NOT FOR PUBLIC USE

MASTER FILES

ROOM C-120 04

INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 85/180

10:00 a.m., December 13, 1985

J. de Larosière, Chairman

Executive Directors	Alternate Executive Directors
	Mawakani Samba
C. H. Dallara	M. K. Bush
	G. Ercel, Temporary
B. de Maulde	S. de Forges
	T. Alhaimus
H. Fujino	M. Sugita
G. Grosche	B. Goos
Huang F.	Jiang H.
J. E. Ismael	Jaafar A.
A. Kafka	
	M. Foot
H. Lundstrom	
	G. D. Hodgson, Temporary
E. I. M. Mtei	
F. L. Nebbia	
Y. A. Nimatallah	
P. Pérez	
J. J. Polak	
	A. V. Romuáldez
G. Salehkhou	
	A. Vasudevan, Temporary
S. Zecchini	N. Coumbis

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

Also Present

Administration Department: H. Wiesner. Asian Department: W. G. L. Evers. Exchange and Trade Relations Department: J. Berengaut, S. Kanesa-Thasan. External Relations Department: J. E. McEuen. Legal Department: F. P. Gianviti, Director Designate; J. G. Evans, Jr., Deputy General Counsel; Ph. Lachman, A. O. Liuksila. Treasurer's Department: W. O. Habermeier, Counsellor and Treasurer; T. Leddy, Deputy Treasurer; D. Williams, Deputy Treasurer; J. E. Blalock, D. H. Brown, D. Gupta, R. B. Hicks, B. E. Keuppens, J. T. McDonald. Western Hemisphere Department: S. T. Beza, Associate Director; P. D. Brenner, L. A. Cardemil, J. Fajgenbaum, J. C. de Sosa, S. J. Stephens. Personal Assistant to the Managing Director: R. M. G. Brown. Advisors to Executive Directors: W.-R. Bengs, M. B. Chatah, L. P. Ebrill, S. Ganjarerndee, G. Nguyen, G. W. K. Pickering, A. Steinberg, E. M. Taha, D. C. Templeman, M. A. Weitz. Assistants to Executive Directors: H. Alaoui-Abdallaoui, A. Bertuch-Samuels, J. de la Herrân, R. Fox, N. Haque, L. Hubloue, O. Isleifsson, A. R. Ismael, Z. b. Ismail, S. King, H. Kobayashi, S. Kolb, M. Lundsager, A. Murakami, A. Mustafa, W. K. Parmena, M. Rasyid, J. E. Rodríguez, M. Sarenac, B. Tamami, L. Tornetta, A. J. Tregilgas, H. van der Burg, E. L. Walker.

1. INCOME POSITION FOR FINANCIAL YEAR 1986 - MIDYEAR REVIEW

The Executive Directors resumed from EBM/85/176 (12/6/85) their discussion of a staff paper on the midyear review of the Fund's income position for the financial year ending April 30, 1986 (EBS/85/258, 11/20/85).

Mr. Mtei recalled that the Executive Directors had been unable to agree on how to handle the projected deficit for FY 1986. His authorities were worried that failure to reach agreement by December 15, 1985 would result in an increase in the rate of charge on the Fund's ordinary resources to 7.87 percent with effect from November 1, 1985. The deficit in the Fund's income in the current financial year was due mainly to the Executive Board's decision to treat overdue obligations to the Fund as deferred income. Accordingly, the Executive Board should review the income target for FY 1986 and consider the possibility of temporarily reducing the Fund's reserves, which could be replenished when the overdue obligations were settled. The staff and a number of members with arrears were holding discussions that should result in the settlement of some of the arrears in the coming several months.

The additional burden of an increase in the rate of charge on all users of the Fund's resources--including debtors that had struggled to remain current in the Fund--could increase the number of members with arrears, thereby increasing the Fund's income shortage, Mr. Mtei said. The additional burden would certainly worsen the position of members that had been forced into arrears by circumstances beyond their control. The Fund was in a better position than debtor countries to cushion a temporary shortfall in the Fund's income by either reducing the income target for FY 1986 or temporarily forgoing the opportunity to build up the Fund's reserves.

It would be unfair if the arrears of a few members were to increase the burden on the poor debtor members that were meeting their obligations to the Fund, Mr. Mtei remarked. Dealing with the Fund's income shortfall solely by increasing the rate of charge would make the poorest debtor countries entirely responsible for responding to a problem that was caused by the few members with arrears. The consequences of the arrears should be borne by the entire membership, which had approved the drawings that had been made by members that had subsequently fallen into arrears. The decision on the Fund's income position should be equitable. He hoped that such a decision could be taken at the present meeting, thereby avoiding a solution that would place a disproportionate burden on debtor countries, including those that remained current in the Fund.

Mr. Ismael recalled that during the previous discussion on the midyear review of the Fund's income position his chair had supported retaining the present net income target, increasing the rate of charge to equal the SDR interest rate, and reducing the remuneration coefficient to 89.3 percent with effect from November 1, 1985. That solution remained his first preference, but he could support any solution under which the burden of meeting the income target would be shared equitably. He could support an increase in the rate of charge to no more than the SDR interest rate, together with a reduction in the remuneration coefficient and a somewhat lower net income target; that combination of actions would constitute a reasonable compromise.

Mr. Kafka said that his position was similar to that of Mr. Ismael. The combination of actions that Mr. Ismael had suggested would be the most equitable solution.

Mr. Polak recalled that at the previous discussion he had made a somewhat different proposal from Mr. Isamel's. However, the burden sharing under Mr. Ismael's proposal was acceptable.

Mr. Dallara considered that the most appropriate action was to use the safeguard provision of Rule I-6(4)(b), under which the rate of charge would be increased to 7.87 percent. The need for that solution was regrettable, but it was important to maintain the current income target for FY 1986, and increasing the rate of charge to 7.87 percent would be consistent with the wish to share the burden of responding to the projected deficit in the Fund's income in FY 1986. Mr. Mtei's comments on the likely settlement of some of the larger arrears in the near future were encouraging. The Executive Board planned to review two major arrears cases in the coming weeks as a part of the effort to mobilize financial support for those countries' comprehensive economic adjustment programs, the implementation of which should enable the members concerned to eliminate their arrears to the Fund. Any excess net income in FY 1986 could be distributed retroactively in order to reduce the effective rate of charge from 7.87 percent to 7.0 percent, provided that the present income target could be met and that any extra amount after the retroactive distribution would be placed in the Fund's reserves.

Mr. Foot stated that his position remained unchanged. He hoped that all or part of the increase in the rate of charge to 7.87 percent could be reversed at a later state. He supported Mr. Dallara's position on the retroactive distribution of any excess net income in FY 1986. It was important to stress the role that creditor countries were playing in the effort to reduce members' arrears.

Mr. Fujino said that his position also was unchanged. He hoped that the issue of arrears would be resolved quickly, and he supported the proposal to make a retroactive distribution of excess net income to members affected by the decision to increase the rate of charge to 7.87 percent.

Mr. Mawakani remarked that while he was concerned about the projected income shortfall for financial year 1986, he did not feel that it was a permanent problem necessitating the taking of specific action, such as an increase in the rate of charge, at the present stage. The most important factor behind the projected shortfall was the amount placed to deferred income because of overdue obligations. On several occasions his chair had expressed its concern about the overdue obligations and their financial implications for the Fund. He, too, was committed to the financial soundness of the Fund. However, as his chair had recently noted, only a few countries facing severe financial and economic problems were behind in their repurchases. The authorities in those countries had expressed their concern about that problem and had indicated their willingness to become current in their obligations to the Fund. The present income deficit was therefore temporary in nature.

