INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 85/138

3:00 p.m., September 11, 1985

J. de Larosière, Chairman
R. D. Erb, Deputy Managing Director

Executive Directors	Alternate Executive Directors
A. Alfidja	
C. H. Dallara	M. K. Bush
J. de Groote	
B. de Maulde	
M. Finaish	
H. Fujino	M. Sugita
G. Grosche	
	Jaafar A.
R. K. Joyce	
	H. A. Arias
	T. A. Clark
H. Lundstrom	H. Fugmann
E. I. M. Mtei	A. Abdallah
F. L. Nebbia	
P. Pérez	J. E. Suraisry
	G. Ortiz
J. J. Polak	J. de Beaufort Wijnholds
C. R. Rye	
G. Salehkhou	O. Kabbaj
A. K. Sengupta	A. S. Jayawardena
S. Zecchini	N. Coumbis
Zhang Z.	Jiang H.

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

Also present

African Department: R. J. Bhatia, Deputy Director; J. W. Kratz. Asian Department: C. Sassanpour. European Department: G. Szapary. Exchange and Trade Relations Department: C. D. Finch, Counsellor and Director; W. A. Beveridge, Deputy Director; M. Guitián, Deputy Director; J. T. Boorman, C. Brachet, S. Kanesa-Thasan, K. M. Meesook. External Relations Department: H. P. Puentes. Legal Department: G. P. Nicoletopoulos, Director; J. G. Evans, Jr., Deputy General Counsel. Middle Eastern Department: G. Tomasson. Research Department: W. C. Hood, Economic Counsellor and Director; R. R. Rhomberg, Deputy Director; A. D. Crockett, Deputy Director; K.-Y. Chu, N. M. Kaibni, M. A. Wattleworth, H. H. Zee. Secretary's Department: J. W. Lang, Jr., Deputy Secretary. Treasurer's Department: W. O. Habermeier, Treasurer; T. Leddy, Deputy Treasurer; D. Williams, Deputy Treasurer; J. E. Blalock, E. Decarli, D. Gupta, D. V. Pritchett, G. Wittich, B. B. Zavoico. Western Hemisphere Department: S. T. Beza, Associate Director. Personal Assistant to the Managing Director: S. P. Collins. Advisors to Executive Directors: E. M. Ainley, P. E. Archibong, D. Hammann, S. M. Hassan, J. Hospedales, G. Nguyen, J.-C. Obame, P. Péterfalvy, G. W. K. Pickering, M. Z. M. Qureshi, T. Sirivedhin, A. Vasudevan, M. A. Weitz. Assistants to Executive Directors: I. Angeloni, W.-R. Bengs, M. B. Chatah, J. de la Herrán, J. J. Dreizzen, G. Ercel, V. Govindarajan, L. Hubloue, O. Isleifsson, Z. b. Ismail, K. Murakami, M. Rasyid, J. Reddy, D. J. Robinson, C. A. Salinas, M. Sarenac, B. Tamami, A. J. Tregilgas, E. L. Walker, Yang W.

1. ENLARGED ACCESS POLICY - EXTENSION AND ACCESS LIMITS FOR 1986; AND LIQUIDITY POSITION AND FINANCING NEEDS

The Executive Directors continued from the previous meeting (EBM/85/137, 9/11/85) their consideration of staff papers on preliminary policy considerations concerning the enlarged access policy and the limits for 1986 on access to the Fund's resources, including the special facilities (EBS/85/174, 7/23/85; and Cor. 1, 8/1/85; and EBS/85/187, 8/9/85), together with a staff paper on the Fund's liquidity position (EBS/85/186, 8/7/85).

Mr. Suraisry considered that a strong case could be made for keeping the present access limits in 1986. The latest world economic outlook papers showed that there were continuing strains and uncertainties in the international financial system. The present limits gave the Fund the flexibility that was essential to enable it to respond appropriately to the financing needs of individual members that faced balance of payments problems that were large in relation to their quotas. At the same time, staff and management had applied those limits cautiously, prudently, and within the Fund's guidelines and policies. Moreover, the staff had shown that the Fund's liquidity position should enable the institution to finance the present limits in 1986.

