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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 85/21

10:00 a.m., February 11, 1985

J. de Larosière, Chairman

Executive Directors	Alternate Executive Directors
A. Alfidja	
C. H. Dallara	M. K. Bush
J. de Groote	
B. de Maulde	X. Blandin
	T. Alhaimus
H. Fujino	
G. Grosche	
J. E. Ismael	Jaafar A.
R. K. Joyce	L. Leonard
A. Kafka	H. A. Arias, Temporary
	E. Olsen, Temporary
	A. Abdallah
F. L. Nebbia	B. Jensen
Y. A. Nimatallah	J. E. Suraisry
P. Pérez	G. Ortiz
J. J. Polak	J. de Beaufort Wijnholds
	A. V. Romuáldez
G. Salehkhou	O. Kabbaj
A. K. Sengupta	
N. Wicks	T. A. Clark
S. Zecchini	N. Coumbis
Zhang Z.	

L. Van Houtven, Secretary
S. J. Fennell, Assistant

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Also Present

European Department: L. A. Whittome, Counsellor and Director. Exchange and Trade Relations Department: C. D. Finch, Director; M. Guitián, Deputy Director. External Relations Department: H. O. Hartmann. Fiscal Affairs Department: F. Sánchez-Ugarte. Legal Department: G. P. Nicoletopoulos, Director; Ph. Lachman. Research Department: W. C. Hood, Economic Counsellor and Director; A. D. Crockett, Deputy Director; R. R. Rhomberg, Deputy Director. Secretary's Department: J. W. Lang, Jr., Deputy Secretary; A. P. Bhagwat, G. Djeddaoui, B. R. Hughes. Treasurer's Department: W. O. Habermeier, Counsellor and Treasurer. Western Hemisphere Department: E. Wiesner, Director; S. T. Beza, Associate Director; M. Caiola, C. Cha, R. A. Elson, R. K. Rennhack. Bureau of Language Services: A. J. Beith, Director. Personal Assistant to the Managing Director: S. P. Collins. Advisors to Executive Directors: G. R. Castellanos, D. Hammann, K. A. Hansen, S. M. Hassan, G. E. L. Nguyen, J.-C. Obame, G. W. K. Pickering, T. Sirivedhin, D. C. Templeman, A. Vasudevan, M. A. Weitz. Assistants to Executive Directors: J. R. N. Almeida, E. M. Ainley, J. Bulloch, M. B. Chatah, J. de la Herrán, J. J. Dreizzen, G. Ercel, V. Govindarajan, N. Haque, G. D. Hodgson, H. Kobayashi, S. Kolb, M. Lundsager, K. Murakami, J. A. K. Munthali, M. Rasyid, J. E. Rodríguez, A. A. Scholten, A. J. Tregilgas, A. H. van Ee.

1. EXECUTIVE DIRECTOR

The Chairman welcomed Mr. Arjun Sengupta, Executive Director, to the Executive Board.

2. REPORT BY MANAGING DIRECTOR

The Managing Director, commenting on his recent visit to Europe, informed the Executive Board that in Paris he had met with officials of the French Treasury to discuss the work of the Paris Club and the multi-year approach to rescheduling and had delivered a speech to the Federation of French Industries. He had then traveled to Stockholm where he had addressed the Federation of Swedish Industries on the interrelationship between protectionism and indebtedness. He had met with the Ministers of Finance and of Trade, and the Governor of the central bank, and he had been received by the King of Sweden. On his return to Paris he had addressed the Institut de la Defense Nationale on the problems of international indebtedness. About one third of the members of the institute were military, one third academic, and one third businessmen and officials. The discussion had been fruitful and the audience had shown a remarkable awareness of the role of the Fund and of the debt problems. He had also met with delegations from Brazil and the Philippines in Paris.

3. HONDURAS - 1984 ARTICLE IV CONSULTATION

The Executive Directors considered the staff report for the 1984 Article IV consultation with Honduras (SM/85/22, 1/18/85). They also had before them a report on recent economic developments in Honduras (SM/85/26, 1/28/85).

Mr. Pérez made the following statement:

> Honduras maintained respectable rates of economic growth during the second half of the 1970s, before the onset of the economic slowdown in 1980. During the first period the authorities expanded export-oriented commercial agriculture, created a light industrial base, and added significantly to the infrastructure and capital stock of the country. However, in 1980-82 the economic and financial position of Honduras deteriorated sharply. Several factors contributed to this performance: political instability in Central America, the second oil shock, the world recession, a decline in the external terms of trade, and the implementation of countercyclical expansionary domestic fiscal and monetary policies. In 1982, the authorities implemented an adjustment program supported by the Fund aimed, inter alia, at correcting the fiscal situation of the public sector. Although the results of the program were not totally satisfactory, the

program contributed nonetheless to the implementation of a number of significant measures in the fiscal, monetary, and external areas. It should also be pointed out that the observed deviations can partially be attributed to the fact that the program was designed in a framework of economic growth; however, GDP actually declined and, consequently, the Government's revenues were lower than expected. The latter made the achievement of the fiscal target more difficult, since it was not possible to adopt complementary revenue measures at the time.

Despite the maintenance of extremely severe political and economic difficulties in Central America and the relatively weak price response of the country's principal export products to the recovery in some industrial countries, combined with the negative effects of restrictive quotas as on coffee and sugar, the economic performance of Honduras in 1984 was satisfactory. Output increased by 2.8 percent in real terms, while the rate of inflation was almost halved, from 9 percent in 1983 to 4.8 percent in 1984. The aim of the Government's economic policies was to strengthen the development of basic infrastructure, increase the domestic production of food--especially of basic grains, promote export of nontraditional products, and improve the employment situation.

