Fund will have to take more of the lead.

The staff papers generally regard the type, and importance, of structural measures to be the same whatever the type of Fund facility under consideration. Structural adjustment measures, however, appear to take longer to work their way fully through the economy than do conventional demand-management policies, although some counterexamples--some aspects of the Philippine programs, for instance--can be suggested. Structural adjustment will therefore be relatively more important in adjustment programs in direct proportion to the length of the overall program. Thus, extended arrangements, for instance, may tend to have a larger structural component than stand-by arrangements. Indeed, the Board has agreed--for instance, in the November 1987 discussion on Ghana--that an extended arrangement should not be simply a succession of stand-by arrangements, and should have a number of specific structural adjustment objectives. As enhanced structural arrangements are also relatively long term in nature, they too will include significant structural components. Indeed, as the enhanced structural adjustment facility is a once only, exceptional facility, it would seem a particularly appropriate vehicle for significant structural reform. Given the seriousness of the initial position of many of the countries embarking on an arrangement under the enhanced structural adjustment facility, and the tremendous costs if these programs fail, it is certainly essential that the structural reforms likely to be included in such programs be monitored very carefully.

Mr. Goos said that the topic before the Board related to previous discussions through the common theme of strengthening the growth orientation of Fund-supported programs. He remained fundamentally concerned that the current review of Fund policy should not encourage the Fund to move in a direction that would be inconsistent with the monitoring character of the Fund--which had been explicitly recognized by other speakers. The Fund had to serve its overriding mandate of assisting the viability of payments positions in the medium term without compromising the revolving character of its resources.

The promotion of sustainable growth could be essential for the lasting success of Fund arrangements, and might require the Fund to support structural reforms, Mr. Goos remarked. He was certainly not opposed to growth or structural reform, but explicit growth promotion and structural reform appeared to be appropriate only as instruments for the restoration of balance of payments viability and not as objectives in their own right. Bank-Fund cooperation also had an immediate bearing on the kind of structural reform measures that could be actively pursued by the Fund.

While there might be no a priori basis for general exclusion of a particular reform, he was not sure whether the staff should venture into all areas of structural adjustment, Mr. Goos commented. The different mandates and areas of expertise of the Fund and the World Bank had to be respected. While the overlap in the concerns of the two institutions had become more pronounced in recent years, that hardly justified actions that would blur the demarcation line even further. Rather, it appeared necessary to identify more clearly than was the case in the paper those structural reform measures that were suitable for Fund arrangements as opposed to measures that should be left to the World Bank. Effective cooperation also implied a clear division of labor; he therefore strongly recommended that the staff further address the subject in a more detailed and specified manner, so as to provide a clearer picture of potential conflicts that might arise with the World Bank.

With respect to technical assistance, the staff was obviously prepared to draw heavily on the expertise of the World Bank in areas other than fiscal, financial sector, and exchange system reform, Mr. Goos noted. That raised the question why that division of labor should not also be respected in regard to the design of structural adjustment measures in Fund-supported programs. The Fund should generally concentrate on reform measures that had a rather direct bearing on external adjustment and relatively short gestation periods. Such measures could be implemented early in the reform process--preferably as a prior action so as to enhance the credibility of the exercise, which was of the utmost importance. Reforms would have to be implemented together with an appropriate set of macroeconomic policies, and the latter would remain essential for domestic and external stabilization within the medium-term time horizon of the Fund.

Within the additional analysis suggested, the staff might also address the question whether the Fund should try restoring its prerogative in the area of monetary policy, Mr. Goos said. The World Bank had apparently expanded its activity recently--particularly the technical assistance and support of reform measures in financial and central banking systems.

He broadly agreed with the views explicitly or implicitly expresssed in the paper on the remaining topics for discussion, Mr. Goos remarked, including the staff's observations regarding the process of reform in Section 3 of the paper. However, he, like others, cautioned against the development of any complex indicator system in view of the presumably limited contributions such efforts could make to the identification and monitoring of structural aspects of adjustment.

As to the specificity and scope of structural reform, it appeared that important lessons could be drawn from the World Bank's experience in structural adjustment lending, Mr. Goos went on. He endorsed the views presented in the paper on the choice of the appropriate monitoring technique--and had already expressed a preference for quick-yielding, a priori measures--and the views on surveillance and the Fund's technical assistance. Increased emphasis on structural reform in Fund-supported programs needed to be matched by an increased receptiveness to such reforms by members.

The problem of hard choices between slow growth and structural adjustment mentioned on page 5 of the paper could not be resolved by making foreign financing a substitute for tackling the distortions arising, for example, from the institutional framework of a country or from vested interests, Mr. Goos noted. The receptiveness shown by members to structural adjustment would also determine the extent to which Guideline 4 might give rise to serious difficulties.

It could be expected that structural issues would gain increasing importance for the success of national economic policies, Mr. Goos concluded. Therefore, it appeared to be in their own best interest for borrowing countries to reconsider or structure their domestic, social, and political objectives with a view to securing the most efficient use of foreign financing. Since that point had been repeatedly stressed, those domestic, social, and political objectives could not necessarily be considered as sacrosanct, if a country wanted to rely on foreign financing; there had to be give and take. It would therefore be helpful if the Fund took greater initiative in pointing out to the authorities potential areas of policy inconsistencies.

Mr. Yamazaki made the following statement:

The increasing focus on structural reform is a salient feature of recent developments in Fund-supported adjustment programs. After several years of low or negative growth, an increasing number of countries have come to realize that improved prospects for growth are needed to maintain and strengthen their adjustment efforts. This consideration has guided the Fund toward structural policy measures, since structural reform has been considered an important link between adjustment and growth. For instance, the structural adjustment measures strengthening external sector performance no doubt have a salutary effect on the supply side of the economy through improved efficiency of resource allocation or through increased production capacity.

In the context of incorporating economic growth into adjustment programs, I endorse the extensive adoption of structural policy measures in Fund-supported programs. I do, however, attach particular importance to the monetary character of the Fund, and my comments regarding growth should not be taken as advocating any modification of the basic character of the Fund. Moreover, macroeconomic and statistical measures are mutually complementary.

The Fund's guidelines on conditionality--adopted in 1979, when the Fund focused mainly on macroeconomic adjustments--could facilitate the Fund's extensive involvement in structural reform, although I am--at this stage--open minded about revision of the guidelines.

Guideline 4--which refers to the need to pay due regard to domestic, social, and political objectives of members--should not be interpreted as a restriction on structural reform. Article V, Section 3(a) requires the Fund to establish adequate safeguards for the temporary use of Fund resources. As the guidelines must be interpreted in accordance with the Articles, the Fund should promote the structural reforms necessary for the attainment of external viability by a member country. Guideline 4 also refers to the causes of balance of payments problems as well as to domestic objectives, and the Fund should therefore take the initiative to convince authorities of the need for structural adjustment policy measures when structural impediments have negative effects on the external balance. In addition, I wish to stress the role of the Fund in promoting structural reform, in spite of the difficulties associated with the implementation of such reforms. Although effective structural reform measures would be accompanied by drastic changes in the institutional framework of the member country, the relaxation of adjustment efforts would impair the external viability of the member and the credibility of the Fund. The Fund's credibilty in promoting appropriate policy implementation has been directly related to the Fund's ability to catalyze resources.