However, the enlarged access policy was temporary, Mr. Suraisry commented. It was generally agreed that the policy should be phased out, and it seemed preferable to do so gradually, rather than abruptly. The Fund's resources were limited, and in 1987 and beyond the Fund could find it difficult to mobilize new resources, particularly in view of the growing problem of overdue financial obligations to the institution. He agreed with the staff that the problem of prolonged use should be contained, but that problem could be tackled in the context of the actual implementation of the enlarged access policy. While he preferred to retain the present limits, he would consider supporting a consensus in favor of a modest reduction in the cumulative access limits. He agreed with the staff that the current annual and triennial access limits should remain unchanged in 1986.

He endorsed the staff's recommendation to retain the present access limits for the special facilities for the reasons the staff had given, Mr. Suraisry said. The special facilities had provided a valuable source of rapidly available assistance for many members, and he attached importance to using those facilities flexibly and effectively.

He agreed with the staff's general conclusion that barring major shocks, the Fund's liquidity position was likely to remain comfortable in the rest of 1985 and 1986, Mr. Suraisry remarked. All the principal liquidity ratios were moving broadly in the right direction. Although the Fund's liquidity position was comfortable, experience showed that conditions could change, often rapidly, and the Executive Board should of course continue to keep the position under close review in the coming period.

Mr. de Maulde commented that although world economic conditions had improved since the adoption of the enlarged access policy, the process of international adjustment was not yet complete, and the outlook for the world economy remained highly uncertain. The prospects for the remainder of 1985 and for 1986 suggested that little improvement in the balance of payments position of indebted developing countries was likely. The gross financing requirement of the indebted developing countries was expected to increase from $102 billion in 1985 to $110 billion in 1986. The strains and uncertainties that had plagued the international economy at the time of the introduction of the supplementary financing facility had essentially persisted.

The Fund's effectiveness as a source of economic policy advice was crucially dependent upon its ability to commit sizable resources of its own, Mr. de Maulde remarked. Experience over the previous several years showed the extent to which the Fund's effectiveness and credibility hinged not only upon the conditionality associated with access to its resources, but also upon the size of the resources at its disposal. Moreover, in handling cases that required concerted action in cooperation with official and private creditors, the Fund should be able to act both to meet its own objectives and to show that it was able to remain financially involved in the adjustment process. Otherwise there was some risk that the Fund could gradually be turned into, or perceived as, a mere provider of technical assistance and policy assessments on behalf of creditors, whose objectives and concerns might well differ from those of the Fund.

The pace at which individual countries were able to correct their external imbalances was far from uniform, Mr. de Maulde noted. Therefore, access policy must continue to give the Fund the flexibility it needed to provide effective support in individual cases. Many members with Fund-supported adjustment programs or which had not yet adopted needed adjustment policies faced heavy debt service payments in coming years; those countries would likely need large-scale debt restructuring in a medium-term context to restore a viable balance of payments position.

All the points he had noted had been made in EBS/85/174 and they had led him to conclude that the current access limits should be maintained in 1986, Mr. de Maulde commented. The staff itself had suggested in the first two paragraphs of its concluding section on pages 9 and 10 that its own analysis led to the same conclusion. In the third paragraph, however, the staff had in effect tried to second guess what a minority of Executive Directors might believe: it had suggested that if a clear signal of the direction of the Fund's policies were deemed unavoidable, a limited reduction in the cumulative access limits could be considered. That conclusion seemed entirely inconsistent with the staff's own analysis in EBS/85/174. His authorities had concluded from that analysis that the current access limits should be maintained in 1986. In addition, the access limits for the special facilities should also be maintained in 1986.

The only significant change in the Fund's liquidity position since the previous discussion was the slightly more positive staff forecast: the borrowed resources gap that had been expected to appear at the end of 1986 had disappeared, Mr. de Maulde remarked. The staff had concluded that the Fund's overall liquidity position continued to be satisfactory and was expected to remain comfortable through 1986. The staff had concluded that liquidity considerations would not seem to provide an important reason for reducing the access limits for 1986.

The Treasurer said that in 9 of the 11 cases mentioned on page 5 of EBS/85/186, the member's request for an arrangement with the Fund had not been eliminated but was to be carried over to 1986. Of the two remaining cases, one country did not have an urgent balance of payments need to use the Fund's resources, and the other member appeared unable to adopt the measures needed to achieve a viable balance of payments position.