The authorities are aware that the fiscal imbalances of recent years continue to be a fundamental problem. Consequently, measures were taken in 1984 to increase domestic revenues, including the imposition of a 5 percent custom service surcharge on imports, an extension of the base of the sales taxes, and an improvement in tax administration. These measures lead to an increase in central government revenues of almost 22 percent, despite the fact that some of these measures were implemented at the beginning of the second semester and, consequently, should also contribute positively to strengthen the Central Government's financial situation during 1985. Total expenditure grew significantly in 1984 owing to increases in capital outlays required to cover the domestic financing of the El Cajón hydroelectric project that will gradually start operations at the beginning of March 1985; therefore, this type of expenditures will decline in 1985. On the other hand, the increase in current expenditures resulted from the need to strengthen the country's national defense. Although the Government's overall deficit in 1984 was higher than that registered in 1983, the most recent statistical figures--albeit preliminary--show that the deficit was L 49 million (approximately 0.8 percent of GDP) less than estimated by the staff. Also, the deficit was partially covered by external financial assistance and, consequently, the domestic financing of the deficit was lower than in 1983.

Monetary developments in 1984 were characterized by an acceleration in the growth of credit to the private sector to finance the economic recovery of this sector. The latter should not necessarily be seen as an undesirable result, since private sector activity contributed to increase employment while no excess demand pressures resulted, as evidenced by the rapid fall of the inflation rate. Also, real interest rates in 1984 were positive, helping to increase savings and time deposits as a percentage of GDP. As of December 1984, M-2 had increased approximately 9 percent above the level of December 1983, while the healthy growth of quasi-money (14.3 percent) is a result of the flexible interest rate policy followed by the Honduran authorities.

In the external sector, the authorities continued with the process of liberalization of exchange restrictions. Although exports grew by 9.5 percent in 1984--in comparison with an increase of only 3.4 percent in 1983 and successive decreases in 1981 and 1982--the current account deficit of the balance of payments was higher than in 1983, owing mainly to the additional imports associated with the El Cajón project and a freer import system. The current account deficit was partially financed with development loans, mostly on concessional terms, and with external financial assistance. It is expected that the external assistance will continue in 1985 and will contribute to supporting the Government's economic program and the implementation of policies aimed at reducing the country's social problems, particularly unemployment.

The authorities fully intend to maintain the existing parity of the lempira. In their opinion, a devaluation of the lempira would not bring about significant positive effects to their price-inelastic main export crops, since their prices are exogenously determined in U.S. dollars in the international market. The potential increase in cultivated areas is a time-consuming process, and, at the moment, the acreage cultivated depends more on export quota than on prices. On the other hand, higher production costs arising from a devaluation would probably evaporate the producers' eventual increases of profitability. Also, although a devaluation would initially promote competitiveness of manufactured exports in the interregional trade--as long as the corresponding increase in production would not immediately offset the gains--the financial difficulties being experienced by the rest of the Central American countries would limit these advantages. With respect to exports to markets outside the region, the authorities are committed to use policy instruments other than the exchange rate. In this regard, an export incentive law was recently approved which includes a reduction of indirect and export taxes for the nontraditional exports, as well as the creation of a promotion fund to provide a financial basis for export operations of new products to nontraditional markets. In addition, a second free zone will be opened soon. It should be noted that both organized labor and business sectors strongly share the point of view of the authorities in relation to the exchange rate.

The authorities reached an agreement in principle to reschedule government-warranted private debt with commercial banks, equivalent to one tenth of the total external debt of the country. Payments on the institutional debt of the Government are current to date. In addition, during 1984, payments of commercial arrears were made, indicating the authorities' intentions to further reduce these arrears in the future.

The Honduran authorities consider that the projections for 1985 presented by the staff are tentative, since all forecasts are currently under revision on the basis of more recent figures for 1984. Nevertheless, these projections can be viewed as rough indications of what could be expected. It must be emphasized that the Honduran authorities have the firm commitment to continue with their adjustment efforts. In line with the recommendations of this Board and the staff in 1985, they have the intention of implementing a set of measures aimed at maintaining a satisfactory performance of the monetary, fiscal, and external sectors, although they are conscious that the pace of implementation should be carefully considered bearing in mind the particular political circumstances of the country.

In the monetary field, the credit expansion will be controlled through adequate management of the discount rate of the Central Bank, and the establishment of a limit to the amount of rediscount operations. In addition, credit limits will be set to the public sector, while basic aspects of the rediscount policy of public bonds will be reviewed, such as the interest rate. The increase of monetary aggregates is being projected in accordance with a suitable growth of the GDP at current prices, while interest rates will continue to be positive in real terms and competitive with those abroad.

In the fiscal area, besides the strengthening of the administrative control, the authorities will implement a tariff reform program including: the adoption of the Brussels Tariff Nomenclature; the conversion of duties from specific to ad valorem basis; the training of qualified personnel in the new nomenclature; and a substantial tariff review and modification in order to adapt its structure to the present economic circumstances. Government revenues for 1985 have been projected in a very conservative manner; furthermore, as a result of improvements in tax administration, the Government will collect back taxes on oil imports. The preliminary figures of government revenues in January 1985 show a continuation of the increasing trend of the second part of 1984.

In the external sector, the authorities are committed to a policy of promoting export diversification through the use of selective financial instruments, including a more flexible system of deliveries in the official market. Moreover, the authorization of foreign currency-denominated deposits will facilitate the use by exporters of their export proceeds to cover their import requirements and other external obligations.