As I stated in the discussion on December 16, the availability and effectiveness of policy instruments vary from one country to another according to the institutional framework of each economy. This underscores the need for a case-by-case approach in program design and the choice of monitoring techniques. Structural adjustments must be reflected in the choice of monitoring techniques, and effective monitoring techniques must be developed for structural reform. I therefore support Secretary Baker's proposal to incorporate structural reform measures in performance criteria.

The World Bank and the Fund can increase their collaboration in areas of mutual interest without encroaching on each other's domains. I note with interest Secretary Baker's proposal for strengthening Bank-Fund collaboration and I would particularly like to hear the staff's view on the effectiveness of this proposal, in the light of the heavy work load of the Executive Board and the staff.

The issues raised by the staff concerning the early identification of structural problems are important and need further reflection. As the staff has stated, the use of indicators is less developed in the structural policy area than in the macroeconomic policy sphere. This fact reflects the inherent difficulties in incorporating structural adjustment measures into indicators. Given these difficulties, the Fund should avoid the mechanical use of such indicators in both the structural and macroeconomic policy areas.

Mr. Abdallah made the following statement:

I welcome today's discussion on the extent to which structural reforms should be subject to conditionality and on the way in which these reforms should be monitored in Fund-supported programs, and would like to identify myself with the perceptive contributions made by Mr. Kafka, Mr. Ortiz, and Mr. Fernando. There is certainly a need for a thorough review of operational procedures as the Fund continues to shift further toward structural aspects of member countries' economies and away from the traditional macroeconomic sphere, whether in upper credit tranche stand-by arrangements, extended arrangements, or enhanced structural adjustment arrangements.

Conditionality attached to upper credit tranche purchases and extended arrangements should be different from structural adjustment arrangement conditionality. Likewise, monitoring of structural adjustment in the latter should be done through benchmarks confined to a few important variables monitored on a semiannual basis, so as to concentrate the mind of the authorities on those policies which can make a lasting contribution to the improvement of the external position and growth of their economies. In this connection, I note the assurance--in the Chairman's summing up of the Board's informal discussion on the enhanced structural adjustment facility of November 20, 1987--that under the new facility, performance criteria will be limited in number and will generally involve only a subset of benchmarks, and that prior actions will be required sparingly. Within the limits of the guidelines on conditionality, the scope of necessary reforms should be determined on a case-by-case basis.

Experience at this early stage of monitoring structural adjustment in Fund-supported programs does not appear to warrant any modifications to the existing guidelines on conditionality, which are reproduced in Appendix III to EBS/87/240. While the guidelines contain limitations to protect domestic social and political objectives--such as those in Guideline 4 and the restrictions on monitoring procedures in Guidelines 7, 9, and 10--considerable flexibility still remains, which should accommodate structural reform. More important, when the need to extend the guidelines on conditionality arises because of the increased spectrum of Fund operations, the World Bank guidelines on conditionality will have to be reviewed at the same time in order to avoid overlaps; if not, new conditionality for members might be imposed in areas already subject to World Bank conditionality. The staff has raised the question whether, given the contribution that many types of structural reforms can make to growth-oriented external adjustment, the Fund staff should take more initiative in emphasizing to authorities the implications of the policies that they have adopted. Within the limits of Guideline 4, the staff should work out various alternative scenarios based on different policy options and should spell out the implications of what is already being done. For example, the full implications of reforming the public enterprise sector through rehabilitation, privatization, or liquidation should be worked out, and the precise effects of these changes on credit creation, the fiscal position, the balance of payments, employment, and GDP growth analyzed. The authorities will then be in a position to take decisions in the light of all the possibilities open to them.

Different techniques may certainly be required--prior actions, performance criteria, and reviews--depending on the situation. However, structural reforms take time and, as is generally recognized, there are uncertainties involved which may call for flexibility or even a major recasting of a program which is already under way. While prior actions cannot be ruled out completely, they are not appropriate in most cases, and, as Guideline 7 implies, they should be applied only under exceptional circumstances. Midyear reviews are valuable in cases in which progress in structural reform cannot be fully quantified. Such reviews should serve as early indicators of whether the program is broadly on course, or whether further adjustments are needed. The G-24 report notes that structural adjustment cannot be monitored in precise terms in most cases. Performance criteria should therefore be used to indicate the direction of policy; quantitative performance criteria should not be set precisely, but rather as ranges.

Structural reform is indeed complex, and it is important--for the success of a program--to formulate an appropriate strategy. Many countries will require technical assistance for this purpose. Indeed, the authorities' structural adjustment programs should incorporate the technical assistance of the Fund and the World Bank. In this connection, present modalities for collaboration between the Fund and the Bank should be continued as opposed to the development of formal joint missions.

I see no objection to the growing practice of Fund-Bank collaboration, provided that the distinctive roles of the two institutions are respected. As the Fund's primary responsibility is in the sphere of members' balance of payments, and the World Bank's traditional responsibility is for projects and development programs, the Fund's present shift toward structural reforms for the achievement of external viability and growth and the Bank's move toward policy-based lending have clearly tended to create overlapping functions. Yet the new emphasis in Fund-supported programs on structural aspects and growth means that the structural adjustment programs that are being supported by the Fund stand to benefit considerably from the long-standing expertise of the World Bank in this field. Bank-Fund collaboration can therefore be very useful. Nonetheless, this collaboration should be conducted so as to ensure consistency and complementarity between the two institutions' programs. So far as Africa is concerned, close Fund/Bank collaboration is already a fact of life--clearly seen in programs for sub-Saharan Africa and under the structural adjustment facility. Practical cooperation must be continued without pushing the process to the point at which the law of diminishing returns begins to operate.

Under the new emphasis of the Fund and the World Bank on structural aspects of adjustment, the policy framework papers are becoming a focal point of interest. While I see merit in the policy framework paper's role of promoting aid coordination, they could be taken as a panacea for all developmental and structural problems facing a country, implying that the Fund would also be providing a stamp of approval for all financial assistance to low-income countries. While the Fund has an important role to play in assisting low-income countries--particularly with the enhanced structural adjustment facility--given its nature and expertise, the Fund should not become the center of development financing. It is unfortunate, therefore, that this linkage is leading to a growing tendency to make all development assistance to low-income countries policy based at the expense of long-term projects--even when the latter are viable.

Mr. Massé made the following statement:

Today's discussion is in some respects a natural counterpart to our recent discussion on the theoretical underpinnings of economic growth. The papers before us take the issue one step further by outlining the concrete measures which can be taken under Fund programs to raise countries' growth potential.