The Executive Board had taken up the problem of overdue obligations and had taken steps to improve the financial position of the Fund, Mr. Mawakani noted. Furthermore, at a time when the Fund was asking for increased participation by private creditors, it was inappropriate for it to take measures that would send conflicting signals to the financial markets. The overdue obligations to the Fund should be treated as temporary and should not lead the Fund to take actions such as changes in rates which would introduce an element of uncertainty in to its dealings with members. The Fund should not take steps that would increase the burden on members that were already facing balance of payments problems. Furthermore, at a time when interest rates were falling everywhere, the Fund's rate of charge should not be increased.

Given all those factors, the income shortfall could be eliminated by a downward revision of the income target and by using the ample reserves that the Fund had accumulated, Mr. Mawakani considered. Those reserves could be replaced later, when the overdue obligations were discharged.

Mr. Nebbia said that he accepted Mr. Mtei's proposal.

Mr. Vasudevan remarked that his chair continued to prefer the proposal in paragraph (iv) on page 17. He wondered whether Executive Directors who had said that they could accept a rate of charge equal to the SDR interest rate meant that over the rest of FY 1986 the rate of charge should move in line with the SDR interest rate; alternatively there could be a cap on the rate of charge.

Mr. Ismael said that he preferred to see the rate of charge fluctuate in line with fluctuations in the SDR interest rate.

Mr. Hodgson stated that the position of his chair had remained unchanged. That position was close to the compromise that Mr. Ismael had proposed at the present meeting. He was prepared to support any reasonable compromise under which the burden of responding to the Fund's projected income deficit would be shared among all members. He hoped that Executive Directors who favored a solution based solely on an increase in the rate of charge would remain open minded and would be prepared to consider alternative courses of action if, as he hoped, a further review of the Fund's income position would be held in three months.

Mr. Lundstrom commented that he continued to prefer the combination of actions suggested by the staff--namely, increasing the rate of charge to make it equal to the SDR interest rate and temporarily reducing the remuneration coefficient to 89.3 percent. He could go along with a broadly supported proposal for a more limited, temporary reduction in the remuneration coefficient to, for example, the basic level of 91.66 percent, in which event the rate of charge would have to be set at a level that would ensure that the reserve target for FY 1986 would be met.

The Treasurer remarked that under Mr. Lundstrom's proposal, 75 percent of the burden of covering the shortfall of the Fund's net income would be borne by debtor countries and 25 percent by creditor members.

Mr. Grosche said that the steep increase in the rate of charge needed at the present stage was regrettable. He had hoped that the rate of charge would not have to be increased above the SDR interest rate. He had been prepared to have the Fund assume some of the burden of covering the projected net income shortfall in the hope that some of the arrears to the Fund would be settled in coming weeks, thereby enabling the Fund to build up its reserves and eventually meet the 5 percent income target. He might even have been prepared to suspend temporarily that part of Rule I-10(b)(i) whereby the remuneration coefficient moved inversely with the level of the SDR interest rate, along the line of Mr. Lundstrom's latest proposal, with the effect of temporarily freezing the rate of remuneration at 91.66 percent of the SDR rate. However, the position that had been taken at the present meeting by Mr. Foot, Mr. Dallara, and Mr. Sugita was understandable. There was considerable uncertainty about likely developments in the Fund's income position in coming months; there was no certainty that the members with large arrears would become current in the Fund in the near future. Indeed, the arrears problem could worsen before it improved. Accordingly, the Fund had to take action on the income side by increasing the rate of charge. It would be appropriate during the next discussions on the Fund's income position to consider how the increase in the rate of charge with effect from November 1, 1985 could be cushioned by actions in other areas.

Mr. Nimatallah commented that he continued to have an open mind and was prepared to accept any reasonable solution.

Mr. Vasudevan inquired what rate of charge would be required to enable the Fund to meet the current income target if the remuneration coefficient were reduced to 91.66 percent and the SDR interest rate for the rest of FY 1986 were assumed to be 7.6 percent. He also asked what the rate of charge would be if there should be no surplus or deficit in net income.

The Deputy Treasurer replied that the rate of charge would have to be 7.87 percent.

Mr. Lundstrom said that he had suggested that the remuneration coefficient should be 91.66 percent because that was the coefficient as of May 1, 1985, and it was the base coefficient for FY 1986. Maintaining that coefficient through the rest of FY 1986 would require creditors to forgo temporarily the scheduled automatic increase in the coefficient.

Mr. Zecchini stated that his position had remained unchanged. He hoped that Executive Directors would keep an open mind on the reserve target for FY 1986 and would reconsider the advisability of maintaining the current target through the whole year. The target could be reduced and the effects of the reduction could be offset through the establishment of a loan-loss provision which could be financed by contributions from all member countries. His authorities attached considerable importance to the possibility of establishing a special fund, financed by voluntary contributions, to support the implementation of strong adjustment programs by members with arrears.

Mr. de Maulde said that he was prepared to accept a reasonable compromise.

Mr. Pêrez remarked that, while his position was unchanged, he was prepared to go along with any reasonable compromise under which the burden of the net income shortfall would be shared by the whole membership.

The Chairman said that it would be useful to have the staff comment on the feasibility of reducing the reserve target while establishing a loan-loss provision that would be financed on the basis of some kind of burden-sharing mechanism.

The Treasurer remarked that he wondered whether the Executive Board was at present in a position to judge whether a loan-loss provision should be established. The staff had not yet had time to reach a conclusion on the appropriateness of such a provision. The Executive Board would have to decide not only whether or not to introduce a loan-loss provision but also how to fund it. One of the proposals for such funding was to reduce the reserve target by the extent necessary. A loan-loss provision could conceivably be handled as a special reserve that would be used to cover special losses. In an accounting sense, care would be needed to avoid closely associating the general reserves with any loan-loss provision, each of which would have its own separate identity.

Mr. Dallara said that he shared Mr. Zecchini's interest in the establishment of a loan-loss provision. However, the staff and the Executive Board were not yet in a position to reach a judgment on the need for such a provision, which should be discussed in detail on another occasion in the near future.

Mr. Vasudevan remarked that as he understood it, under Mr. Lundstrom's proposal the remuneration coefficient would be reduced to 91.66 percent and the rate of charge would be increased to 7.8 percent, in which event the rate of charge would exceed the SDR interest rate and the Executive

Board would therefore be required to conduct a separate review of the remuneration coefficient. At the same time, any rate of charge equal to or exceeding the SDR interest rate would no longer be concessional; indeed, a rate of 7.8 would have a negative concessional element. During previous discussions on the rate of charge Executive Directors had consistently underscored the importance of the rate's concessionality, which helped to encourage members to approach the Fund early in the development of their balance of payments problems. An increase in the rate of charge to 7.87 percent under the safeguard provision, or any larger increase, would be one of the steepest increases in the rate of charge in recent years. Such an increase would place a substantial burden on users of the Fund's resources. The staff should comment on the SDR interest rate that it had projected for the rest of FY 1986.