Finally, prices will continue to reflect essentially the interplay of market forces and important steps will be taken to liberalize the controls of domestic prices which still remain.

In the framework of the government stabilization program for 1985 discussed and negotiated with international development organizations, measures will be adopted to redress, in the medium term, the financial position of the decentralized institutions such as the National Investment Corporation (CONADI) where a schedule has been established to reactivate some enterprises and to sell others to the private sector. In the same way, actions are being taken to improve the financial situation of other institutions of the public sector in an effort to eliminate transfers from the Central Government to these institutions. It is expected that these measures will produce positive results for 1986.

Mr. Arias stated that for some time Honduras had faced serious difficulties stemming from unfavorable international and regional developments that had prevented the authorities from designing a set of comprehensive stabilization policies. Directors should be cautious in judging the country's performance. Government revenues had increased, owing largely to the tax measures taken in May 1984 and the improvement in tax administration. Further action was called for, however. He wondered whether the authorities would begin converting quotas to tariffs in 1985.

The financial position of the public enterprises should continue to be strengthened so as to limit the capital transfers from the Central Government, Mr. Arias considered. The World Bank had been providing technical assistance to improve the management of the National Investment Corporation (CONADI), and he wondered how the Bank staff viewed the recent developments in CONADI and its future profitability. Would that corporation be able to contribute to the country's economic development and, if not, what options existed to prevent a further deterioration of the public finances because of its unprofitability?

The hydroelectric project, El Cajón, would be completed by 1985, Mr. Arias noted. Did the import projections in Table 6 of SM/85/26 take account of the reductions in imports of investment goods following the completion of that project? How much savings on oil imports would be generated by the plant?

The authorities were reluctant to change their exchange rate policy given the possible negative impact it could have on prices and wages, Mr. Arias observed. Although an exchange rate adjustment might have positive results, in the short term the results might be less favorable due to costs or inflationary expectations. The staff could perhaps make an analysis to indicate the size of capital outflows in 1984 and to determine an appropriate exchange rate, taking into consideration the uncertainties in the region.

Ms. Bush observed that Honduras had recently benefited from various favorable developments that had eased the financing difficulties, most notably substantial foreign assistance and capital inflows for the hydro-electric project which had generated employment and economic growth. Furthermore, favorable weather had reduced the need for food imports. While those developments had enabled Honduras to maintain budgetary and external stability, they would not necessarily be recurring and should not be relied on in the medium term. If the authorities did not take action to reorder economic priorities and lay the foundation for longer-term growth, the Honduran economy would experience serious imbalances.

The rate of inflation had fallen to about 6 percent in 1984 owing, in part, to the availability of imports to meet aggregate demand, Ms. Bush noted. Without a more coherent policy package, however, external imbalances would remain, possibly prompting the authorities to increase the trade and exchange controls in order to contain the current account deficit. Aggregate demand pressures would thereby be channeled into domestic price increases, leading to even larger imbalances. She urged the authorities to begin addressing the basic disequilibrium in their economy while they had the luxury of substantial foreign assistance.

A more direct approach to containing the current account imbalance than relying on trade and exchange restrictions might be an exchange rate adjustment, which need not lead to rampant inflation if supported by restrained monetary and fiscal policies, Ms. Bush commented. The exchange and trade restrictions represented a greater disincentive to foreign investment than the possibility of a devaluation. Foreign investors viewed an exchange rate adjustment as inevitable and were thus postponing their investment until competitiveness was restored to the local economy.

External arrears were high and substantial debt servicing obligations remained, although a rescheduling agreement had been reached with commercial banks covering more than one year's maturities, Ms. Bush noted. The Honduran external debt was equal to 67 percent of GDP and even though the debt service ratio remained manageable--20-25 percent of exports of goods and services--continued expansionary policies might force the authorities to increase their reliance on debt financing.

The relatively large budget deficits registered in 1984 and projected for 1985 were clearly unsustainable, Ms. Bush considered. In contrast to 1984, when the deficit had been largely related to investment in the hydroelectric project, the 1985 deficit would result mainly from a sharp increase in current expenditures and slow revenue growth. Additionally, the Central Government might have to make transfers to some public enterprises to cover their capital expenditures and interest payments. She welcomed the authorities' commitment to adjust tariffs and control expenditures of those enterprises and urged them to take additional steps to control current expenditures. The authorities should also eliminate domestic price controls to permit the most efficient allocation of resources.

Without tighter fiscal control, it would be difficult for the authorities to contain monetary expansion, Ms. Bush stated. It was disturbing to learn that they expected to finance a significant share of central bank credit expansion to part of the banking system through additional long-term foreign loans, which would only generate future problems. She welcomed the positive real interest rates which would provide incentives to save. She would be interested in hearing the staff's views on whether interest rates were high enough to curtail private capital outflows.

Honduras must begin its adjustment effort immediately rather than wait until pressures were such that a Fund arrangement was necessary, Ms. Bush commented. The country had experienced substantial difficulties in complying with its previous Fund program, and prompt implementation of the necessary policy measures outlined by the staff would ease the process of negotiation on a new Fund arrangement.

Mr. Nebbia noted that, following some years of financial stability and rapid growth, the economic and financial position of Honduras had deteriorated in the 1980s, owing to political instability in the region and worldwide recession. Unfortunately, the objectives of the 1982-83 stand-by arrangement had not been met, although some positive measures in the monetary, fiscal, and external areas had been implemented under the program.