The question had been raised whether the implementation of the enlarged access policy had caused a reduction in the use of the Fund's resources, the Treasurer recalled. Table 2 on page 6 of EBS/85/186 showed that gross commitments of Fund resources in 1985 and 1986--namely, SDR 4.5 billion and SDR 4.2 billion, respectively--would be above or about the same as in 1984--namely, SDR 4.1 billion. The table also showed that gross purchases had declined somewhat from the high level in 1984 of SDR 7.2 billion to SDR 5.1 billion in 1985. However, the level was expected to increase to SDR 6.2 billion in 1986. Those figures suggested that the Fund was not retreating from its role in providing financial assistance. Directors had correctly noted that there was a slowdown in the use of Fund resources on a net basis, and that that trend was expected to accelerate in 1986. That outcome was the result of the large-scale extension of credit by the Fund in earlier years. However, Table 2 showed that although the net change in Fund credit outstanding would be significantly reduced in 1985 compared with 1984, it would nevertheless be positive and remain so in 1986. Moreover, the staff estimate for 1986--SDR 0.2 billion--was likely to prove to be on the low side given the uncertain outlook for the world economy. It seemed to be premature to conclude that there was a trend of contraction in net Fund credit. In fact, there had been a fairly high level of purchases in recent years, and the level was expected to remain high in 1986. At the same time, repurchases had been picking up, and while the rate of expansion in net Fund credit was slowing, a contraction in net Fund credit in 1986 seemed unlikely. Individual countries would make net repurchases in coming months, but net credit for the membership as a whole would likely continue to increase.

There were few indications of likely trends in the use of Fund resources in 1987, the Treasurer commented. Predictions for such relatively distant periods were especially difficult to make because most arrangements with member countries covered one year, rather than two or three years. Still, the staff suspected that there would continue to be substantial purchases in 1987, given the continuing balance of payments deficits forecast for developing countries. In addition, there were risks inherent in the external position of some industrial countries that were not yet either Fund creditors or debtors. Much would depend upon the evolution of the world economy and the international payments situation as well as the ability of non-Fund financing sources to provide the resources necessary to finance members' balance of payments deficits.

There seemed to be some uncertainty among Executive Directors about how long the Fund's liquidity position was likely to remain comfortable, the Treasurer remarked. The volume of the Fund's usable currency holdings was admittedly at an historic high--roughly SDR 40 billion on an unadjusted basis--and the list of countries whose currencies were usable was relatively long. The countries with external positions that were considered sufficiently strong to include their currencies on the list of usable currencies had quotas that were approximately 70 percent of total quotas. That share was unusually high: it had been about 50 percent in 1980 and 1981. That latter position--in which roughly half of the Fund's quotas belonged to countries with strong external positions and half belonged to countries with balance of payments deficits--was basically symmetrical. In that context, the present position was clearly asymmetrical, although it was important to remember that the Fund's two largest creditors had substantial external current account deficits. Hence, he agreed with those Executive Directors who had concluded that, on the supply side of the Fund's liquidity position, there was some risk of a decline in the supply of usable currencies. Nevertheless, the staff had made a precautionary adjustment of about SDR 10 billion in the estimate of the Fund's usable assets. That adjustment was substantial and left a sizable--about SDR 30 billion--usable currency base at least for 1986.

The staff continued to feel that the Fund's liquidity position was not an important reason for reducing the access limits in 1986, the Treasurer said. The staff's estimates suggested that if the access limits were reduced in line with the illustration in EBS/85/186, the impact on the Fund's liquidity would not be significant. Of course, the liquidity position could change, and the staff believed that it should be kept under close review.

Arrears to the Fund amounted to about SDR 400 million, the Treasurer noted. That amount might not be large in relation to the Fund's total liquidity, but the countries with those arrears had a much larger amount--about SDR 1.5 billion--in outstanding credit to the Fund. Accordingly, the staff agreed with Executive Directors who had stressed that it was important to bear those arrears in mind, which could over time adversely affect the Fund's credit standing. For the time being, the arrears were not sufficiently large to have a serious effect on the Fund's liquidity position. A separate discussion on overdue financial obligations to the Fund was to be held on November 25, 1985.

Mr. Dallara said that he continued to feel that the Executive Board should avoid taking steps at the present stage which might well limit its options in the period after 1986. A further comment on the Fund's likely liquidity conditions after 1986 would be helpful.

The Treasurer remarked that in the absence of significant unexpected developments in the world economy, the Fund's liquidity position was expected to continue to be fairly comfortable by the end of 1986. The Fund's two largest creditors--the United States and Saudi Arabia--had substantial current account deficits, but there was no reason to expect the U.S. dollar to be removed from the list of usable currencies in 1986 or 1987. The staff's estimates of the Fund's usable resources included a substantial margin of adjustment, but the list of usable currencies was likely to be somewhat reduced over time.