To a considerable extent, the staff papers describe the current state of structural adjustment supported by the Fund. Clearly, there has been an evolution in the use of structural adjustment measures in Fund programs. There are also practical problems in identifying the areas of structural reforms which are most urgently required, in designing the specific measures to be taken and the time frame in which they are to be taken, and in monitoring these measures. The combination of prior actions, performance criteria, and reviews will continue to be important elements for monitoring structural adjustment.

Two questions can be raised. First, has a clear link actually been established between structural adjustment and the fundamental role of the Fund--the achievement of balance of payments sustainability over the medium term? Second, if that link exists, what further steps can be taken to improve the design of Fund programs and the monitoring of structural adjustment measures so as to achieve the dual goals of balance of payments sustainability and the highest possible level of economic growth?

Increasing use of structural adjustment measures, focusing both on better resource allocation and more durable improvements in macroeconomic policy, can certainly contribute to balance of payments sustainability over the medium term. However, the relationship between structural change and a stronger balance of payments position remains a rather tenuous one, particularly in those areas not directly affecting the external accounts. Structural reforms in trade and tariff policy or the exchange rate can clearly have a direct impact on the balance of payments position. Priority should be given to changes in these areas in Fund-supported programs because they might have an immediate positive effect on the allocation of scarce foreign exchange resources, might increase incentives to export, and might therefore lead to rapid improvements in the current account.

It could also be argued that as the balance of payments position reflects the underlying relationship between savings and investment within an economy, efforts which concentrate first and foremost on increasing domestic savings and the efficiency of investment will have a more durable impact on the medium-term balance of payments position and growth. Some have argued that the economies of East Asia--particularly Korea and Japan--have achieved both high rates of growth and balance of payments sustainability over long periods not because of efforts to liberalize prices or privatize the ownership of capital, but precisely because they encourage the accumulation of domestic savings. The setting of priorities is therefore a critical issue, but it is not fully discussed in the staff paper. I agree with the staff that measures have to be tailored to each individual country's circumstances, but I would be interested in further work by the staff on how we can set priorities, and whether particular measures are especially more important at a certain phase of balance of payments adjustment and economic development.

On the second question, I accept fully the staff's point that a bold start to the reform process may be critically important, and that prior actions can remain an important method of ensuring that programs get off on the right footing. The continuous monitoring of reform is a more difficult issue, however, and we have only begun to understand the best method of monitoring progress. I would be interested in further staff work on intermediate indicators which could show the step-by-step progress being made. Multiyear arrangements with annual reviews may well be a more suitable vehicle for monitoring progress than annual programs, and multiyear arrangements have already been implemented--in essence--under the structural adjustment facility. However, I would be interested in staff thinking on ways in which to develop more concrete benchmarks, both for Fund monitoring and to give the authorities explicit goals in their policy reform process.

With respect to Guideline 4, the Fund must pay due regard to the social and political objectives of members. At the same time, each member's decision to join the Fund requires the relinquishing of some sovereignty. It is a question of fine judgment whether the Fund is intruding excessively upon sovereignty by recommending structural adjustment policies which limit countries' medium-term growth potential. The staff could take greater initiative in focusing on structural inadequacies not only under Fund-supported programs, but on a more regular basis during Article IV discussions.

The staff could emphasize barriers to growth and the implications for poverty alleviation and income distribution, as sustainable adjustment policies can be successful only if there is broad-based popular support for them. In many cases, countries have been unable to sustain adjustment measures in the absence of a broad base of support for adjustment, and it is in the interest of developing such a base that I would encourage the staff to emphasize implications of various policy choices.

Finally, the Fund and the World Bank have clearly begun to collaborate more fully and more effectively on adjustment measures. In many cases, the issues of balance of payments adjustment and economic development have become tightly interlinked. Provided that each institution keeps in sight its fundamental mandate--medium-term balance of payments sustainability for the Fund, and long-term economic development for the Bank--I can see no difficulty in closer coordination of Fund and Bank staffs in promoting structural adjustment, even if this implies an overlapping of monitoring and benchmarks.

Mr. Finaish made the following statement:

I welcome the increased recognition over the past two years of the important role that structural reform can play in fostering improved and durable growth performance, recognition essential for the realization of balance of payments viability over the medium term, while maintaining acceptable improvements in the standard of living. The problem of adjustment fatigue has been, and continues to be, an important issue that needs to be addressed. In this regard, it should be recognized that unless output growth is accompanied by an acceptable level of absorption, it will be difficult to maintain public acceptance of adjustment measures.

The precision with which the diagnosis and assessment of distortions in the structure of economic incentives that underlies structural problems may be carried out is rather limited, due to the difficulties involved in developing reliable structural indicators of the magnitude of structural distortions. The staff correctly points out that the link between these indicators and policies is typically uncertain and operates with considerable lags. In addition, data necessary for most suitable indicators are either unavailable or costly to collect. Therefore, while I agree that in some cases it might be feasible to supplement detailed institutional knowledge with the monitoring of "carefully selected indicators," I, like the staff, wish to emphasize that a mechanical use of indicators should be avoided and that their use should be evaluated on a case-by-case basis to ensure that the time and cost associated with the setting up of these indicators are justified by their potential benefits. It should be emphasized, however, that it is important to approach the identification of structural problems and the scope of needed reforms in an objective manner, based on an in-depth knowledge of the economy.

Detailed planning and proper sequencing of structural adjustment policy measures are important, but, as the staff points out, such planning and sequencing may not be feasible in all cases, in view of the complexity of structural reform programs, and because those reforms often cover a period of several years. The administrative capacity of a member to design and implement complex programs of structural reform has to be an important factor in determining the extent of the structural adjustment that can be incorporated in an adjustment program, and, therefore, emphasis should be limited to key structural areas only. The member's sociopolitical capacity is at least as important a consideration as any other in this regard; nor should a decision on the scope or pace of adjustment be made without simultaneously considering the all-important issue of the availability of adequate external financing.

I welcome the staff's position on the need, in some instances, for gradual implementation of structural reforms in order to mitigate the associated transitional costs in terms of output and employment, and on the need for flexibility in cases involving unanticipated problems with implementation. I note, and appreciate, the staff's concern about the need to balance the requirements of flexibility and uniformity of treatment among members. These requirements, of course, need not compete, as uniformity of treatment will be satisfied so long as Fund decisions are based on a careful and fair assessment of individual country circumstances, and as long as members whose circumstances are similar are treated similarly.

On another point relating to the pace of adjustment, the staff notes that "a bold initial move can also help to ensure that a reform program is carried through by ensuring that significant beneficial effects, which can muster support for the reform are experienced relatively quickly." While this statement is somewhat qualified, and can in some cases be valid, "rapid and sizable initial steps" could also lead to more immediate short-run adjustment costs. If these costs are such that they might lead to an interruption in the adjustment effort, the credibility and acceptance of the structural reform policies may be jeopardized.

The choice of monitoring techniques should be guided by the considerations that structural reforms generally require a long time to affect target variables, and that there is uncertainty with respect to the appropriate timing and magnitude as well as to the ultimate impact of these reforms. Therefore, monitoring of structural adjustment policies should focus on a few areas with the aim of assessing progress toward achieving program objectives.