Output and the rate of inflation had improved somewhat in 1984, Mr. Nebbia observed. The rate of inflation had decelerated to about 6 percent from 9 percent in 1981-83, and real GDP had increased by 2.8 percent. However, the financial situation had deteriorated during the past year. The overall government deficit had risen. Total expenditure had increased, largely because of higher capital outlays associated with the El Cajón hydroelectric project and increases in current expenditures on defense. As a large portion of the deficit had been covered by external financial assistance, the need for domestic financing in 1984 had been less than in 1983.

Monetary conditions had not improved in 1984; credit to both the private and public sectors had risen, Mr. Nebbia observed. Emphasis should be given to increasing the rate of economic growth given the social and political tensions arising from high unemployment. An increase in external assistance might facilitate the achievement of economic growth, while maintaining financial stability.

The authorities intended to improve the performance of the public enterprises by adjusting tariffs and restraining expenditure, Mr. Nebbia stated. Priority should be given to reducing current expenditures. The recent improvement in tax administration was encouraging, but further action might be needed in that area.

The authorities' intention to restrain credit expansion in 1985 was commendable, Mr. Nebbia remarked. The maintenance of positive interest rates was important to increase domestic savings and improve the balance of payments position. Could the staff indicate the possible evolution of the Agricultural Development Bank's lending operations in the future? An increase in the rediscount rate would help to contain credit demand.

Although the authorities had eased some exchange restrictions, all should eventually be eliminated, Mr. Nebbia considered. Foreign assistance and the pursuit of prudent demand management policies should help to strengthen the balance of payments position in 1985. Additionally, an appropriate exchange rate policy would improve the country's external position. He had serious doubts, however, about the need to devalue the lempira. Most exports from Honduras were agricultural products whose dollar prices were determined in the international markets. Furthermore, the amount of land cultivated in Honduras depended more on export quotas than on prices. While a devaluation would promote competitiveness of manufactured exports in the region, the financial problems of the rest of the Central American countries would limit that advantage. Could the staff comment on those arguments? Finally, he welcomed the authorities' commitment to implement a stabilization program in 1985 and wondered if Honduras would adopt a Fund-supported program in the future.

The staff representative from the Western Hemisphere Department remarked that the authorities intended to convert duties from a specific to an ad valorem basis in 1985, but they would not be able to overhaul the tax structure in that year. A large number of the 60 or so industrial and agroindustrial enterprises making up CONADI, a state-owned holding company, were facing serious financial difficulties. With World Bank assistance, the authorities had been classifying those enterprises according to their profitability.

With respect to interest rate policy, although there was a ceiling of 19 percent on lending rates, the actual level of interest rates for both loans and deposits was determined essentially by market forces, the staff representative stated. Most interest rates in the banking system were positive in real terms, but it was difficult to determine whether those rates were high enough to prevent capital flight. Nevertheless, interest rates should probably be increased to bring credit demand in line with available resources. In 1984, the pool of financial savings available to the banking system had increased by about 9 percent, while credit expansion had been nearly 19 percent. Consequently, the level of international reserves had been lowered. The interest paid on government bonds was one instrument that could be used to raise effective interest rates in the banking system. Additionally, the rediscount rate of the central bank could influence interest rates.

The El Cajón hydroelectric project would generate about 290 megawatts of electricity compared with the country's present generating capacity of 250 megawatts, the staff representative stated. About one third of

El Cajón's generating capacity would be working in 1985, thereby saving about $10 million in oil imports. The staff had taken those savings into account in its medium-term balance of payments projections.

The authorities preferred to promote exports through the use of subsidies, the staff representative pointed out. The staff, however, had serious doubts about whether such a selective approach could increase exports to such an extent that the country's balance of payments position would be viable in the medium term. Furthermore, the fiscal cost of promoting exports through subsidies would be enormous; it would cost the Government about 2.5-3.0 percent of GDP in subsidies a year to make the nontraditional exports competitive at present. The provision of subsidies would not affect imports or capital movements as would be the case if a more flexible exchange rate policy was adopted as the staff proposed. The provision of subsidies would not help some of the country's traditional exports, particularly coffee, sugar, and bananas, which faced market constraints in the United States. The staff was also concerned that the authorities' selective approach to promoting exports would distort the efficient allocation of resources. The authorities should adopt a more flexible exchange rate policy and the exchange rate should be determined by market forces.

The recent rescheduling agreement with the commercial banks had been reached on the understanding that Honduras would adopt a Fund-supported adjustment program at the latest by the first half of 1986, the staff representative from the Western Hemisphere Department indicated. The staff was not sure whether the present Government or the Government to be elected in November 1985 would approach the Fund regarding a new arrangement.

Mr. Pérez commented that the political instability in Central America severely limited the authorities' ability to achieve their economic objectives by pursuing appropriate economic policies. They had established a schedule to improve the operations of some public enterprises and to sell others to the private sector. The positive results of those measures would be felt in 1986. The exchange rate for the lempira had been fixed over the past 50 years and there was general agreement in the country that the exchange rate policy should not be changed at present.

The Chairman made the following summing up:

> Executive Directors agreed with the appraisal in the staff report of the 1984 Article IV consultation with Honduras. Directors noted that, despite the effects on Honduras of the instability in the region and the lingering effects of the past international recession, there had been a recovery in output and a slowdown in inflation in 1984. But they wondered about the durability of those gains in view of the continued weakening in the overall financial situation. In this connection, Directors pointed out that, although the country's balance of payments difficulties were being eased temporarily by foreign assistance,

Honduras needed to strengthen its stabilization effort in order to bring about a sustained improvement in its external position over the medium term and to resume sound economic growth.