The Treasurer said that for the purposes of the projections in EBS/85/258, the SDR interest rate for the rest of FY 1986 was assumed to be 7.6 percent, the rate that had prevailed at the time the staff had made its projections. Of course, the SDR interest rate was adjusted on a weekly basis, and the latest rate was slightly higher than 7.6 percent. The actual SDR interest rate for the rest of FY 1986 was likely to be somewhat different from 7.6 percent. The staff assumed that if on average the SDR interest rate were to exceed 7.6 percent, the rate of charge would be increased by a corresponding amount under Mr. Ismael's proposal while the rate of charge would remain fixed under Mr. Lundstrom's proposal. If the rate of charge were to exceed the SDR interest rate at any time, the Executive Board would be required to review the remuneration coefficient. The rate of charge would exceed the SDR interest rate at the outset under Mr. Lundstrom's proposal, thereby necessitating a review. In effect, the present discussion was a part of that review.

The Deputy Treasurer explained that if the remuneration coefficient were reduced to 91.66 percent and the SDR interest rate were kept at 7.6 percent, the rate of charge needed for a break-even income position would be approximately 7.3 percent. There had been a number of fairly large increases in the rate of charge in the past. For example, between 1970 and 1971 the rate had been increased from 3.3 percent to 3.7 percent; between 1976 and 1977 the rate had been increased by 75 basis points; between 1980 and 1982 the rate had been increased from 5.3 percent to 6.25 percent, and had then fallen somewhat before rising to 7 percent. Those changes in the rate of charge had been in line with fluctuations in market interest rates.

Mr. Grosche said that he attached considerable importance to the element of concessionality in the Fund's rate of charge. The new rate of charge of 7.87 percent would exceed the SDR interest rate but would still contain a sizable element of concessionality, as it would be below the market rate that users of Fund resources would have to pay for loans of the same maturity as Fund credit.

The Deputy General Counsel commented that Rule I-10(d) would not be violated by an increase in the rate of charge above the SDR interest rate. Under that rule, the Executive Board was required to review the remuneration coefficient when the rate of charge should exceed the SDR interest rate. If the Executive Board did not take a decision at the present meeting and the safeguard clause under Rule I-6(4)(b) were invoked, the rate of charge would rise above the SDR interest rate, requiring the Executive Board to review the remuneration coefficient. An increase in the rate of charge above the SDR interest rate was obviously a possible outcome of the present review of the Fund's income position. Therefore, the present review of the income position inherently had to include a review of the remuneration coefficient.

Mr. Vasudevan said that the degree of concessionality in the rate of charge depended upon the interest rates to which the rate of charge was compared. It had often and broadly been assumed by the Executive Directors that the SDR interest rate was a representative rate. There were of course many different market interest rates to which the Fund's rate of charge could be compared. However, a comparison with interest rates on loans for periods comparable to the period in which the Fund's general resources were typically available to members suggested that a rate of charge of 7.8 percent or 7.87 percent clearly would not be concessional. Indeed, assuming that the SDR interest rate was 7.6 percent, a rate of charge of 7.87 percent would have a negative grant element of 0.95 percent. A rate of charge in excess of the SDR interest rate would be inappropriate. The staff proposed increasing the rate of charge from 7.0 percent to 7.87 percent. As he understood it, there had been only one comparably large increase in the rate of charge since 1970.

The Deputy Treasurer remarked that it was true that on the basis of short-term interest rates, the grant element of the rate of charge was slightly negative. However, short-term interest rates had never been the standard by which the concessionality of the rate of charge had been judged. In its paper on burden sharing (EBS/85/126, 5/14/85) the staff had used the combined SDR five-year interest rate in measuring the grant element of the rate of charge. On that basis, a rate of charge of 7.87 percent would have a grant element of nearly 3 percentage points. The grant element would be larger on the basis of open market rates. Given the medium-term borrowing rate for developing countries in the open market, a rate of charge of 7.87 percent would have a grant element of almost 5 percentage points. That calculation was based on the average rate for floating rate issues in London over the first half of 1985 for a large range of countries with varying degrees of creditworthiness; that rate was a reasonably good indicator of market rates for medium-term borrowing at the present stage.

Mr. Polak said that he agreed that if, as Mr. Lundstrom had proposed, the Executive Board should decide at the present meeting on a rate of charge in excess of the SDR interest rate, the present discussion could be seen as the review of the remuneration coefficient required when the rate of charge exceeded the SDR interest rate. However, he doubted whether the present discussion could be seen as constituting the required review of the remuneration coefficient if the Executive Board were simply to fail to adopt a decision, thereby bringing into play the safeguard provision under which the rate of charge would automatically increase to a rate that would exceed the SDR interest rates.

The Deputy General Counsel commented that he agreed with Mr. Polak that the two situations that Mr. Polak had described were different. However, the fact that not taking a decision at the present meeting would lead to an increase in the rate of charge that would bring that rate well above the SDR interest rate with effect from November 1, 1985 was one of the considerations that had been examined in the staff paper that was now before the Executive Board. The staff paper discussed various possible actions concerning the remuneration coefficient and the rate of charge. Hence, the material prepared by the staff for the present review of the Fund's income position was designed for a review under Rule 10(b) and the present review could be seen to have inherent in it the review of the remuneration coefficient that was required when the rate of charge exceeded the SDR interest rate. The Executive Board could of course agree to hold another separate review of the remuneration coefficient.

Mr. Polak considered that if the Executive Board did not take a decision on the course of action that should be taken by December 15, thereby resulting in an automatic increase in the rate of charge above the SDR interest rate in accordance with Rule I-6(4)(b), the Executive Board should conduct a separate review of the remuneration coefficient.

The Chairman said that he agreed with Mr. Polak. The staff could prepare a separate paper for discussion by the Executive Board.

Mr. Kafka remarked that Rule I-10(d) seemed to require the Executive Board to hold a separate review as long as the SDR interest rate was lower than the rate of charge.

The Deputy General Counsel said that under Rule I-10, if both the SDR interest rate and the rate of charge were fluctuating, a review would be precipitated each time that the rates crossed and the rate of charge exceeded the SDR interest rate. However, the continuation of a rate of charge in excess of the SDR interest rate would not precipitate a continuous review of the remuneration coefficient. The rate of charge and the rate of remuneration were reviewed periodically in any event; in the interim, a separate review was to be held when the rate of charge should exceed the SDR interest rate--namely when it moved above the SDR interest rate.

Mr. Kafka remarked that Rule I-10 stipulated that the Executive Board was to review the rate of remuneration when the rate of charge exceeded the SDR interest rate. It did not say that the rate of charge should continuously exceed the SDR interest rate or that the rate of charge should come to exceed the SDR interest rate as the result of a fluctuation in the SDR interest rate. Under Rule I-10, the review of the remuneration coefficient was to be held whenever the rate of charge was in excess of the SDR interest rate. The Executive Board should continuously review the remuneration coefficient as long as the rate of charge exceeded the SDR interest rate. If necessary, the question of the interpretation of Rule I-10 could be taken up by the Committee for Interpretation.

Mr. de Maulde said that the issue that Mr. Kafka had raised might be usefully considered by the Committee for Interpretation.

The Treasurer remarked that in interpreting paragraph (d) of Rule I-10 it was useful to bear in mind all the provisions of that rule. Rule I-10 referred to the meeting of the target amount of net income, a variable that did not necessarily change during any review of the rate of charge or the remuneration coefficient.