The evaluation of economic performance in the context of program reviews should also be done in a flexible manner, so that undue delays do not occur in the completion of these reviews. Prior actions should be envisaged only if they are deemed necessary to enhance the credibility of the program and when the imbalances to be corrected are very large and require a wide range of measures. In some cases, the insistence that certain measures be implemented prior to the arrangement with the Fund can lead to costly delays in the whole adjustment effort. In addition, in those cases in which prior actions are deemed necessary, the actions should be specified flexibly, so long as they represent movement in the desired direction. Mainly because of the inherent difficulty in quantifying structural policy measures--and the consequent need for a broad and qualitative evaluation of performance--it will probably not be feasible to broaden the scope of structural policies that can be monitored through performance criteria.

As structural adjustment typically stretches over a number of years, structural reforms are more appropriately tackled in the context of extended arrangements than in that of arrangements of relatively short duration--especially in cases involving far-reaching changes in the institutional structure of an economy.

Given the nature of the problems that structural adjustment policies are intended to address, the overlap between the Fund and the World Bank has become rather pronounced, especially in view of the increased emphasis on structural reforms for the achievement of external viability, and the World Bank's increased involvement in policy-based lending. One could therefore see the importance of increased cooperation between the two institutions for ensuring consistency in the content and timing of recommended policies, but at the same time it is essential, as noted by other speakers, that cross conditionality be avoided.

Structural reform almost inevitably bears on the domestic, social, and political objectives of members, as the staff recognized. In view of the Fund's increased involvement with structural reform, the Fund should ensure that due regard will be paid to these objectives in the choice of adjustment measures.

Mr. Posthumus made the following statement:

Today's discussion is a natural extension of the recent discussion of growth exercises. The objectives of structural reform are either to enhance the efficiency of resource allocation, or to add to the effectiveness of macroeconomic adjustment, or, in most cases, both. Because structural factors in the economy are often felt to be a constraint on growth, structural adjustment is essential for the promotion of growth-oriented adjustment. Structural measures are often seen as identical to liberalizing, deregulating, or market-oriented measures. This is often but not always true: well-devised government programs exist in many countries and can do a job which markets often can not. Given the emphasis on growth, it is indeed highly relevant to discuss the monitoring of structural adjustment in Fund-supported adjustment programs as well as in the framework of Article IV consultations. That expanded monitoring might lead to actions prior to balance of payments problems, rather than prior to financing.

The problem of adjustment--defined as the difficulty of sustaining adjustment policies when growth performance is weak--has led to greater emphasis on the need for heavily indebted countries to grow out of their debt problems. The adjustment fatigue problem is not confined to heavily indebted countries, as all countries constantly have to adjust in some way because the world is constantly changing. Adjustment fatigue arises basically from a series of continued attempts to adjust without sufficient success--attempts which are constantly perceived as painful. Slow adjustment, however, also means slow results. Growth helps because it allows reallocations of resources and changes in the distribution of income without--or with reduced--deterioration in the positions of some sectors. However, growth cannot be the cure for adjustment fatigue if the causes of the latter are not removed, if only because adjustment is necessary to achieve lasting growth.

Behind these issues of adjustment fatigue and the need for growth there may be an implicit, unresolved, debate. The emphasis on growth orientation of adjustment programs seems to have something to do with the feeling that too much short-term external adjustment adversely affects living standards and growth possibilities, and that more gradualism is necessary. Longer adjustment periods also stem from the longer gestation periods of structural measures; hence the urgency and the current move to provide more long-term--and low-cost--financing to low-income countries. However, the Fund needs to continue to work toward external payments viability, and growth is best promoted by--and is even dependent upon--sufficiently bold adjustment to that end. Growth-oriented adjustment means adjustment plus structural measures, but this does not necessarily mean that every program requires structural policy conditionality. Thus, while growth-oriented adjustment can imply less political risk in the framework of Fund programs, it can require more--and politically sensitive--structural adjustment measures. This problem is not restricted to developing countries with Fund-supported programs.

In this connection, I note the staff paper's emphasis on the importance of timely diagnosis, and on rapid and sizable adjustment steps, together with the careful thought that must be given to the optimal sequence in which structural reforms in different areas should be implemented and the need to coordinate these reforms with demand-management policies. This is clearly a task that must be undertaken in the framework of Fund-supported programs, and--much more important--concerns all member countries in the framework of Article IV discussions.

The monitoring of structural adjustment in Fund-supported programs should reflect all these considerations, which implies that we should move very cautiously. Introducing monitoring when there is uncertainty about the value of the measures monitored naturally leads to problems, and the staff analysis is in this respect very helpful. A primary function of monitoring is to facilitate effective policy implementation by providing information about how adjustment is proceeding. In addition, monitoring gives the member clearer assurances of the circumstances under which purchases can be made from the Fund. Of course, monitoring also allows the Fund to help to ensure that purchases are made only when the program is on track.

Finally, the staff rightly stresses that the Fund and the World Bank have different mandates, different functions, and different areas of expertise. Yet the areas of common concern have naturally become broader, with increased emphasis on the need for structural reform as a key to the achievement of external viability. The policy framework papers produced in the context of the structural adjustment facility are a prominent example of the resulting increased collaboration between the two institutions, and I strongly welcome this trend; collaboration may help each institution to continue to focus primarily on its traditional role, because the other's expertise need not be duplicated. I attach great importance to preserving the traditional focus of the two institutions, because each does have its own role to play. Preserving the character of both institutions while meeting the new financial and economic challenges is indeed a challenge. Perhaps difficult questions about the interrelationship between the conditionality associated with programs sponsored by the institutions could then be avoided.

Mr. Salehkhou made the following statement:

The staff is justified in emphasizing that the papers should not be considered in isolation from other papers, like those considered recently on the design of growth exercises. I am, however, concerned by the striking differences in the approaches adopted by the two sets of papers. While the papers on growth exercises--prepared by the Research Department--raised theoretical issues and stimulated interesting discussions, the papers before us, prepared by the Exchange and Trade Relations Department, are much more operations oriented. Since we have not yet arrived at any decision on the growth exercise content of our programs, and given the linkage rightly established by the staff in this regard, we should refrain from taking any decision to change our policies related to structural adjustment at this time.

The ambiguous way in which the papers are written and the substantial details that they provide make me wary of the conclusions that could be drawn by the staff from this Board discussion. I would, therefore, strongly emphasize the preliminary character of today's dicussion, and insist on having any change in our operations based on a formal decision on changing the guidelines on conditionality--a decision which should be duly approved by the Executive Board, rather than merely reflecting the first reactions expressed by two or three Executive Directors.

The subject matter at hand is very sensitive to member countries and, as the staff also recognized, it extends beyond economic problems into social, political, ideological, and even institutional problems as well. These issues cannot be easily translated into a mathematical equation, and they raise fundamental questions for member countries.