The staff expected the demand for Fund resources to continue to be substantial in 1986, and it was of course conceivable that the demand would keep the Fund's liquidity position from being comfortable in 1987, the Treasurer went on. Mr. Dallara apparently was concerned about the possible risk of having to advance the next general quota increase or of having to borrow additional sums. For the moment, however, the staff did not foresee a liquidity squeeze by the end of 1986. There was of course some risk that such a squeeze could occur, but given the current and prospective conditions in 1986, the staff did not expect liquidity problems to arise by the end of 1986. The Executive Board might have to consider whether or not additional borrowing by the Fund was required, but that issue had also to do with the appropriate mix of resources. If the Fund's liquidity were to come under considerable pressure, a case could be made for using one of the credit arrangements that had been negotiated specifically for such a situation--namely, the General Arrangements to Borrow (GAB), and any associated agreements with countries with a sufficiently strong external position.

The Chairman remarked that the Fund's financial position followed a cyclical pattern. A trend in which repurchases dominated the Fund's financial situation had begun in 1985/86 and would gather strength in 1987/88; resources were flowing back to the Fund, thereby strengthening its liquidity position. That trend should be kept in mind in assessing the means that would be available to finance members' possible need for enlarged access in coming years.

The Director of the Exchange and Trade Relations Department commented that developments since the drafting of the staff papers had tended to increase the staff's concern about the possible increase in the demand for Fund resources and about the need for adequate annual access limits under the enlarged access policy to enable the Fund to respond to members' financing needs in a rapid and flexible manner. The amounts of the financing packages that the Fund had been helping to arrange over the previous two months had not been particularly large, but their relative importance for the countries concerned had been substantial, and the growing difficulty in arranging the packages had been a cause for concern. It seemed odd for the Fund to be unable to make an adequate contribution to the package that was meant to support policy measures that the Fund itself strongly advocated.

In its papers the staff had not meant to suggest that the prudent application of the access limits under the enlarged access policy in individual cases was a means of phasing out the enlarged access policy, the Director continued. The issue of the phasing out of that policy was of course still being considered by the Executive Board. The staff had meant to say that it was important to note that enlarged access had been leading to the prolonged use of Fund resources, and that the issue of prolonged use should be addressed. The staff believed that the member countries concerned should introduce appropriate policies that would obviate their need for continued access to the Fund's resources. The adoption of policies consistent with a reduction in the gross use of Fund resources by certain countries would eliminate the main problem related to the enlarged access policy--namely, the prolonged use of the Fund's resources by some members. Having the Fund become a permanent source of financing for individual members would be inconsistent with the institution's monetary character.

The Executive Board could of course decide to eliminate the triennial access limits, the Director of the Exchange and Trade Relations Department commented. However, it would then have to be understood that access under a three-year arrangement would be the equivalent of three times the annual access limit under the enlarged access policy.

The Director of the Research Department recalled that the question had been raised why commodity prices had continued to be soft despite the turnaround in the rate of output. It was important to remember that the expansion of industrial output had not been particularly vigorous and had indeed slowed somewhat from its pace at the beginning of the recovery. In addition, the rate of inflation generally had been declining, and there had been a decline in petroleum prices, which were an important part of the complex of production and commodity prices. In any event, the substantial absolute decline in commodity prices which had begun in mid-1984 was attributable more to supply factors than to demand conditions. The increases in total commodity production in 1984, about 5.9 percent, and in total commodity supply--production plus stocks--of almost 4 percent, were the largest rises since the late 1960s. As a result, there was an excess supply of a number of commodities; and there had been substantial increases in production thus far in 1985, although the increases in most commodities had been less substantial than in 1984. A departmental memorandum on commodity prices was in the final stage of preparation.

It had been noted that some members had not submitted requests to use the compensatory financing facility because they had already nearly reached the quota limit on access to that facility, the Director commented. The new quotas and quota limits had had the effect of increasing the absolute access to the compensatory financing facility; no member had reached the new access limits once the new quotas had taken effect. The only countries that were currently at or near the limit were those that had used the facility in the period since the new quotas had come into effect. The staff had commented on those cases in detail in the staff papers.