Directors emphasized that it was essential to improve fiscal performance to achieve those objectives. They acknowledged the revenue effort undertaken in 1984, but stressed that further efforts should be made to improve tax administration. Directors also called attention to the need for expenditure restraint, which would be facilitated by a more effective control over the operations of and tariffs changed by the main public entities and enterprises outside the central administration.

Concern was expressed over the acceleration in the growth of bank credit in 1984. The authorities' intention to pursue a more restrictive credit policy in 1985 was therefore welcomed. The authorities were encouraged to continue with their current policy of interest rate flexibility as a result of which interest rates had become positive in real terms.

Some Directors urged the authorities to adopt measures that would permit the removal of the exchange restrictions as well as the settlement of arrears. Restrictions, they noted, constituted a significant disincentive to foreign investment. The liberalization of restrictions, combined with a more flexible exchange rate policy, would provide the incentive for the growth of exports that was needed to stimulate the economy and to ease the heavy debt service burden in the coming years.

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

4. INTERIM COMMITTEE - PROVISIONAL AGENDA

The Executive Directors considered the provisional agenda for the Twenty-Fourth Meeting of the Interim Committee, including annotations relating to the format of the meeting (EBD/85/34, 1/25/85).

Mr. de Groote inquired whether Interim Committee members would be able to change the agenda at the meeting on April 17, 1985. He was also concerned about the restrictions on attendance at the informal afternoon session, which would be an integral part of the Interim Committee meeting. If attendance at the informal session were limited to four persons from each constituency--the Committee member, accompanied by at most two associates, plus the Executive Director--he would have difficulty in convincing some Ministers of countries in his constituency to come to Washington. It was important to have representatives from all countries at the informal session to ensure that the discussion was broad and represented the views of all members. It was unfortunate that the rule limiting attendance at the Interim and Development Committee meetings to the Committee member, seven associates, and the Executive Director had never been enforced.

The Secretary replied that the Committee members traditionally approved the agenda as the first item of the provisional agenda, providing members with the opportunity to introduce changes in the agenda if they so wished.

Mr. Kafka stated that he assumed that the members of the Interim Committee would not be prevented from speaking on trade questions. On format, he had the same concerns as Mr. de Groote. He would find it difficult to inform a Minister from his constituency that he could not attend the informal afternoon session. The informal meetings should be as constructive as possible; to that end, it would perhaps be better to expand attendance to seven associates from the two associates who would obviously have to rotate and might disturb the meeting. There was no need for a formal record of the afternoon session, but he wanted reassurance that the matters discussed during the informal session would be included in the communiqué. Perhaps the Managing Director or the President of the World Bank might make an informal summary at the end of the meetings that would help the Committee members to formulate the communiqué.

The Chairman informed Directors that the Chairmen of the two Committees had suggested that trade policies be dealt with primarily, but not exclusively, in the Development Committee. A Committee member would not be prevented from speaking on trade issues at the Interim Committee meeting. The Chairman of the Interim Committee had considered the question of attendance carefully and had felt strongly that, to ensure that the informal session would have the maximum chances of success, only two associates--who need not be the same associates for the entire session--the Committee member, and the Executive Director should attend.

The Secretary stated that the informal session would be an integral part of the Interim Committee meeting. A formal record of the morning meeting would be kept in the usual fashion. As the discussions at the afternoon session would have to be integrated into the communiqué, it would be useful to have an informal summary record of that session, its form and distribution to be decided upon by the Committee Chairman and members.

The Director of the Legal Department, responding to a question from Mr. de Groote, stated that there was no need for the Resolutions establishing the Interim and Development Committees to be changed in order to hold the informal meetings. Furthermore, it was not a legal requirement to keep a formal record of the informal meeting in the afternoon.

Mr. Wicks commented that the Chairmen of the two Committees had considered the format of the meetings at great length. They had diverse points of view and were deeply concerned about the success of the discussions. The Executive Board should consider carefully the procedures proposed by the Chairmen before suggesting a new approach. The question of format should be decided on before the meetings in April, as it would be unfortunate if the Committees spent the first hour of the meeting debating the appropriate procedure.

Mr. de Groote agreed with Mr. Wicks that it was important to support the Chairmen in their attempt to hold an effective meeting. The proposed format should be discussed beforehand so that a compromise could be reached, and to ensure that the Chairmen did not reach a decision that was divisive of members. If attendance at the morning session were limited to the Committee member, seven associates--who need not be the same for the entire session--and the Executive Director, perhaps it would be easier to convince the Committee members that attendance at the informal session should be restricted further. Entry to the meeting room could be restricted to those wearing color-coded entry tags.

Mr. Kafka stated that he was not objecting to the format proposed by the Chairman, but was expressing his concerns about the limitations on attendance.

The Chairman remarked that the concerns expressed by some Directors about the restricted attendance at the informal session would be conveyed to the Chairmen of the Interim and Development Committees. It was very important that the format be decided upon well in advance of the meeting so that Committee members, particularly those from multicountry constituencies, would know how many associates could attend the meetings. It would be discourteous to inform a Minister on the day of the meetings that he would be unable to attend.

The Secretary said that it was his understanding that the Interim Committee Chairman intended to inform the Committee members of the draft agenda and the suggestions with respect to format and procedures, following the present meeting. Members would have an opportunity to comment on those suggestions so that a consensus could be reached on the format prior to the meetings in April.

The Director of the Legal Department, responding to a question from the Chairman, said that a simple majority of the members was necessary to decide on procedural matters in the Interim Committee.

Mr. de Groote stated that it was not so much a problem of informing Ministers and Governors beforehand about the format of the meeting but of convincing them to come to Washington. Attendance by representatives from all member countries was essential to ensure that there was overall support for any proposals that would be made.