Member countries are not against structural adjustment; far from it. In fact, three members of my constituency have been undertaking fundamental reforms with the support of the Fund and the World Bank. But they did so in great part without having to deal with monitoring devices such as those now suggested by the staff. The imposition of such devices--be they called performance criteria, benchmarks, intermediate indicators or by any other disguising labels--could prove counterproductive, as they would not facilitate the formulation of a consensus on such major reforms in the member countries concerned. I, therefore, wish to oppose the introduction or expansion of any such devices. The timing of such reforms is also essential. Imposing deadlines on sovereign governments or parliaments would jeopardize the necessary consensus and the orderly adjustment process in the most sensitive areas of the economy.

Another issue is the definition of these areas of structural reforms. Some of the measures identified as structural by the World Bank are not so considered by the Fund and vice versa. Similarly, the ideological content of the Fund and World Bank approaches--aiming at liberal and open market economies--can be challenged in some member countries that have been managing their economies in different ways, sometimes successfully. I would therefore request that the staff define precisely, on some future occasion, the areas that it considers of a structural nature. I also suggest that future papers should address the external as well as domestic effects of the recommended policies on the member countries. I was struck by the lack of any reference to the effects of industrial countries' policies on the developing members undertaking structural reforms. Should the latter proceed with the recommended trade and exchange liberalization policies--considered implicitly by the staff as a panacea--even in the absence of any symmetrical adjustment of the protectionist policies in the industrial countries? In other words, should the Fund impose the observance of performance criteria concerning trade liberalization and consequently deny a purchase if a country decides not to liberalize as programmed in retaliation against restrictive measures taken by its trading partners? This question suggests the type of situation that may develop if we proceed with the suggested changes.

Similarly, on the domestic side, structural reforms have a social and political impact. If we ask for a program and precise timing of these reforms, we will have to share these consequences. I would urge the staff to look more carefully into these issues before making any final recommendations.

Other consequences of structural measures are their short-term side effects, since these reforms generally bear fruit in the medium term. The Fund and the World Bank should carefully take this into account in the design of adjustment programs. It is regrettable that the competition between the two institutions--and I purposely use the word competition--often now leads to demands on the adjusting country for the simultaneous production of short-term and medium-term effects. Failing that--due generally to conditions largely beyond the control of the authorities--the member country is asked to come up with additional measures, even if those measures are not consistent with the medium-term framework, and even if there is no additional financing.

Technical assistance--a most valuable part of Fund activity--should not be used as an active tool on conditionality, as the staff suggested. Such an abuse would discourage member countries from seeking Fund advice at an early stage of their problems. I attach great importance to structural reforms in the framework of Fund-supported programs, but the mechanistic approach adopted by the staff is not consistent with the cooperative character of the institution. It raises serious questions related to the faithful observance of the Articles and of the guidelines on conditionality. Cognizant of the need for such reforms, members want the Fund to pay due attention to their institutions as well as to their social and political fabrics. They are willing to discuss their problems with the Fund if due consideration is given to their sovereignty. Trying to establish monitoring techniques for structural adjustment goes far beyond the expectations held by these countries concerning the Fund at the time that they joined the institution.

Mr. Rye made the following statement:

The question of structural adjustment and its monitoring raises a number of important and complex issues, as the dicussion today has clearly demonstrated.

I have had some uneasiness as the Fund has become more and more involved in questions of structural adjustment. Of course, this trend is to some extent inevitable, given that the balance of payments problems of many members reflect deep-seated structural weaknesses which have to be tackled if the objectives of Fund support are to be achieved.

It does, however, seem that increasing Fund involvement in structural issues raises difficult problems, not least for the Fund's relations with members' authorities and with other institutions--particularly, of course, the World Bank. Structural adjustment frequently involves tackling powerful interest groups in the member country, and this may have contributed to the widespread misrepresentation of the Fund and its role today; and structural adjustment does lead us into that grey area where the roles of the Fund and Bank, as they have been extending in recent years, overlap, creating a danger of confusion and duplication. I agree with Mr. Ortiz that the staff paper is oversanguine in its assessment of Fund-Bank cooperation.

Fund involvement in structural reform raises quite sharply the dilemma of case-by-case flexibility versus consistency and equality of treatment of member countries. A minor criticism of the staff paper might be that it skates over this question rather too lightly. Obviously, institutions and institutional structures differ widely from country to country, and although there are certainly areas--such as taxation and pricing policies--in which structural weaknesses are common, country-to-country differences dictate that each case must be treated on its merits. But flexibility can be seen as unfairness, and it can be difficult to demonstrate consistency on the part of the Fund when some countries are required to undertake comprehensive programs of structural reform and others are not.

In the light of these considerations, I very much agree with those who have stressed the necessity of full commitment by the authorities concerned if structural reform is to be successful.

The focus of Fund involvement in structural reform should be on areas in which adjustment would clearly make macroeconomic policies more effective. While the distinction is not always clear cut, structural reform directed at long-term development is in contrast primarily the reponisibility of the World Bank and other development institutions. Therefore, the areas in which the Fund should be intimately involved would include, for instance, reforming taxation systems so that fiscal policy can become a more flexible tool of economic management, and freeing up financial systems so that interest rates and market intervention can be made effective tools of monetary policy.

Structural reforms in Fund-supported programs should be limited to those areas in which such reforms are clearly necessary for the achievement of balance of payments viability over the medium term. This implies that Fund involvement in structural reform should have its limits. In few cases will it be appropriate for the Fund to take the lead in devising wholesale or comprehensive reform strategies.

In any event, there are practical reaons for a limited approach to structural adjustment. As the staff paper notes, the "administrative capacity of a member to design and implement complex programs of structural reform has to be an important factor in determining the scope of structural adjustment." Given the central importance of planning for effective structural adjustment, the constraints on administrative capacity evident in many countries must put sharp limits on the extent to which structural adjustment can be planned and successfully implemented. Such capacity is more likely to be in short supply where structural defects are most abundant--otherwise, presumably, those defects would have been identified and tackled earlier.

I have only a few points to make on monitoring per se. First, structural weaknesses become more difficult to eliminate the longer they are entrenched, and we should take the opportunity of Article IV consultations for early monitoring and consideration in detail of emerging structural difficulties--within the areas of Fund competence. And we should not be stinting in responding to member countries' calls for technical assistance for structural reform.

Second, prior action is in many cases essential for effective adjustment. In this regard, I very much agree with the staff paper, which points out that "rapid and sizable initial steps can enhance the credibility of an adjustment effort, limit uncertainty, and establish appropriate price signals...[whereas] in contrast a small first step may arouse equally substantial opposition, but fail to induce sufficient positive effects to rally political support." There has been abundant evidence in recent Fund programs of the truth of these propositions.

Of course, there has to be recognition of the constraints on prior action, including the time needed for planning and the limitations on administrative capacity. So in many cases in which prior actions might otherwise have been seen as highly desirable, we may have to accept that the best that can be done is to reach prior agreement with the authorities on a program and broad timetable for reform.