The Director of the Legal Department recalled that the question had been raised whether the annual access limit under the enlarged access policy could be less than 100 percent when the Articles of Agreement enabled a member to make cumulative purchases up to 100 percent of quota and to use any available reserve tranche in any given period. As the staff understood it, any reduction in the annual limit under the enlarged access policy would apply only to the annual limit on purchases under that policy and would not apply to amounts that a member might purchase under the credit tranches outside the enlarged access policy. The enlarged access policy was available to members that had a need for Fund resources which was very large in relation to their quotas. Accordingly, arrangements providing for use of Fund resources under the enlarged access policy were available to members only when the use would bring the Fund's holdings of the member's currency above 200 percent of quota. The Fund was clearly entitled to set an annual access limit on arrangements providing for the use of Fund resources under the enlarged access policy of less than 100 percent of quota. The amounts that members could receive under policies other than the enlarged access policy were to be determined by the applicable policies. Paragraph 2 of the decision on the enlarged access policy (No. 6783-(81/40), 3/11/81) stated that "access to the Fund's resources under other policies of the Fund will remain available in accordance with the terms of those policies." Under the credit tranche policies members could obtain financial assistance from the Fund which would, and was often, less than 100 percent of quota.

The Chairman said that as he understood it, prior to the adoption of the enlarged access policy, a member was entitled to negotiate an arrangement for up to the equivalent of 100 percent of quota. At present, a member was also entitled to negotiate an arrangement for an amount of resources up to the cumulative limit under the enlarged access policy. In the period before the enlarged access policy, a member could negotiate an arrangement for the equivalent of 100 percent of quota, which would be financed entirely through the Fund's ordinary resources. The enlarged access policy did not entitle a member to use Fund resources equivalent to 100 percent of quota in one year and to request further Fund resources under the enlarged access policy in the following year.

The question naturally arose why the Fund typically kept access under an arrangement under the enlarged access policy to less than 50 percent of quota per year when the same member could conceivably use Fund resources equivalent to 100 percent of quota under another policy, the Chairman commented. The advantage of enlarged access was that it left open the expectation that the member concerned could make a second approach to the Fund as a result of which its cumulative access could exceed 100 percent of quota. That flexibility was an important characteristic of the enlarged access policy.

Mr. de Groote said that he wondered whether staff missions negotiating arrangements with members always clearly explained to the authorities the choice available to some of them of use of Fund resources under either the credit tranches or the enlarged access policy, the latter typically involving relatively reduced access in the first year with the possibility of use of resources in excess of 100 percent of quota over the life of an arrangement.

The Treasurer replied that the staff made members aware of the financing options available to them. Of course, no member was automatically entitled to receive 100 percent of quota under an arrangement; a member must have a balance of payments need for the financing requested and it must be willing to make an appropriate adjustment effort. Moreover, access to the Fund's resources could conceivably be limited by the Fund's liquidity position as well as the Fund's policies on access: the Fund might not have sufficient resources to make available the equivalent of 100 percent of quota to all members that had a genuine balance of payments need for that amount of financing. Under present policies and practices, a member whose position in the Fund was the equivalent of 100 percent of quota and which made a drawing for resources equivalent to less than 100 percent of quota would not receive financing under the enlarged access policy; all the financing would be covered by the Fund's ordinary resources. If the arrangement with that member was for an amount that would raise the relevant Fund holdings of its currency to a level in excess of 200 percent of quota, the resources provided would be a mix of ordinary and borrowed resources as prescribed under the enlarged access policy. The enlarged access policy applied to arrangements that would bring the relevant Fund holdings of the member's currency above 200 percent of quota.

Mr. de Groote considered that the expectation that the staff had described should be clearly spelled out during the negotiations with a member on an arrangement with the Fund. The arrangement would in effect reflect the staff's interpretation of the member's intention with respect to its policies in the period covered by the arrangement. The arrangement should explain what the authorities of the country expected to receive from the Fund at a later stage in the arrangement if they succeeded in implementing policies in the initial stage of the arrangement.

Mr. Joyce commented that it was particularly important for the staff to explain the various financing options to smaller members that might wish to use the Fund's resources and which might not be in a position to remain fully up to date on developments in policies and practices concerning the use of Fund resources. A Fund mission to a member country typically had a mandate to negotiate certain terms of an arrangement with the Fund. He wondered whether that mandate permitted the staff to present to the authorities concerned the various available financing options and to permit the member to choose among them. Conceivably the staff's mandate could require the staff to limit the negotiations to specific financing terms.

Mr. Grosche said that his understanding of the relationship between the use of the credit tranches and drawings under the enlarged access policy was consistent with the explanations by the Chairman and the staff. However, he wondered how the Fund would respond when a country that had originally expected to be able to solve its balance of payments problems with Fund assistance up to 100 percent of quota subsequently concluded that additional assistance was required to solve those problems and that it would wish to use the enlarged access policy in order to receive resources equivalent to more than 100 percent of quota.