The Chairman remarked that fewer Ministers might attend the meeting because of the restrictions on attendance. However, the advantages and disadvantages of a smaller meeting should be assessed. The Committee Chairmen had decided that in order to have an active, informal discussion attendance should be restricted.

Mr. Joyce agreed that the format should be established well in advance of the meeting through consultation by the Chairmen with the Committee members. He shared the doubts expressed by some Executive Directors at the present meeting regarding the rules on attendance; Directors' concerns should be conveyed to the Chairmen. It was important to establish rules regarding attendance, as the practice of holding an informal session in addition to the formal session might be repeated in the future. He was not necessarily proposing that seven associates should be allowed to attend the afternoon session but that some recognition should be given to the fact that multicountry constituencies would perhaps need to have more associates at the meeting than single country constituencies. He agreed with Mr. de Groote that the rule should be observed that attendance at the morning session should be limited to the Committee Member, seven associates, and the Executive Director.

The Chairman, responding to a question from Mr. Joyce, said that Committee members would be allowed to discuss debt-related issues in the morning session, as well as other topics that they considered important, as long as their spoken statements were limited to less than ten minutes. If members wished, they could enter an extended statement directly into the record.

The Secretary remarked that in recent years it had become very difficult to enforce the limitation on attendance at the meetings to the Committee member, seven associates, and the Executive Director. The attendance list had grown from 394 in April 1980 to 720 at the September 1984 meeting. The new meeting rooms in the Fund were larger than the Eugene Black Auditorium, where the meetings had previously been held, and attendance had increased correspondingly. In order to limit attendance as set out in the Resolution establishing the Committee, he would need the cooperation of all the delegations.

Mr. de Groote suggested that entrance to the meetings should be restricted to those wearing color-coded tags, nine of which would be issued to each delegation. The delegation could then decide on how those nine badges would be distributed. Associates could rotate throughout the session by exchanging badges.

Mr. Nebbia stated that he had a different problem from Mr. de Groote regarding attendance at the informal session. Even if attendance were limited to two associates, he would still find it difficult to discourage Ministers from his constituency from coming to Washington with the hope of attending the meetings. The limit on attendance at the informal session should be increased for multicountry constituencies.

As the informal session would be the core of the meeting, the communiqué should reflect the discussion at that session, Mr. Nebbia considered. Perhaps an informal record should be kept or the Chairman should sum up the meeting.

The Chairman assured Mr. Nebbia that the communiqué would reflect the sense of the discussion in the informal session.

Mr. Alfidja expressed his doubts about limiting to two the number of associates to be present at the informal session. With respect to the formal session, he agreed that the limit on the number of participants from each constituency of one member, the Executive Director, and seven associates should be enforced. He would cooperate with the Secretary on finding a diplomatic way to limit attendance.

Mr. Dallara indicated his agreement with the suggestion to limit attendance at the formal meeting to nine by issuing color-coded tags. Furthermore, he supported the limit on attendance at the informal afternoon session. Even though he was from a single country constituency, it would be difficult for him to inform his Ministers that they could not attend the meetings. There were many officials at the Deputy Secretary and Under Secretary levels in various agencies of the U.S. Government who would be excluded from the informal sessions despite their wish to attend.

Mr. Dallara made the following statement:

> The United States attaches considerable importance to the upcoming Interim and Development Committee meetings, believing they can provide a frank and open exchange of views on the prospects and policies for adjustment, growth, and balance of payments sustainability in the medium term. I would underscore, as the provisional agendas do, the medium-term nature of these discussions.
>
> In order to help achieve this frank exchange of views, we and others suggested a number of procedural arrangements for the meetings. These included a joint discussion by the two committees on issues of common interest, a maximum of informality in the discussions to facilitate a genuine dialogue, and a brief communiqué or brief communiqués, to avoid the need for lengthy formal statements in the afternoon sessions.
>
> We are pleased that the Chairmen of the two committees, the Chairman and President Clausen, have worked closely together in developing a joint approach to the meetings which embodies a number of the suggestions which have been put forward.
>
> We would have preferred a joint meeting, believing that this would have provided the most productive framework. The Chairmen have taken this into account, but have put together a somewhat different approach, with which we are prepared to work. We believe the proposed procedural arrangements should, in our view, contribute to frank and open discussions. Included among these are the time limits for the formal oral remarks in the morning session, the informal afternoon sessions, and the joint dinner to discuss issues of common concern, which we believe

could be helpful in this whole process. We support these arrangements and hope that members will make every effort to take full advantage of them.

With regard to the issue of the communiqué, I have noted the views of other Directors, expressing interest and concern that the informal discussions be in some form incorporated into the final communiqué of the meeting. While I can appreciate these concerns that the communiqué should reflect those discussions as well as the formal discussions, I would caution strongly against efforts to develop a detailed, substantive communiqué. This, in our view, would be time-consuming, counterproductive, and indeed inconsistent with the basic purpose of the meeting to encourage an open, frank discussion of policies for growth and balance of payments adjustment in the medium term.

I have noticed a tendency today to evaluate these coming meetings on the same basis as the traditional Interim and Development Committee meetings, that is, by looking to see what is in the text of the communiqué. I recognize that it may take a certain leap of faith to acknowledge that other things can come out of a meeting that are not necessarily reflected in the black and white of the communiqué, but which are important and meaningful. It is in that spirit that I suggest that efforts to develop an extremely detailed substantive communiqué for these meetings could really miss the purpose of the meeting and could be counterproductive.