Mr. Vasudevan said that the Treasurer had made a telling point. It was important to consider the entire text of paragraph (d) of Rule I-10. Part of the text said that the objective was to keep the rate of charge from exceeding the SDR interest rate while still meeting the net income target for a financial year. In the situation dealt with by paragraph (d) the only way to meet the income target while keeping the rate of charge from exceeding the SDR interest rate was to adjust the remuneration coefficient.

The Deputy General Counsel remarked that the review under paragraph (d) was to consider an adjustment of the remuneration coefficient and specifically whether that coefficient could be set at a level within 80 percent of the SDR rate that would still permit the rate of charge to be set at a level at which the Fund could meet its income target for the financial year. That factual situation was unlikely to change in the short run, and a single review of the remuneration coefficient--rather than a continuous review--was sufficient and consistent with the text that called for a review "of the rate of charge...should exceed the SDR interest rate."

The Chairman said that there did not seem to be a 70 percent majority in favor of adopting a decision to deal with the income position. Accordingly, under Rule I-6(4)(b), the Executive Board would hold a separate review of the remuneration coefficient. The staff would prepare a paper for that discussion.

Mr. Vasudevan stated that the outcome of the present discussion as summarized by the Chairman was regrettable. The Executive Board was being forced by a mere procedure to take a one-sided action--raising the rate of charge without adjusting any of the other possible variables--in order to meet the net income target for FY 1986. Moreover, that one-sided action would place the entire substantial burden of meeting the income target on one group of members, including countries that remained current in their obligations to the Fund. If the remuneration coefficient were reduced under the review required by the provisions of Rule I-6(4)(b), he wondered whether the reduction could be made retroactive. Could the increase in the rate of charge effective November 1, 1985 be reduced retroactively as a result of the review of the remuneration coefficient required under Rule I-10(b)?

The Deputy General Counsel said that the review under Rule I-10(b) was meant to consider the rate of charge as well as the remuneration coefficient. The objective of the review was to ascertain whether the remuneration coefficient could be set at a level that would permit the rate of charge to be reduced to the level of the SDR interest rate while still enabling the Fund to meet its net income target for the financial year. Under Rule I-6(4), the Executive Board could decide to decrease the rate of charge retroactively. The Fund could not take decisions that retroactively increased a burden on members, but it had taken decisions that retroactively gave members a benefit. One such decision that the Fund could take was to decrease the rate of charge retroactively at the end of a financial year under Rule I-6(4).

Mr. Polak stated that the review of the remuneration coefficient should be a full one, and the staff should be given sufficient time to prepare the relevant paper, which should contain a detailed discussion of the requirements of, and intentions behind, Rule I-10. Some Executive Directors had suggested that the Fund's income position could usefully be reviewed again in three months. In any event, in coming weeks there might well be relevant developments in the arrears situation. The review of the remuneration coefficient could take place in the first half of February 1986.

Mr. Vasudevan inquired what steps might have to be taken if the Executive Board did not have the necessary majority to take a decision at the conclusion of its review of the remuneration coefficient.

The Chairman said that the review could be completed with or without a decision to reduce the remuneration coefficient.

Mr. Pérez remarked that an increase in the rate of charge to cope with the shortfall in the Fund's income position would place a substantial burden on the users of the Fund's resources. Moreover, such a solution was, in principle, inconsistent with the spirit of cooperation that should guide the workings of the Fund and with the Fund's role in solving the debt problem. Placing the responsibility for dealing with the Fund's income shortfall exclusively on the users of Fund resources—most of which were debtor countries--was clearly inconsistent with the recent steps that had been taken in recognition of the seriousness and persistence of the debt problem.

The problems that had caused the income shortfall would not be ameliorated by increasing the rate of charge, Mr. Pérez commented. Indeed, the problem of overdue financial obligations to the Fund was bound to worsen before it began to improve. The Fund should devise formulas that would equitably distribute the burden of handling income shortfalls among the whole membership. To that end, the staff should prepare a paper examining optional courses of action in connection with the coming review of the remuneration coefficient.

Mr. Foot said that he agreed wih Mr. Polak that the staff should be given sufficient time to prepare the paper for review of the remuneration coefficient. It was important to remember that the procedures under Rule I-6(4)(b) had been adopted in order to avoid the chaotic situation that would arise if the Executive Board were unable to reach a decision on the best way to handle an income shortfall. Alternatives to the present procedures were worth considering in detail, but any new procedures would have to be fully adhered to; they should not be set aside when the Fund faced income problems and had to take difficult steps to deal with them.

Mr. Salehkhou remarked that he too agreed with Mr. Polak that the staff paper for the review of the remuneration coefficient should be carefully prepared. He hoped that the review could be held no later than the second half of January 1986.

As a result of the present discussion, the burden of dealing with the Fund's income shortage in FY 1986 would fall entirely on the rate of charge, Mr. Salehkhou noted. It was essential to agree at the present meeting that any excess income would be used first to reduce the rate of charge retroactively to 7 percent.

Mr. Vasudevan stated that he too believed that any excess income should be used first to reduce retroactively the rate of charge for members that had had to pay a higher rate.

The Chairman said that he wondered whether any retroactive reduction in the rate of charge should be applied to all the affected members or only to members that had remained current in their obligations to the Fund.

The Deputy General Counsel commented that the rate of charge was to be uniform for all members. Accordingly, any retroactive reduction in the rate of charge would have to be applied uniformly to all members.

The Treasurer said that he wondered whether the present stage was the appropriate one at which to decide on a distribution of any surplus net income in the form of a retroactive reduction in the rate of charge. The question whether members in arrears to the Fund should benefit from such a retroactive redistribution should be carefully considered. After all, a net income surplus could conceivably arise for reasons other than or in addition to the settlement of overdue financial obligations to the Fund. Moreover, one rate of charge--the special rate that the Executive Board might decide to apply to members with arrears--obviously did not have to be applied to all members. For example, that special rate might have to be high enough so that any distribution of a net income surplus to reduce retroactively the rate of charge on the Fund's regular resources would not reduce the special rate of charge for members with arrears. Refunding could also mean making a payment to members that were in arrears, and that raised a question if not an issue of principle.

Mr. Dallara said that the need to increase the rate of charge was regrettable. However, it was necessary to protect the Fund's financial position. There were legitimate differences of opinion about the issue of sharing the burden of responding to a shortage in the Fund's income. As the operational budgets and designation plans in the recent year showed, certain countries had taken on a major portion of the burden of supporting the Fund's financial position. His authorities' position on the issues at hand had been influenced by the lack of broad concern within the Executive Board about recent individual cases of arrears, and he hoped that the serious concern about the arrears which had been expressed during the present discussion would be translated into concrete action by debtors and creditors. In that connection, Mr. Mtei's comment that the arrears problem was due to certain circumstances beyond the control of the members concerned was somewhat worrying. He hoped that Mr. Mtei had not meant that the members of his constituency that had overdue obligations to the Fund felt that they were unable to take steps to eliminate their arrears. After all, in the final analysis, while the solution to the arrears problem facing a number of countries might not be entirely within their control, the basic prospects for solving those problems could only be improved by actions taken by the members themselves. There was an urgent need for debtors and creditors to act to solve the arrears problems so that any excess net Fund income could be distributed to reduce the rate of charge retroactively.