Mr. Dallara stated that the perception that a member using the credit tranches could gain access to resources in excess of 100 percent of quota in a single year was a cause for concern. It was useful to recall that the average annual access in 1985 of 52 percent was some 10 percent above the average annual access in 1976-79.

Mr. Zecchini said that he wondered whether it was correct to assume that the main difference between a three-year stand-by arrangement under the regular access policy and a three-year arrangement under the enlarged access policy was that the latter provides larger amounts of financing. If so, and assuming that the yearly limit over three consecutive years under a regular stand-by arrangement was 33.3 percent of quota, it could be concluded that 33.3 percent was the indifference point between resorting to a regular stand-by arrangement or the enlarged access policy. That conclusion implied that the relevant range for phasing down the enlarged access policy had to consist of the span between its present limits and 33.3 percent of quota, below which the enlarged access policy was not an attractive substitute for the standard access policy. In addition, it would be useful to have an explanation of what financing accounts for the difference between the enlarged access policy's cumulative and triennial limits. Finally, he wondered whether the timing of the disbursement of Fund credit would be different without the triennial limits than if the limits were retained.

Mr. Sengupta suggested that it would be useful to have the staff circulate a short paper on the subject of access under the credit tranches and under the enlarged access policy. A separate discussion based on the paper might well be warranted. He wondered whether a member that had opted initially to use the enlarged access policy and to receive access up to 95 percent of quota in the first year of an arrangement with the Fund could subsequently request to receive assistance instead under the credit tranche policies after it had begun to use the enlarged access policy in support of that arrangement.

Mr. Suraisry stated that he supported Mr. Sengupta's request for a staff paper on the question of access under the credit tranches and the enlarged access policy. An important factor in a member's choice between using the credit policies or the enlarged access policy was the amount of time the member wished to have to repay the Fund; the enlarged access policy gave the member more time than the credit policies.

The Director of the Exchange and Trade Relations Department said that the staff had mentioned the use of the regular credit tranches in making its argument for providing the Fund with sufficient flexibility to respond to the needs of individual members; the staff had merely wished to mention a course of action that had been found useful in the period before the introduction of the enlarged access policy. The use of the four credit tranches in a single year had occurred on several occasions in the past, and, given the uncertainties about conditions in coming years, it seemed appropriate to continue to have the option to make resources available on that scale irrespective of funding considerations. In making that suggestion the staff had not meant to raise a legal issue. Staff missions did not discuss with governments the resources that would be available under one or the other policy because such an option did not arise. It was up to the Executive Board, on the basis of the decision on enlarged access policy, to decide whether use of such enlarged access was appropriate for any given country and its adjustment program. The staff's task was to describe the program for the Executive Board and to give its opinion on the program's feasibility. In recommending that a member should receive assistance under the regular credit tranche policies the staff assessed the country's program with a view to determining whether the necessary adjustment could be achieved during the program period so that the member would be unlikely to need Fund financing in addition to the ordinary resources to be made available under the arrangement in support of the program. The staff could provide a paper discussing access to Fund resources under the enlarged access policy and the credit tranche policies. For the time being, given the current overall economic and financial situation, it seemed useful to concentrate on the appropriate scale of Fund assistance, in general, rather than to try to examine a complicated set of rules on the use of particular policies.

Mr. Sengupta said that he continued to feel that a paper on the policies regarding the use of Fund resources would be helpful. That matter could be dealt with on another occasion.

The Deputy Managing Director noted that the decision on the mix of ordinary and borrowed resources (No. 7601-(84/3), 1/6/84) stipulated that any use of Fund resources under the enlarged access policy in excess of 100 percent of quota would be financed entirely by borrowed resources. Paragraph 1(a) stated that "under a stand-by arrangement, purchases will be made with ordinary and borrowed resources in the ratio of 2 to 1 in the first credit tranche, and 1 to 1 in the next three credit tranches. Thereafter, purchases will be made with borrowed resources only." The mixing ratio had subsequently been changed, but the requirement to use borrowed resources to finance drawings in excess of 100 percent of quota remained in effect.

The Chairman stated that the staff would prepare the paper that Mr. Sengupta had requested.

Mr. Polak said that he continued to doubt whether there was any need to maintain the triennial limit under the enlarged access policy. It could be understood that a member with a two-year or three-year arrangement with the Fund could receive up to two or three times, respectively, the annual access limit under those arrangements.