With regard to the provisional agendas, I would make the following comments. The agenda for the morning session is rather straightforward, covering items 3 and 4. I take the point mentioned by Mr. Joyce that in formal statements submitted for the record, members should not, of course, be precluded from addressing some of the issues of the afternoon session which they want to touch upon.

The subjects for discussion in the afternoon session are taken directly from paragraph 5 of last fall's Interim Committee communiqué and repeated in the Note to the provisional agenda for the upcoming meetings. We support this, but have two particular concerns. The first relates to the treatment of policy issues. We noted that agenda item 3-b "World economy in the medium term: policy issues" is slated for discussion in the morning session, but it is not clear that it is an integral part of the discussion in the afternoon session.

There are certain issues related to adjustment efforts and balance of payments prospects in the medium term which are perhaps implicit in the language lifted from last fall's communiqué. We of course support that language as providing the basic framework for the informal afternoon discussions. But there are certain policy issues, some of which fall within the traditional concerns of the Fund, such as fiscal, monetary, exchange rate, pricing, and structural policies, which are not highlighted in the excerpt from last fall's communiqué. However, I am sure that we would all recognize them as important for the medium-term adjustment efforts which will be under consideration.

Therefore, I wonder whether some means could be found to clarify that certain policy issues covered by 3-b, which are part of the formal discussion in the morning, also be covered in the informal afternoon session. It seems to us that these are not just policies for the short term, but are an important part of any medium-term solution to the problems we face.

My second point is with regard to potential overlap of the two agendas. I recognize that an effort has been made to minimize the overlap between the two committees. To a certain extent, some overlap will be unavoidable because the language of the two communiqués agreed to last fall touches on a number of the same subjects. Nevertheless, there are perhaps two areas where the potential for overlap still seems to exist and could be minimized. The principal discussion of trade policy issues has been pointed toward the Development Committee, and the discussion of the medium-term outlook pointed toward the Interim Committee. But, in the area of capital flows, I suggest that it would be useful if it were understood that the Interim Committee would focus on commercial banks' capital flows and the Development Committee focus on direct investment and concessional flows.

We recognize that these agendas are the proposals of the Chairmen, and therefore we make these comments in the same spirit that other comments have been made. I would, of course, appreciate that our concerns be referred to the Chairmen and be taken into account as appropriate.

In concluding, let me reiterate our basic support for the provisional agenda and the various procedural arrangements which have been put forward as providing a potentially productive framework for these upcoming unique discussions. We also believe it will be crucial in the preparation of these meetings for the two staffs to continue to work closely together in the preparation of papers for these meetings, so as to minimize overlap and to ensure consistency in analysis and approach. With such preparations, I believe that we can look forward to a productive and meaningful dialogue during these meetings.

The Chairman stated that he had always considered that item 3(b) of the provisional agenda would be an integral part of the discussion in the informal session, and the wording of the note to the provisional agenda should be changed to reflect that view. Consideration by the Committee of the policy issues relating to both debtor and industrial countries was important.

Mr. Dallara agreed that the afternoon session should include consideration of appropriate medium-term macroeconomic adjustment policies in both the developing and industrial countries.

Mr. Abdallah welcomed the importance with which the U.S. Government regarded the upcoming Interim and Development Committee meetings. The developing countries also attached great importance to those meetings and it was therefore essential that their outcome be successful. Only if the Governors attending the meetings were well informed and open minded would a genuine dialogue take place and the outcome be worthwhile.

The difficulties that would face multicountry constituencies if attendance were restricted at the informal session had been noted by previous speakers, Mr. Abdallah stated. He had recently informed the Ministers of Finance for Sierra Leone and Nigeria, the members of the Interim and Development Committees, respectively, of the rules regarding attendance. They had been concerned that some of their colleagues might not be able to attend the meetings. The fact that the meetings were held in Washington had a special attraction to Ministers from developing countries who had a number of issues to discuss with the Management of the Fund and the Bank. He agreed with other Directors that attendance at the more formal morning session should be limited to the Committee member, seven associates, and the Executive Director.

The limit on attendance at the informal session should be regarded as experimental, Mr. Abdallah considered. The discussion at that meeting should be recorded officially, however briefly, and the sense of the discussion should be reflected in the communiqué. If no official record was produced, each Committee member would depart with a different impression of the discussion. Press reports on their views would therefore differ in content as well as emphasis. It would be unfortunate if the experimental informal session, the principal purpose of which was to promote genuine dialogue, should generate misunderstandings. The best way to ensure that Committee members did not get sidetracked on political problems or technicalities but discussed the real issues of international debt and development was to ensure that an official record was kept and that the communiqué included the points made in the informal discussion.

The developing countries hoped that the meetings would lead to an increase in the flow of resources to their economies and greater cooperation on the problem of external indebtedness, Mr. Abdallah remarked. The rich industrial countries undoubtedly had their own expectations regarding the outcome of the meetings, and he hoped that the two groups of countries would find a common ground early in the discussions. Finally, he supported the draft agenda for the next meeting of the Interim Committee.

Mr. Sengupta made the following statement:

I have the impression from the discussions that have taken place so far in the Board and from the Chairman's and Mr. Van Houtven's statements that the press communiqué of the Interim Committee will reflect the general sense of the informal discussions in the Interim and Development Committees. It is also my understanding that some record will be maintained of the informal discussions that take place in these Committees.

Mr. Dallara has mentioned that the coming Interim and Development Committee meetings are important to the United States. We also recognize that these meetings are very important since they would be dealing with a number of issues relevant to us, and from the point of view of the orderly functioning of the international monetary and financial system.