The Chairman remarked that there was not the 70 percent majority required to take a decision at the present meeting. Executive Directors agreed that the fact that the rate of charge would exceed the SDR interest rate meant that the Executive Board must hold a review of the remuneration coefficient under Rule I-10. While that issue had been raised by the staff paper for discussion, to err on the side of caution, another review should be held separately, on another occasion. The preparation for that separate review should not be hasty; the relevant staff paper should be as substantive as possible and should reflect suggestions that had been made by Executive Directors. In addition, Mr. Foot had suggested that it might be useful to review the Fund's income position again within the coming several months.

Mr. Foot commented that the next review of the Fund's income position that he had suggested could be a part of the next quarterly report on overdue financial obligations to the Fund. That report could contain a brief statement as to whether or not the arrears situation and the outlook for the Fund's income position in FY 1986 had changed significantly.

The Treasurer remarked that as he understood it, the assessment of the Fund's income position that Mr. Foot had mentioned need not require another full-fledged staff paper like the papers prepared for a six-monthly review of the Fund's income position.

The Chairman said that he agreed with the Treasurer. The staff should merely bring the Executive Board up to date on the arrears situation, which would of course have an important impact on the Fund's income position. The Executive Directors seemed to agree in principle that the surplus net income by the end of FY 1986 should be used to reduce the rate of charge retroactively. The detailed aspects of a distribution--such as the part of FY 1986 that would be covered and the extent to which the rate of change would be reduced--would be decided later, when the surplus income was actually at hand.

It had also been suggested that the staff should be asked to examine alternatives to the present procedures for dealing with income shortages, the Chairman remarked. The objective would be to consider alternatives that would avoid the kind of outcome of the present discussion, on the basis of which one of the important variables--the rate of charge--was to be increased automatically under the present rules of the Fund. The staff should review the procedures, including the safeguard provision, to see whether some other formula could be devised. Executive Directors representing more than half of the voting power had mentioned the burden-sharing issue.

Mr. Polak commented that the present complicated Executive Board decisions governing the determination of the rates of charge and remuneration had been agreed after extensive and difficult discussions. However, circumstances had changed since the adoption of those decisions. For example, the Executive Board was more inclined to accept freely floating rates; the rate of remuneration was already floating, and the Board might be amenable to a floating rate of charge. Still, he doubted whether the staff would be able to propose a fundamentally different system from the present one. The staff might be able to propose a useful, fundamentally similar system.

The Chairman remarked that the problem of burden sharing would have to be faced, and the present system reviewed so as to consider possible alternatives. That matter should be the subject of a separate Executive Board discussion. The issue of a possible loan-loss provision should be discussed by the Executive Board before the end of the current financial year. Meanwhile, because there was not a 70 percent majority of the total voting power needed to take a decision on a different rate of charge at the present review, the rate of charge would be adjusted in accordance with the provisions of Rule I-6(4)(b) to 7.87 percent with effect on November 1, 1985.

2. VENEZUELA - 1985 ARTICLE IV CONSULTATION

The Executive Directors considered the staff report for the 1985 Article IV consultation with Venezuela (SM/85/308, 11/15/85), the second report prepared under the procedures for enhanced surveillance proposed by the Venezuelan authorities. They also had before them a report on recent economic developments in Venezuela (SM/85/316, 12/2/85).

Mr. Pérez made the following statement:

During the past two years Venezuela has overcome most of its internal and external economic disequilibria thus paving the way for a new phase of economic recovery compatible with servicing its external debt. This, of course, subject to the uncertainties surrounding the international oil market.

As a result of the adjustment program designed and implemented by the Administration that took office in February 1984 the financial situation of the public sector has improved substantially--a surplus of 7.6 percent of GDP was recorded in 1984, compared with a deficit of 12.3 percent two years earlier--while a dramatic turnaround in Venezuela's external position was achieved. The current account shifted from a deficit of $4.2 billion in 1982 to a surplus of $5.2 billion in 1984. Even more remarkable is the evolution of the overall balance of payments which, from a $7.9 billion deficit in 1982, turned into a surplus of $2.1 billion in 1984. In addition, inflation was held within manageable bounds. Notwithstanding the pressures exerted by the sharp devaluation of the bolívar, and the use of production incentives in the form of producer price increases, the consumer price index rose by an average of only 12.2 percent in 1984.

These gains were attained through a tightening of demand and the adoption of policies aimed at promoting structural changes. The tightening of demand was achieved mainly through a drastic cut in public expenditures and a stringent monetary stance. In addition, the Government took measures to adjust the most important relative prices and the cost/price structure of the economy, contributing, in turn, to reduced aggregate demand. These measures included a marked devaluation of the bolívar; the elimination of exchange and tax subsidies; a freeze on wages and salaries of public sector employees; a rise in prices with the specific aim of encouraging certain productive activities; and sectoral policies designed to stimulate internal production mainly in those sectors producing tradable goods. All these actions were framed and developed in the context of a social pact that has been a key element in the adjustment process.

The achievements, however, have entailed high costs, as witnessed by real GDP declines of 5.6 percent in 1983 and 1.4 percent in 1984. Meanwhile, unemployment rose from 7.1 percent of the labor force in 1982 to 13.4 percent in 1984.

The Government's main objectives for 1985 were the achievement of positive real economic growth and the reversal of the unemployment trend, but without jeopardizing the gains already obtained. In this regard, the Quantified Economic Program set as policy goals for 1985 the attainment of a moderate rate of growth in real non-oil GDP; a reduction of the unemployment rate; a decrease in the inflation rate; and the maintenance of a current account surplus. In order to meet these goals, the Government was to implement cautious fiscal and monetary policies, while enforcing the set of measures aimed at structural changes.

In the fiscal area, the Government's intention was to attain equilibrium in the consolidated public sector, giving the economy a moderate boost through an increase in public investment.

In the monetary field, the Central Bank of Venezuela established a ceiling of 18.4 percent growth for the monetary aggregate M-2, thus setting a less stringent monetary stance than in 1984, but maintaining it basically compatible with a deceleration of the inflation rate.

As for the cost/price structure of the economy, two main actions should be mentioned. In the exchange rate area, the monetary authorities adopted a timetable for the unification of all official exchange rates by December 1985. Also, the authorities sought to maintain domestic interest rates at positive levels in real terms.

In my buff on Venezuela circulated on May 30, 1985, I listed the following main economic performance trends observed during the first part of the year: A sharp deceleration of inflation; an external current account surplus higher than forecast; a public sector surplus higher than budgeted; and monetary aggregates growing well below the ceilings. Events in the last few months have confirmed these trends. Latest estimates point to the following outcome for the year as a whole, compared with those targeted in the Quantified Economic Program:

	1985	
	Quantified Ecconomic Program	Last Estimate
Non-oil GDP in real terms (percent)	2-3	0.5
Consolidated public sector--surplus as percent of GDP	0	2.7
External current account--surplus in millions of U.S. dollars	1,700	3,700
Net international reserves--millions of U.S. dollars	11,867	14,800
M-2--percentage change below	18.3	10
Consumer Price Index--percentage change Dec. to Dec. below	13	7

Source: Central Bank of Venezuela

According to the latest available indicators, the economy has continuously performed below expectations, although economic recovery now shows evidence of consolidation in certain sectors, namely, agriculture and a growing number of manufacturing industries. Nevertheless, construction--one of the fastest growing sectors during the demand surge of the last decade, and responsible for the generation of a large part of total employment--has persistently declined since the early 1980s.