Third, I have some sympathy with those who have expressed concern about the overuse of performance criteria in structural areas. Many structural reforms do not readily lend themselves to quantification, and legislative and other timetables are not always under government control. It is indeed essential to monitor structural adjustment as well as macroeconomic policies effectively, but a review will often be an appropriate mechanism.

I am inclined to agree with speakers who have argued that the guidelines on conditionality are in need of comprehensive reconsideration. Some of the guidelines--Guidelines 2 and 9, for instance--seem out of date.

Mr. Zecchini made the following statement:

This discussion is the first complement to the recent Board discussion on ways and means to couple growth with adjustment. In contrast with the rather abstract and theoretical approach adopted in the earlier discussion, today's discussion goes into the design of specific policy measures, among which structural policies have a crucial role to play. These policies can contribute significantly to the expansion of output via different channels of operation, even in the context of a program aimed at achieving a sustainable balance of payments position. Of course, these measures are not a substitute for cautious demand-management policies requiring an appropriate use of macroeconomic instruments.

The difficulties in estimating econometrically the impact of total factor productivity on potential output growth cannot obscure the widely accepted truth that enhancing the efficiency of resource allocation, improving the quality of the factors of production, and improving the circumstances in which production and investment decisions take place are all factors determining growth.

Structural policies can also significantly raise the rate of return or the profitability rate on investment, thereby improving the conditions under which a country is justified in borrowing abroad on purely economic grounds. By raising the productivity of capital above the real cost of external resources, a country might be able to raise more external financing to support a viable balance of payments position. These are two of several arguments which should induce the Fund to consider the structural dimension of external adjustment in a deeper and more forceful way in all programs, without discriminating between one-year stand-by and the longer-term extended or structural adjustment arrangements.

As in the choice of the model to be used to support adjustment and growth, the design and monitoring of structural adjustment measures do not lend themselves to easy and clear-cut solutions that are valid irrespective of the country under consideration. Experimentation with alternative solutions is necessary before we finalize our procedures, and in this area we can benefit from the experience of the World Bank without having to repeat its mistakes.

In the design of the Fund's approach to structural adjustment, it is essential that the Fund identify the structural problems at a very early stage by using Article IV consultations or discussions of possible arrangements with the Fund. Early clarification requires the collection of extensive information on the institutional setting of the economy, while the use of structural indicators, although valuable under some circumstances, is not a necessary prerequisite.

The definition of the policy approach to structural reform cannot disregard the social and political objectives of the country concerned, nor its economic priorities--as the guidelines on conditionality state. But even under this binding condition there is ample room for enforcing structural reforms which affect the system of economic incentives and particularly the pricing and savings areas. The move toward increased reliance on market forces is not and should not be a doctrinaire prescription for all countries or for all economic sectors in a given country: prescriptions have to match the sociopolitical reality of the country. If there is extensive government intervention in the economy, then the aim of the adjustment program must be to make intervention consistent with the objective of increasing the efficiency of resource allocation. Thus, I strongly endorse measures to establish rules for intervention, restricting the room for discretion. The recent unsatisfactory experience of several countries, like Yugoslavia--a consequence among other things of limited compliance with the chosen rules--indicates the need for the Fund to follow a stricter approach in this area.

The design of reforms has to be tailored to the characteristics of the country, and particularly to its capacity to manage the implementation and the implications of the planned reforms. In this respect, the success of any reform depends crucially on full backing of the planned changes from the authorities and the political majority of the country. It is up to the country to decide the most appropriate speed of implementation of structural change after considering the extent of the constraint stemming from the availability of external financing. Nonetheless, experience has shown that the impetus to reform fades away a limited time after the introduction of a program of reforms, as vested or affected interests muster increasing forces to delay or even prevent changes. The general chances for success are better if the initial reforms are sizable and rapid.

As to monitoring, it is important to dispel countries' usual impression--that monitoring equals policing. As the staff points out, monitoring should aim to provide the country concerned with information about and an assessment of progress and durability in correcting imbalances and in creating better conditions for growth. Monitoring has to highlight at an early stage the implications of the current course of policies for balanced growth.

With regard to the instruments for monitoring, an appropriate mix of prior actions, performance criteria, and reviews should be sought. In some areas like exchange and trade systems, performance criteria might be advisable. However, in areas in which the monitoring of reforms involves numerous institutional dimensions, it is more appropriate to focus on intermediate indicators in evaluating the strength of the policy action.

Although structural reforms often involve long periods--both in implementation and in the manifestation of results--they need not necessarily be confined only to multiyear arrangements with the Fund. There is scope for important reforms even in a one-year program, although their range is limited. When reforms have to cover several areas of the economy, it is advisable to phase the different segments of the reforms over a few years, seeking to increase the synergy between the effects of the various segments. The question of whether each adjustment program requires structural reform can be answered only by analyzing the causes of the external and internal imbalances: if the causes are traced back to structural, deep-seated weaknesses, the program has to include a component of structural reform.

On Fund-Bank collaboration, cooperation between the staffs of the Fund and the World Bank is important, both in the design and monitoring of the measures. New ways of making this cooperation more workable and effective have to be devised.

In general, the present guidelines on conditionality are flexible enough to incorporate most of the requirements for monitoring structural adjustment. However, Guideline 9--which refers to the contents of performance criteria--might require some reformulation in order to extend its range to include structural measures.

Mr. Jiang made the following statement:

Authorities in the developing countries were compelled to adopt major reform measures to restore growth after adverse developments in the international economy in the early 1980s. The debt crisis which ensued showed clearly that these problems were mostly structural in nature and that long-term comprehensive structural adjustment was often needed. Of course, structural adjustment that supports long-term growth is needed not only by the developing countries, but also by the industrial ones. As we are discussing the monitoring of structural adjustment in Fund-supported adjustment programs, I shall touch only on this particular part of the problem.

Under the present circumstances, it is fairly accurate to say that the Fund is facing new challenges to develop new ideas and innovative instruments to address the present problems. We are accustomed to dealing with short-term balance of payments needs and are now confronted with the more difficult structural adjustments which will take more time and energy to solve. Unfortunately, we have less experience in this area.

On December 16, the Board explored the issues of the Fund's program design. Today's discussion of implementation of structural adjustment programs may be deemed a continuation of that discussion. In view of our comparative lack of experience with structural adjustment, both of these discussions should be seen as preliminary, and more solid conclusions will have to be drawn from later experience.

I agree with the staff that structural adjustment is very difficult, as it often goes to the heart of a country's institutional framework, and it takes rather a long time to achieve some success. Taking this into consideration, I wonder whether it is still appropriate to emphasize the achievement of balance of payments viability over the medium term within the framework of a Fund-supported structural adjustment program, as this will inevitably lead to the adoption of some premature, quick-success measures. In some cases, the end result may turn out to be contrary to the original objective.