I have a point to make on the treatment of the question of allocation of SDRs. A majority of the members of the Interim Committee are in favor of an immediate allocation of SDRs. The Group of Twenty-Four representing all the developing countries gave a call for a substantial and immediate allocation. The Board has discussed these issues extensively on earlier occasions, and I also note that on the basis of a Board discussion to be held on March 11, 1985 a further report will be made to the Interim Committee. It is recognized that what is needed now is not any further technical analysis on the need to allocate SDRs but to develop a political consensus. In this background I would request the inclusion of the question of allocation of SDRs in Item No. 4 also for discussion in the afternoon informal session on April 17, as that would provide the necessary political forum for useful exchange of views on this question at the level of Ministers.

I recognize that the items included in the present agendas of the Interim and Development Committees cover some of the major areas of concern of the developing countries. In different forums the developing countries have indicated the subjects which they consider to be of great relevance to the orderly functioning of the international monetary and financial system and to the solution of the problems of their own development. They include, besides increased concessional flows and aid through multilateral institutions, SDR allocations, external indebtedness, sustained growth of exports, misalignment and volatility of exchange rates, and coordination of macroeconomic policies among the developed countries. I am aware that we may not be able to include at this stage all the subjects of concern to the developing countries in the agendas of these special meetings. The broad items to be discussed have already been indicated by the Interim and Development Committee communiqués. I find that concessional flows which I hope will include IDA assistance will be discussed in the Development Committee. However, it will be necessary to ensure that subjects which have a bearing on the items listed in the provisional agenda of the Interim Committee, for example exchange rate variability and coordination of policies among industrial countries, are adequately discussed. In this context, it may be noticed that we do not have a specific subject on the future role of the Fund in the provisional agenda, similar to the one on the World Bank, included in the Development Committee agenda. However, I believe that the scope of the discussion on the subjects to be covered in the informal session would be extensive enough to cover this and all major areas of policy that the Fund's Articles provide for. I gather from your statement that policy issues would be discussed in the afternoon sessions as I have indicated.

We hope that the discussions at the spring meetings of the Interim and Development Committees would form a beginning toward a larger discussion on the questions of the reform of the international monetary and financial system.

Mr. Zhang inquired whether a televised monitoring system could be set up for the benefit of associates who did not have access to the informal sessions. With respect to the agenda, it might be necessary to allocate an entire day to the informal session in view of the number of topics to be discussed. Finally, he agreed with Mr. Sengupta's suggestion that item 4 of the provisional agenda should be discussed in the afternoon session.

Mr. Wicks agreed with Mr. Sengupta that a communiqué of some substance was particularly warranted given the informal and fairly restricted nature of the meeting. A communiqué drafted in neutral and studied language, capturing the main elements of the discussion, would be helpful. He disagreed, however, with Mr. Sengupta's suggestion that the question of an SDR allocation should be discussed in detail in the afternoon's informal session. His authorities had been a little surprised to see the emphasis given to the question of an SDR allocation in the provisional agenda of the formal session.

He supported the suggestion that, on the question of international capital flows, the Interim Committee should focus on commercial bank capital flows and the Development Committee on direct investment and concessional flows, Mr. Wicks indicated. The afternoon informal session should be well structured. Perhaps the Committee Chairman should send a telex near the time of the meeting informing members of the main items that might be discussed in the afternoon. He wondered when the background papers prepared by the staff would be circulated to the Committee members and in what form.

The Chairman remarked that it was the Committee Chairman's intention to structure the afternoon discussion in consultation with his colleagues.

The Secretary stated that Committee members would receive in advance of the meeting a substantive document on the world economic outlook, Fund surveillance, trade policy issues and developments, external indebtedness of developing countries to commercial banks, official export credits, and developing countries' indebtedness to official creditors. Those documents would be prepared following the Executive Board's discussion of those issues between March 15 and March 22.

The Chairman agreed with a suggestion put forward by the Secretary that the staff papers prepared for the Executive Board's discussion of those issues should also be made available to the Committee members. A list of the staff papers should be included in the main documents.

Mr. Dallara stated that he was strongly in favor of integrating the staff papers into the material made available to members of the Interim Committee.

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

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/85/20 (2/8/85) and EBM/85/21 (2/11/85).

5. KENYA - STAND-BY ARRANGEMENT - EFFECTIVE DATE

1. The Fund notes the arrangements made for the financing of the expected balance of payments deficit in 1985 described in EBS/84/261, Supplement 3, and finds that these arrangements are satisfactory.

2. Accordingly, the stand-by arrangement for Kenya set forth in EBS/84/261 shall enter into effect on February 8, 1985.

Decision No. 7904-(85/21), adopted
February 8, 1985

6. RULES AND REGULATIONS - OFFICIAL HOLIDAYS - AMENDMENT OF RULE B-4

The Executive Board approves the proposal to amend Rule B-4 of the Rules and Regulations, as set forth in EBAP/85/29 (2/5/85) to reflect U.S. legislation establishing a new U.S. public holiday in 1986.

Adopted February 8, 1985

7. ASSISTANT TO EXECUTIVE DIRECTOR

The Executive Board approves the appointment of an assistant to Executive Director as set forth in EBAP/85/33 (2/6/85).

Adopted February 8, 1985

8. EXECUTIVE BOARD - INFORMAL RECESS

The proposed period for the Executive Board's informal recess, as set forth in EBAP/85/34 (2/6/85), is approved.

Adopted February 8, 1985

9. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors and by an Advisor to Executive Director as set forth in EBAP/85/35 (2/7/85) is approved.

APPROVED: November 6, 1985

LEO VAN HOUTVEN
Secretary