In the fiscal area, the Government may end this year with a new consolidated public sector surplus of approximately 2.7 percent of GDP. This surplus would result from a level of total revenues similar to the target and from a lower level of public expenditure. On the revenue side, the decline in petroleum earnings has been compensated by the improvement in customs duties and income tax collections. Other contributing factors were a tax increase on liquor and cigarettes, as well as an increase in stamp duties. In addition, the improvement in management procedures in State agencies and enterprises has contributed to increase the operating surplus of the nonfinancial public sector. On the expenditure side, the lower level of outlays associated with the servicing of the public debt as well as delays in the implementation of public investment programs are the main factors contributing to the recording of a lower than budgeted level.

The balance of payments will again show a surplus estimated at over $500 million, leading to a new increase in external reserves. This is accounted for by a current account surplus which may exceed $3.7 billion, reflecting lower than expected imports and interest payments. These factors, together with an increase in nontraditional exports of 32.6 percent, have more than offset the decline in revenues of Petróleos de Venezuela (PDVSA) on account of the weakness of the oil market during the year. It should be stressed that nontraditional exports would have performed even better in a less protectionist environment. In fact, limits on steel exports to the United States will determine a reduction in this category for 1986.

In the exchange rate area, as mentioned above, exchange subsidies have been gradually phased out, and progress continues toward the goal of achieving a single official exchange rate by the end of 1985. Since the last visit of the Fund staff, the number of agricultural products in the Bs 4.30 per dollar list was reduced to two--milk and wheat. These products, as well as the exchange rate of Bs 6.00 per dollar set for oil, will be moved to the 7.5 exchange rate category at the end of the year. These movements in the exchange rate, together with the decline in the U.S. dollar and the depreciation registered by the bolívar vis-à-vis the dollar in the free market during the last few months, will probably correct most of the appreciation of the bolívar referred to in the staff report.

Money supply growth during 1985 will probably be positive in real terms, although substantially less than expected. The seasonal factors for higher liquidity in the closing months of the year may lead to a nominal annual growth of this aggregate of about 10 percent. The recovery observed during the second half of the year in credit demand may be associated in part with the downward adjustment of interest rates in line with developments abroad; notwithstanding these reductions, interest rates remain positive in real terms.

As regards prices, results have been encouraging, since inflation--as measured by the consumer price index--may reach only 7 percent--December 1985/December 1984. This reflects the awareness shown by trade unions in collective wage bargaining, facilitated by the prudent and gradual phasing out of exchange subsidies during the course of the year, and the policy of price controls.

Although the results obtained thus far in terms of the adjustment process are better than expected, my Venezuelan authorities remain deeply concerned with respect to the current situation and prospects for economic growth and employment. The depressed behavior of demand, which is jointly attributable to the slackness in public expenditure and to the weakness of consumption and private investment, has certainly not contributed to the improvement of the labor market situation. In addition, the correction of distortions such as those stemming from a resource allocation pattern unduly biased toward the production of nontradeable goods, has not clearly favored a recovery of high employment sectors. The persistent decline in the construction sector during the process of adjustment has markedly contributed to the high level of unemployment that the Venezuelan economy is currently experiencing.

With a view to strengthening current policies and ensuring the reactivation of the economy in 1986, the Venezuelan Government proposes to implement a recovery plan leading to a sounder overall economy and intended to combat the existing depressed conditions in the labor market but without generating inflationary pressures. This recovery plan includes three specific objectives. First, it aims at achieving sustained growth in the economy. To this end, domestic aggregate demand will be encouraged through support programs for basic infrastructure, agriculture, and tourism, promoting new employment opportunities and stimulating the resurgence of private investment. Second, the plan intends to strengthen the external sector even further by reorienting the economy in the medium term toward the production of tradeable goods, so as to compensate to some extent for the weakening of activities associated with traditional exports. Third, it attempts to improve the sources of public sector financing to a level consistent with the overall saving capacity of the economy, preventing thus the emergence of undesirable inflationary effects. Considering the relatively low level of ordinary resources in the budget, the program considers the possibility of changing domestic taxation mechanisms with a view to introducing greater flexibility in the current tax system.

After recognizing that the Venezuelan economy has gained some room for maneuver, allowing for a more expansionary fiscal policy in 1986, the staff warns my authorities on some potential dangers stemming from the full implementation of the three-year special investment program designed by the Government. I would like to make two considerations in this respect. First, the program has been reassessed, and the level finally submitted to the Congreso Nacional has been reduced to Bs 38 billion for the whole period, compared with the initial figure of Bs 45 billion. The reduction has been concentrated on those projects entailing import components and/or calling for external financing. Second, the financing of this program will be covered through domestic savings in accordance with the capacity already shown by the public sector, and the margin existing in household economies to absorb the public debt, preventing the emergence of inflationary pressures.

The budget project for 1986 submitted to Congress contemplates a Bs 10.155 million surplus in the accounts of the public sector. This would result from a nominal increase in government revenues of 2.6 percent and from an expenditure decline of 8.5 percent, with respect to 1985, without taking into account the special investment program which is scheduled to start in 1986 and will represent an additional Bs 15 billion in capital expenditure. As regards the revenue side, nonpetroleum revenues would increase by 11 percent, more than compensating for the possible decline in petroleum earnings. The proposed measures include a 31 percent increase in cigarette taxes, a decrease in tax exoneration, and improvements in tax collection procedures. On the expenditure side, it should be underscored that the freeze in current outlays will continue through 1986.

Regarding the external debt, as of May 1985 the Bank Advisory Committee agreed on the principles for a multiyear rescheduling of the public and publicly guaranteed debt. My authorities, nevertheless, considered the convenience of including a contingency clause in the rescheduling contracts in order to forestall the consequences of future events beyond the authorities' control. This clause was already accepted by the Bank

Advisory Committee, and the new agreement is now in the process of being submitted to the Government of Venezuela for its final approval. It is expected that all formal procedures, including the signature of contracts by individual creditor banks, will be completed by the end of January 1986.

With respect to the private external debt, the commission in charge of the registration of the private sector debt will end its task on December 13. With this step the situation concerning the private debt will have been completely clarified.

I am sure that my colleagues will recognize that Venezuela has made great strides in reducing the economic imbalances that the economy recorded three years ago and that the gains already obtained in the public and external sectors, inflation and level of reserves, together with the new profile for the external debt resulting from the rescheduling contract that will be agreed upon with the creditor banks will allow the country to look at the future with moderate optimism.

Mr. Kakfa observed that the major adjustment steps taken by the Venezuelan authorities had produced highly encouraging and dramatic results from the perspective not only of the short-run stabilization program but also of the medium-term outlook. Staff data showed that the Venezuelan economy had overperformed compared with the Government's program: 1985 would end with higher than expected surpluses in the current account of the balance of payments and in the public sector, together with lower price increases and money supply expansion rates. The cost had been very high, however, as output had declined for the fifth consecutive year and the unemployment rate had doubled during the past three years. Therefore the authorities' plans for a major three-year investment program to stimulate output and employment were understandable. There was no danger of inflationary pressure in the investment program since there was a comfortable surplus in the public sector accounts and, after three years of harsh adjustment, there were no major disequilibria in the economy. The drop in domestic savings had been reversed during the past two years, and both private and public savings had expanded sharply allowing expenditures--which had been curtailed during those years--to grow at a faster pace. In addition, the investment program would be financed by domestic savings and would not put pressure on the balance of payments.