The Director of the Exchange and Trade Relations Department responded that the triennial limit was useful because it assured members with three-year arrangements that they would receive a specified amount of Fund financing over the life of the arrangement even if the enlarged access policy limits were phased down after the negotiation and approval of the arrangement.

The Chairman added that the triennial limit had been agreed in order to provide members with some assurance that three-year programs would be supported by the Fund under its enlarged access policy. The triennial limit in effect assured members that, although the enlarged access policy was temporary and would eventually have to be phased out, the Fund would provide support over a three-year period for sufficiently strong adjustment programs. That assurance had been helpful in dealing, for example, with Mexico and its commercial bank creditors. The triennial limit was strictly speaking not absolutely necessary, but it had been useful.

Mr. Zecchini remarked that he was worried that eliminating the triennial limit, on which explicit agreement had been reached in the past, might change the available options with respect to the Fund's financing of member countries' adjustment programs.

The Chairman said that he shared Mr. Zecchini's concern. The triennial limit clearly showed that the Fund was willing to consider three-year programs and to fix the amount of financing under those programs.

The Director of the Exchange and Trade Relations Department remarked that the triennial limit would be unnecessary if it were clearly understood--on the basis of the Chairman's summing up of the present discussion--that a member could be assured of access equivalent to three times the annual rate under the enlarged access policy over a three-year period.

Mr. Polak commented that the Fund typically worked on the basis of annual rates of access. There had been relatively few three-year arrangements, but any such arrangements could provide for access equivalent to three times the annual access limit. The Fund had already approved a number of arrangements covering periods of 12-24 months under which access was based on the annual limit.

The Director of the Legal Department noted that the elimination of the triennial limit would in effect be a substantive change, since the triennial limit was not precisely equivalent to three times the annual limit.

Mr. Dallara remarked that the difference between the triennial limit--280 percent of quota--and three times the annual limit--285 percent of quota--was small. He did not feel strongly one way or the other, but the possibility that eliminating the triennial limit could constitute a substantial change should be considered. His authorities had initially felt that the triennial limit could play a significant role in the evolution--and particularly the phasing out--of the enlarged access policy.

Mr. Joyce said that there seemed to be little to gain by eliminating the triennial limit. Outsiders might well be suspicious of the reasons for such a decision, which would have to be explained to the public.

The Chairman remarked that he too tended to feel that it would be best to retain the triennial limit.

Mr. Arias said that the comments by some Executive Directors in favor of reducing the access limits under the enlarged access policy were disappointing. In his view, a strong case in favor of that option did not exist. Indeed, as the majority of Executive Directors had stressed, the world economic situation was still uncertain, and a number of individual countries continued to have serious economic imbalances and sizable debt service burdens. Many of those countries had made successful adjustment efforts despite the relatively unfavorable global economic conditions. He agreed with Mr. de Groote that the adjustment process had been taking longer than had been expected and that the Fund must continue to provide adequate and realistic amounts of financial assistance. Any reduction in the access limits under the enlarged access policy at the present stage could be taken as a signal that the Fund was beginning to lessen its financial involvement in debtor countries, something that could tempt other official and private lenders to continue to reduce their involvement as well. Maintaining the present access limits in 1986 would enable the Fund to retain the flexibility it needed to maintain an appropriate balance between financing and adjustment.

The Chairman made the following summing up:

> From our discussion of today I have noted that 17 Executive Directors, who together hold some 58 percent of the voting power, preferred maintaining the present limits for enlarged access in 1986. Three Directors, who account for some 30 percent of the voting power, argued for a reduction in these limits in 1986 and, in that context, two of them mentioned a reduction in the annual limit from 95 to 85, and in the cumulative access limit from 408 to 350. Two Directors, who together hold some 11 percent of the voting power in the Fund, preferred a reduction in the cumulative access limit. With regard to the special facilities, all but two Directors would keep the access limits unchanged for 1986.
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> I shall now turn to the main topics of the discussion and make some personal concluding remarks.
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> Executive Directors considered that the Fund's present liquidity position is comfortable and does not in itself justify a reduction in access limits, although, of course, the liquidity position beyond 1986 cannot be assessed with full precision at this stage.