In general, an adjustment effort which demands initial rapid and sizable steps will not be a suitable model for all countries. In some, more complex cases a breathing spell or a stabilizing period may be needed before any gigantic or bold adjustment program can be undertaken. There is no "quick fix" structural adjustment. There is a broad consensus in the Board concerning the revitalization of the extended Fund facility, although that facility only partly covers structural adjustment. Early inclusion of this problem on the Board's agenda is advisable.

The staff rightly notes that the diagnosis of structural problems and the tracking of measures to deal with them must remain the responsibility primarily of member governments. The Fund's contribution should be advice and suggestions, primarily followed by support through its resources. We should note the World Bank's experience in this area, to avoid suggesting reform packages that are too complex and ambitious. In addition, we must take into account the political and social circumstances of any given country. In most cases, a gradual implementation of the adjustment measures may be necessary, especially as the major institutional changes may span several years.

The Fund's technical assistance can play a significant role in the process of structural reform, but it should not be limited to that area alone. Fund expertise can help to identify structural problems at an early stage, and the early provision of technical assistance may increase the possibility that the Fund's policy recommendations will be accepted by the authorities concerned. The Fund's monitoring function will always be more effective if conducted in a friendly and advisory manner.

Mr. Fogelholm made the following statement:

Before commenting on the topics for discussion proposed by the staff, I would like to make some general points.

I am, by and large, satisfied with the conditionality content and monitoring features of present Fund-supported adjustment programs. I agree with the increased emphasis being placed on structural matters, as the problems of many countries today are more of a structural than of a demand-management nature. That does not, of course, mean that Fund-supported programs should always contain structural measures. Furthermore, the Fund should continue its present policy of "hurrying slowly" into the field of structural adjustment in order to facilitate the gathering of experience, thereby avoiding major mistakes in the process. The introduction of structural policy measures in Fund-supported programs should be predominantly related to the Fund's main task of assisting member countries to achieve a sustainable balance of payments in the medium term. Changes in the foreign exchange system and liberalization of trade are examples of such measures.

The proposed undertakings should, preferably, be as precise and as objective as possible and should be concentrated on arrangements and provisions under the direct control of the borrowing country. In the design of adjustment programs, the Fund should also be careful not to put forward requirements that could be regarded as interference in the internal affairs of member countries. I am, therefore, against structural policies which go beyond purely economic considerations; for instance, privatization for the sake of privatization.

Traditional Fund-supported programs are relatively short in duration, and certain structural adjustment measures take time to implement, produce results only after a long time lag, and generate effects that are difficult to quantify. This is particularly so in arrangements which involve or contain more comprehensive institutional changes. In such circumstances in particular, it would not be advisable to propose structural criteria as requirements for disbursements. In this context, the Nordic countries consider it important that the staff, in its negotiations with member countries, present its assessment of the implications of the various policies to be pursued, including the consequences of structural measures to be undertaken.

As to the more specific points, the language used in the guidelines on conditionality is flexible enough to accommodate the implementation of an increased number of structural adjustment policies in Fund programs. I could, however, go along with a change in the guidelines that would imply making an explicit reference to structural policy measures, if that were thought to be desirable by others.

I generally agree with the principles underlying the staff's opinions on the choice of monitoring techniques and policy actions. And I share the staff's view that intermediate indicators are rarely suitable as performance criteria, but could, in some instances, be used for monitoring purposes. Altogether, one should be careful about using performance criteria in relation to reforms involving substantial institutional changes. Prior actions and reviews would, in such cases, be more feasible and advisable.

The Fund should continue to provide member countries with technical assistance within the framework of existing economic resources. I agree with Mr. Hubloue that technical assistance should, whenever feasible, be connected to and used in monitoring structural reforms. I also look forward to the coming review of technical assistance in the Fund.

Fund involvement in structural reform might, indeed, raise questions about the division of responsibilities between the Fund and the World Bank. Even without an explicit need for an immediate increase in, or a formalization of, Fund-Bank cooperation, every effort should be made to avoid duplication of work and to coordinate policy actions and the monitoring of structural reforms. In addition, both organizations should draw fully on the experience and expertise available in the sister organization, and should divide their work accordingly.

The Fund should carefully follow both economic and institutional developments in member countries so as to be able to anticipate possible problems at an early stage, and to encourage members to undertake corrective measures so as to support growth within adjustment programs.

Mrs. Ploix made the following statement:

A major conclusion of our discussion on growth exercises in the context of the Fund was that sustainable growth can best be promoted through actions designed to enhance the total factor productivity of an economy. For the most part, such actions are of a structural nature, as they are intended to offset the functioning of the economy. The central objective of structural adjustment is not only to improve the overall efficiency of a given economy, but also to increase its resilience in the face of external shocks and its responsiveness to policy measures. Thus, the main areas of action should be the exchange and trade regimes, and the financial and fiscal systems.

The first two areas are already fairly well covered in Fund-supported programs, as was stressed in the staff paper. For the other two, additional efforts seem needed, and well-directed technical assistance could play a more important role in these areas. An initial benefit would be to fill the "information gap" which the staff views as a major impediment to structural monitoring. A second aspect that should be kept in mind is the time requirement of structural adjustment. Technical assistance could prove helpful in laying the groundwork before a program is put into place, and could facilitate aid once the program is completed. The Fund should not confine its technical assistance to the economic and financial aspects of reforms, but could help by providing legal or regulatory advice when institutional changes are envisaged.

With respect to monitoring techniques, a few basic rules should be remembered, and prior actions should be preferred, with a view to avoiding a proliferation of performance criteria. Criteria pertaining to structural adjustment measures could be formulated in terms of target ranges, so as to introduce more flexibility than is the case in the monitoring of macroeconomic variables.

An essential factor in keeping up the momentum of a structural program is the precise sequencing of its various interrelated components. In that sense, the phasing of structural reforms should adequately reflect the specific conditions of each member country.

The main difficulty in the monitoring of a structural adjustment program by the Fund stems from the time frame: the normal time horizon for a structural adjustment program is the medium term, whereas the financing constraints faced by most countries are short term.

By paying due consideration to the medium-term perspective, the staff is led to take account of some proposals already put forward by the Group of Twenty-Four, the French authorities, and Secretary Baker. Such proposals include the introduction of prior actions, of performance criteria to be examined during annual reviews, and of intermediate benchmarks whose monitoring could be more frequent.

The best way to overcome the contradiction between short-term and medium-term considerations, and to develop the most adequate conditionality, would be to remember that structural adjustment--aimed at strengthening the supply side--is a supplement to short-term adjustments to the level of domestic demand which result from the need to take account of the immediate financial constraints. As a general rule, medium-term conditionality must therefore complement and not substitute for, regular short-term conditionality. A reactivation of the extended Fund facility should not weaken the adjustment effort provided by a sequence of stand-by arrangements.

Increased Fund involvement in structural matters is likely to result in somewhat more difficult coordination between the Fund and the World Bank. When difficulties arise that lead to significant delays in the formulation of structural programs, the Board should be kept informed. Executive Directors would then find themselves better able to appreciate the context and the main features of a program that they will subsequently be asked to approve.