The real effective exchange rate had been slightly depreciated in 1985, Mr. Kafka noted. He commended the authorities' intention to simplify the exchange system and to move by the end of the year toward a single controlled rate while avoiding new inflationary consequences. The staff seemed to believe that the only way to improve competitiveness was through exchange rate measures, but he considered that the key factor in Venezuelan adjustment was a firm social pact that supported wage restraint and wage adjustments that were in accordance with productivity increases, thereby keeping down unit labor costs. As long as unit labor costs were restrained there was no need for an exchange rate move.

He commended the authorities for maintaining Venezuela's bilateral economic cooperation with Central American and Caribbean countries, Mr. Kafka concluded. That assistance had been critical for the well-being of those countries.

Mr. Nebbia observed that Venezuela's economy had made impressive progress during the past two years. Earlier, Venezuela had experienced increasing economic difficulties that had culminated in a serious crisis in 1983. Output growth had been stagnant since 1980 and, following the imposition of severe adjustment measures, had declined in 1983. Although the authorities had acknowledged inadequate policy responses in a number of areas, the major factors that had contributed to the severe difficulties in Venezuela could be traced to the shortfall in oil revenues and uncertainties in the capital markets.

The Venezuelan authorities had taken significant steps since 1983 to adjust the economy, Mr. Nebbia continued. The improvement in the current economic situation had been the result of the implementation of strong adjustment measures: a cumulative average effective devaluation of the bolívar since early 1983, a significant increase in domestic prices for petroleum products, an austerity program for the public sector, a freeze on wages for most public sector employees, and a general tightening of fiscal and monetary policies. It was encouraging that the new Government that had taken office in February 1984 had adopted a further set of measures designed to correct relative prices and restrain domestic demand.

In 1985 the combination of restrictive fiscal and monetary policies with a prudent wage policy had helped to reduce inflation, improve the balance of payments, and enhance the allocation of resources, Mr. Nebbia noted. The Government's objectives for 1985 were the achievement of positive real growth and a decrease in unemployment, without jeopardizing the gains already obtained. Public finances had improved, inflation had decreased, and the external sector had been strengthened; however, results in economic activity and employment were not encouraging.

Exchange rate subsidies had been gradually phased out, and some progress had been made toward achieving a single official exchange rate by the end of 1985, Mr. Nebbia said. He welcomed Mr. Pérez's announcement that the number of agricultural products on the Bs 4.30 per U.S. dollar list had been reduced to two products--milk and wheat. He supported the aim of achieving full unification of the exchange rates as soon as possible. With a corrected exchange rate and tightened demand policies, exchange and trade restrictions would not only be unnecessary for balance of payments protection but would be counterproductive.

The public sector surplus of 2.7 percent of GDP at the end of 1985 was commendable, Mr. Nebbia remarked. That swing represented a great improvement in the management of public finances. Considering the uncertainties in the oil market and the Venezuelan economy's dependence on oil, both the maintenance of an adequate level of international reserves and a responsible management of public finances were key elements that should be maintained in order to avoid economic problems in the future.

During 1985, monetary policy had been correct, Mr. Nebbia commented. Domestic interest rates had been positive in real terms and above foreign rates, and a prudent wage policy had been implemented. The May 1985 agreement with commercial banks on a multiyear rescheduling of debt had contributed to the enhancement of internal and external confidence in the economic program.

He supported the Government's recovery plan for 1986, which would encourage growth in the economy without generating inflationary pressures, Mr. Nebbia stated. The three-year special investment program designed by the Government had been reassessed and the size reduced. Because the financing of the program would be covered by domestic savings, he encouraged that growth-oriented strategy. The increase in public investment should be complemented by steps to deregulate the economy, particularly in the areas of private investment and the implementation of tax and tariff reforms. The Government should encourage conditions and opportunities for the resurgence of private investment. It was therefore essential to continue prudent policies in fiscal, monetary, and wage areas if confidence in the economy was to be reinforced.

In sum, Mr. Nebbia concluded, Venezuela had shown courage in implementing a comprehensive economic program, and he was optimistic that the economic situation of the country would continue to improve in 1986.

Mr. Goos noted that Venezuela was expected to make considerably more progress in overcoming its domestic and external imbalances than initially intended under the 1985 Quantified Economic Program. Compared with those earlier goals, such accelerated progress would definitely be more commensurate with the country's adjustment needs and debt servicing obligations. Nevertheless, and notwithstanding the commendable pursuit of restrictive demand-management policies and the structural measures described by Mr. Pérez, it appeared that the authorities remained confronted with the same key issues of economic policy that had been the focus of the Board's midyear consultation discussion (EBM/85/84, 5/30/85). Those issues were the available scope for stimulatory measures without endangering the progress achieved so far and the appropriate pace of liberalizing the economic system.

In analyzing those issues he had arrived at conclusions that were broadly identical with those of the staff and with the recommendations expressed by his chair on the occasion of the midyear review, Mr. Goos remarked. The sluggishness in the non-oil sector, the increasing unemployment rate, and the ongoing decline in real per capita income were extremely worrisome and commanded sympathy for the authorities who intended to stimulate economic activity. Indeed, a carefully devised investment program based on a thorough cost-benefit analysis and emphasizing quick-yielding projects, could make an important contribution toward overcoming those domestic problems. However, while Mr. Pérez assumed that internal and external imbalances had been overcome, thus paving the way for a new phase of economic recovery, doubts remained as to whether the country had really reached a sufficiently solid base from which to launch a strong recovery program. He believed that improvements in the fiscal and external sector remained fragile, as they seemed to reflect, to a considerable extent, unexpected delays in the implementation of the investment program and a severe compression of imports as a result of administrative controls.

Furthermore, recent developments in the oil market suggested that even the staff's rather conservative medium-term scenario could be over-optimistic, Mr. Goos continued; some analysts projected a drop in the oil price to $20 or less a barrel. Given the sensitivity of Venezuela's economy--and public sector revenue--to oil export earnings, such a drop in the oil price would be bound to create serious adjustment problems that would be greatly exacerbated if they coincided with an undue expansionary policy stance. Against that background, he welcomed the decision of the authorities to reduce the size of the three-year special investment program. However, in view of the worsened outlook for the oil market, he was concerned that even the reduced investment volume could create unsustainable domestic and external financing gaps. He invited the staff to comment on that issue; it would also be interesting to learn about the prospects of the contingency clause in the rescheduling arrangements being activated as a result of the likely weakening in the external position of the country. In any event, there continued to be a strong case for great caution considering the presumably limited capacity of the economy to respond in any efficient and lasting way to stimulatory measures. In the present environment of widespread administrative controls, it was to be feared that much of the stimulus would translate only into additional inflationary pressures and a renewed weakening of the balance of payments position.

The second main issue confronting the authorities was the urgent task of deregulating the economy, Mr. Goos said. Unfortunately, only little progress was being made in that critical area despite the advice of the staff and the Executive Board. It was particularly worrisome that the authorities apparently continued to be reluctant to follow that advice within a decisive and comprehensive framework of structural adjustment. He endorsed the staff's recommendations and emphasized the urgent need to reduce and, to the extent possible, eliminate the existing controls and regulations on exports, imports, and investment, as well as on prices and the exchange rate system. Although the staff had apparently refrained from repeating their previous recommendation to implement a specific timetable for the liberalization of imports, that advice continued to have merit and should be extended to other liberalization efforts, notably with regard to the price system.