Directors clearly stated that the Fund's financial soundness is very important and must be preserved. In this connection two concerns must be dealt with, namely, the worrying increase in members' arrears to the Fund, and the prolonged use of Fund resources, especially by members that have not made sufficient adjustment. Management and staff are very sensitive to these concerns. I share the general view that these concerns can and must be dealt with by the Fund in the framework of the treatment of individual requests for Fund financial assistance rather than by reducing access limits.

The application of access limits in individual cases under the guidelines established by the Board has been very cautious. A number of Executive Directors feel indeed that this application has been too conservative and restrictive. Others feel that this cautious application was the right thing to do. I believe that the prudent application of the guidelines in individual cases--and no one disagreed with that description--should reassure those who put particular emphasis on the temporary nature of the enlarged access policy and on the revolving character of the Fund's resources. In my view, the effective application of the guidelines in individual cases is, in the present conditions, more important or relevant than the issue of the access limits. It is crucial to keep sufficient flexibility in the Fund's policies and to tailor access to the differing circumstances of individual cases. Access limits are not targets, as the actual implementation of the access policy has amply shown. But in some cases, in which a member's adjustment effort is particularly strong and its financing problems are substantial, the existence of sufficiently flexible upper access limits may be essential.

The main question today is whether present world financial conditions enable the Fund to reduce in 1986 the flexibility I have just stressed. I believe that the answer is no for several reasons. First, there are serious uncertainties regarding the outlook for the world economy. As many Directors said today the world economic outlook is not as favorable as it was last spring, let alone in September 1984, when the enlarged access limits for 1985 were established. The most recent projections include a marked deceleration in the volume of world trade and a rather marked trend toward lower commodity prices. The paper on access before the Board today is based on the spring 1985 World Economic Outlook exercise. At that time we were expecting the value of the exports of most of the developing debtor countries to increase 6.6 percent in 1985, compared with the September 1984 forecast of 10.4 percent. According to the latest forecast, the increase in exports in 1985 will be barely 0.5 percent, taking into account in particular that non-oil commodity prices are expected to fall by some 9 percent in 1985. As a result, the balance of payments difficulties of the indebted developing countries are likely to be more severe than had initially been estimated.

Second, there is still considerable uncertainty regarding the functioning of the financial system and the evolution of the international debt situation. The restoration of normal access to financial markets is a slow process, and some major borrowers as well as some medium-sized and smaller countries face financing gaps that will be difficult to cover even if strong adjustment measures are pursued. Given the extreme difficulty the Fund, the interested countries, the World Bank, and the commercial banks had in arranging financing packages for some countries in recent months, it is my impression that it will not be easy to meet the financing needs of some of the indebted countries in coming months.

Third, in the circumstances I have described it is crucial for the Fund to show its ability to cope with the problems at hand in a responsive and flexible way. It is very important at this juncture not to give the "wrong signal." The Fund must be seen as being willing and able to play its role in the adjustment and financing process. I am rather concerned that giving now even limited signals of retrenchment or of phasing out of the enlarged access policy might be interpreted as a backing away by the Fund and might make it all the more difficult for us to catalyze and mobilize the support of other financing sources. Perhaps even more important it might weaken our ability to influence the adjustment process itself; that is personally what I am particularly concerned about.

I wish to stress that the conclusion that no change should be made in the access limits in 1986 does not weaken the notion of the temporary nature of the enlarged access policy. Even a temporary facility must be seen to be able to respond to the needs of the moment.

The issue of the cumulative limits is a very sensitive one. In my view, the flexibility provided by those limits is essential. Some Directors said today that the present cumulative limits are high and that reducing the lower cumulative limit to 350 percent of quota would not have much of an impact. I would advise great caution here. If that access limit were to be reduced below, say, 400 percent of quota, we could face serious problems. In saying this I have in mind a list of countries--none of which are prolonged users--that are now in difficult positions and might need to receive access on the basis of the present cumulative limits. Some of these members have inactive programs, but I hope that they will be reactivated or that new ones can be agreed. If we were to provide these countries with arrangements, for, say, 18 or 24 months on the basis of the present annual access limits, these countries could be adversely affected by a lowering of the cumulative limits. As a result, we could be saddled in 1986 and 1987 with cumulative access limits that we would not really have thought through fully and that could hamper us. The paper before the Board today did not propose a reduction of the cumulative limit to 375. For the reasons I have indicated and in light of the present circumstances, I would strongly suggest maintaining the existing limits as they are. Maintaining those limits seems further justified by what many of you have rightly called the cautious application of the enlarged access policy.

APPROVED: May 21, 1986

LEO VAN HOUTVEN
Secretary