If technical assistance is to play a larger role, its operation will have to be more consistent with the basic work of the Fund. In particular, systematic references should be made to the results of assistance. Those references could occur in the context of structural adjustment programs, in program reviews, and in Article IV consultations. An improved reporting system on the activities of the Central Banking and Fiscal Affairs Departments would also be desirable, and could consist of a more substantive annual review.

Mr. Dallara made the following statement:

We welcome this occasion to focus on practical ways in which the Fund can more fully integrate structural adjustment, and therefore a greater growth orientation, into Fund-supported programs. As Directors are aware, my authorities have attached particular importance to this objective. During the Annual Meetings, Secretary Baker put forward a specific proposal, suggesting that for some longer term programs there be a shift in the frequency of certain performance criteria from three to six months and, at the same time, greater specificity and greater use of certain structural performance criteria. Many Directors have in fact commented on and some were supportive of this proposal this morning and I would hope that it could be kept in mind in the further work that we do. I would have preferred some specific consideration of it in the staff paper, but I recognize that the issues and the concepts are included there.

In any case, we have expounded at some length in the past on many specific suggestions as to how structural reform measures could be incorporated into Fund programs. For that reason I will try to be brief.

The staff paper makes two interesting distinctions concerning the nature and objectives of structural reform. The reforms are distinguished in nature between those designed to create a system of appropriate price incentives, and those of a more institutional or regulatory nature. The objectives of the reforms can be distinguished between those aimed at strengthening the durability and effectiveness of macroeconomic policies, and those aimed at improving the allocation of resources and the growth of productive capacity. Put in the context of our discussion on December 16, the objective of strengthening the durability and effectiveness of macroeconomic policies is one that can enhance and improve the overall environment for both increasing factor inputs and increasing factor productivity, while those policies aimed at improving the allocation of resources focus more on improving factor productivity. It seems critical that we keep each of these objectives in mind as we design our programs.

The experience of the last few years suggests the importance of proper complementary design of macroeconomic and structural policies. One can think of numerous examples. For example, in the consideration of the recent Argentine case, it was rather clear that the need for structural reforms in the tax and parastatal areas was critical to durable fiscal adjustment. In a number of Latin American countries a strengthening of the financial structure seems clearly needed to ensure that the effectiveness of monetary policy is not undercut by periodic difficulties with, and in some cases, bailouts of, troubled financial institutions. In Yugoslavia, we have an example of exchange rate adjustments that are not very effective, owing to impediments to the operation of a national foreign exchange market. These are examples, and there are many others, of needed structural reforms to strengthen the effectiveness of what we generally perceive as macropolicies.

On a number of specific issues and suggestions put forward in the staff paper, first, we would join other Directors in supporting the development, on an experimental basis, of structural adjustment indicators in Article IV consultations.

Regarding program design, we would emphasize the importance of focusing early on a system of relative prices. This should include the full range of relative prices, including the exchange rate and interest rates. It is important, of course, that relative price changes be accompanied by institutional and regulatory reform.

An important and very difficult issue with which we must grapple is the appropriate specificity of structural reform targets in our review clauses and as performance criteria. We accept the fact that data limitations, analytical problems, and issues relating to the sensitivity of some of these policy areas may make it difficult to be as quantitative or specific as we would like. Nevertheless, we should strive for increasing specificity in structural reform commitments and objectives, even though these may later require some adaptation in the context of reviews.

I will not go into details about which particular structural targets lend themselves more easily or less easily to quantification and specificity. Nevertheless, we believe that what is important in the end is not the question of quantification or specificity, but that the member country and the Fund both view structural change as a matter of priority. The techniques of conditionality are important in some sense, because they suggest priorities. In any case, I hope that the time will come when, among the three or four "bottom lines" of a negotiation between a member country and the Fund, there will be included not only credit ceilings and exchange rate policy, which tend inevitably to be bottom lines, but in some cases such areas as price reform and trade liberalization will be bottom-line issues. This is because such areas may be equally as important to payments sustainability and growth in the medium term.

On the question of the guidelines for conditionality, I would state that we do not believe that revision of those guidelines is essential in order to move ahead in this effort. But I wonder whether the Board's guidelines are not lagging behind where the Board and the staff already are in the structural reform effort. We are increasingly inclined to believe that some revision of the guidelines would be appropriate to bring them closer to what we are trying to accomplish in our program.

In closing, let me say that we have an expression in the United States which is "fish or cut bait." It means that there comes a time in considering any issue when you either must act on your convictions, or you must head off in another direction. I have the impression that we are at such a stage: it is time to replace rhetoric about growth-oriented adjustment with steps to ensure that our programs are in fact growth oriented. Indeed, I was somewhat surprised at some of the comments made this morning, because it was not clear that those who were strongly supportive of growth-oriented programs in our theoretical discussions on December 16 are equally supportive of the policy changes needed to achieve growth. I think our masters will not have much tolerance, if we try to explain to them years hence, that our growth-oriented objectives were not achieved as fully as they could have been because we failed to make certain institutional changes, for instance, in our performance criteria. I believe it is important that we strive to avoid that outcome.

The Executive Directors agreed to continue their discussion in the afternoon.

2. EXECUTIVE DIRECTOR

The Chairman bade farewell to Ms. Bush on the completion of her 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/87/174 (12/16/87) and EBM/87/175 (12/18/87).

3. GABON - STAND-BY ARRANGEMENT - WAIVER

1. Gabon has consulted with the Fund in accordance with paragraph 4 of the stand-by arrangement for Gabon (EBS/86/269, Sup. 1) and paragraph 4 of the letter dated November 26, 1986 from the Minister of Economy, Finance and Participations attached to the stand-by arrangement, in order to reach understandings subject to which Gabon may resume purchases under the stand-by arrangement.

2. The Fund decides that, notwithstanding paragraph 4(c) of Gabon's stand-by arrangement, Gabon may resume purchases under the arrangement, provided that purchases under the arrangement shall not exceed the equivalent of SDR 42.50 million until completion of the second review contemplated in paragraph 4(c) of the arrangement and paragraph 4 of the letter dated November 26, 1986, attached to the stand-by arrangement. (EBS/87/265, 12/11/87)

Decision No. 8755-(87/175), adopted
December 17, 1987

4. APPROVAL OF MINUTES

The minutes of Executive Board Meetings 87/86 and 87/87 are approved. (EBD/87/320, 12/10/87)

Adopted December 16, 1987

5. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors as set forth in EBAP/87/231, Supplement 1 (12/16/87) and EBAP/87/273 (12/15/87) and by an Advisor to Executive Director as set forth in EBAP/87/273 (12/15/87) is approved.

6. TRAVEL BY MANAGING DIRECTOR

Travel by the Managing Director as set forth in EBAP/87/276 (12/17/87) is approved.

APPROVED: August 5, 1988

JOSEPH W. LANG, JR.
Acting Secretary