The prospect of a further significant decline in public sector revenue from oil clearly underlined the need to reform the tax system, Mr. Goos commented. He also encouraged the authorities to make an effort toward liberalization of the foreign investment legislation within the Andean Pact. A more liberal environment for foreign direct investment could make an important contribution toward mobilizing foreign exchange and hence toward solving the debt problem on a lasting basis. Finally, he endorsed the staff appraisal and supported the proposed decision.

Mr. Coumbis recalled that during the Board meeting for Venezuela's midyear Article IV consultation (EBM/85/84, 5/30/85), the Executive Directors had commended the authorities for the impressive results in the areas of public finance, balance of payments, and rates of inflation. The current staff report indicated that Venezuela's adjustment effort in the first half of 1985 continued to be successful, and projected outcomes for the whole year in many fields were expected to be better than the original program's targets. Thus, the overall public sector would register a surplus equal to 1.7 percent of GDP instead of the programed deficit of 0.7 percent. The current account surplus would be about 7 percent instead of the 3.7 percent originally projected, and the overall surplus of the balance of payments would amount to $2.2 billion compared with $0.6 billion. However, the major part of the overall budget surplus reflected mainly delays in the implementation of public investment programs, while the doubling of the current account surplus of the balance of payments was mainly due to substantially lower than expected imports, reflecting lower aggregate demand and the tightening of import controls.

Although the adjustment effort had been successful thus far, there were a few areas of concern, Mr. Coumbis continued. Those areas included the negative growth of real GDP--7 percent in the past two years--increases in the unemployment rate to 13.4 percent, and structural weaknesses in the economy--in particular, price restrictions, import prohibitions and restrictions, exchange restrictions, multiple currency practices, controls on exports and private investment, and the lengthy process of registration of private foreign debt.

A high price had been paid for the stabilization of the economy in terms of a negative GDP growth rate in the past three years, Mr. Coumbis commented. In fact, real GDP had decreased since 1981 and was expected to decrease further in 1985 by 1.5 percent, while the population was increasing at a rate of 3 percent. For 1985 in particular, the authorities had attempted to revive investment activity both in the private and the public sectors by reducing interest rates and increasing the investment outlays of the overall public sector budget by more than 30 percent. The results, however, had not been satisfactory in both sectors. Public investment programs had been delayed for organizational reasons, and capital outlays were not expected to increase by more than 15 percent, while excessive reserves in the commercial banks indicated the continued weakness of the private sector with respect to investment activity.

There was no doubt that real GDP had to increase in the coming years and that investment had to be stimulated, Mr. Coumbis stated. As recent developments indicated that the economy had gained some room for maneuver, he agreed with the authorities that public investment expenditures should be increased. However, he shared the staff's concern regarding the contemplated excessive increase of the special investment program for several reasons. First, such a massive increase of government investment would entail organizational problems. Second, the authorities, who would be pressed to increase expenditures as soon as possible, might launch programs including nonproductive investment. Third, past experience with high rates of increase of public investment, especially during 1980-82, indicated rather poor results with respect to both the rates of growth of the economy and price levels. Nevertheless, he was heartened to read that the authorities had already adjusted downward the three-year special investment program to Bs 38 billion instead of Bs 45 billion and that the program would be financed by domestic savings.

Another area of concern was the structural weakness of the economy, Mr. Coumbis remarked. Although substantial progress had been made by Venezuela, further structural changes were badly needed, such as the reduction or abolition of price and import controls, unification of the exchange rates, the elimination of controls on exports, and the simplification of controls on private investment. Progress in those areas was disappointing. The authorities were committed to unifying only the controlled exchange rates while no commitment or time limits for a full unification of exchange rates or the abolition of controls on imports, exports, and prices existed. Similarly, the authorities were not willing at present to adopt a free market exchange rate for a wide range of transactions. Structural improvements in market-oriented policies would undoubtedly promote private investment, but two points should be stressed. First, the social pact agreed among the social partners was a crucial factor in the successful adjustment policies followed so far by the authorities. Moderation in wage increases was obviously based on promises by the Government to control prices and to keep inflation at low levels. It was understandable, therefore, that any attempt by the authorities to deregulate the economy should proceed with extreme caution. In that respect, he welcomed the task of the tripartite commission of reviewing areas where regulation could be reduced, although it was clear that the deregulation process would take a long time to complete.

The second point he wished to stress was that the deregulation of the economy and the full unification of the exchange system, although necessary conditions to promote private investment and to secure sustained growth, were not sufficient conditions, Mr. Coumbis continued. The experience in his own country, and in other developing countries with a long history of government intervention, revealed that the revival of private activity depended on many other factors as well and that it was a long-term process. In sum, at least in the medium term, the revival of the economy had to be based to a certain extent on public investment and its constraints of quantity and quality. The extent to which public investment would be used to revive economic growth would depend especially on the expected rate of increase of private investment and on the quality of public investment projects under the general constraint of restrictive effective demand. The authorities would have to show flexibility in determining each year the size of public investment.

The medium-term outlook also gave cause for concern, Mr. Coumbis observed. After the latest developments in the oil market, he wondered whether even the conservative scenario accepted by the staff was not too optimistic. According to the staff, the sensitivity of the Venezuelan economy to world oil prices was such that a decline in the average export price by $1 a barrel would reduce export earnings by $0.5 billion. Moreover, the staff stressed the fact that its projections for moderate growth and a sustainable balance of payments during the period 1986-90 assumed "the implementation of an exchange rate policy that helped to promote exports and to moderate the growth of imports; [and] policies of deregulation that would stimulate private investment." Furthermore the staff "presumed in this projection that the generation of growth and employment over the medium term will have to come in large measure from changes in economic conditions designed to foster greater private sector investment and improved resource allocation." He asked the staff whether it assumed the full unification of exchange rates and the complete deregulation of import, export, and price controls, as suggested in the staff report, or a continuation of present policies. Clearly, the staff foresaw a strong revival of private investment, and he wondered whether that assumption was realistic. He also asked the staff whether in the present case of enhanced surveillance, a quantified program for 1986 should not have been presented to the Board in conformity with the guidelines approved by the Board.

Mr. Hodgson said that since the midyear consultation with Venezuela under the aegis of enhanced surveillance by the Fund (EBM/85/84), the Venezuelan authorities had continued to make impressive progress toward correcting the internal and external imbalances in the economy. Inflation had been reduced rapidly, and both the fiscal balance and the external current account had moved strongly into surplus. Nonetheless, prospects for the economy in 1986 were clouded by the persistent weakness in the international oil market. The cost of adjustment in terms of unemployment and idle capacity had also been very high and had created an added political constraint.

In light of the continued wage restraint and the comfortable level of foreign exchange reserves, there appeared to be scope for some fiscal stimulus, Mr. Hodgson commented. He therefore agreed in principle with the Venezuelan authorities' intentions to increase capital expenditure as one means of stimulating economic activity. Yet, because the world petroleum market might weaken further, inflationary expectations might still be present, and the debt service burden could remain heavy, the staff's cautious fiscal advice was credible. There seemed to be room for compromise however. The most important concerns at present should be, first, to maintain public finances roughly in balance over the medium term and, second, to avoid a stop-go pattern of public sector expenditure, in particular public sector investment, over the coming years. Wide swings in investment expenditure in past years had led to needless resource waste and had made it difficult to plan fiscal outlays efficiently. He encouraged the authorities to develop a sound investment plan to ensure that projects were selected on the basis of long-term profitability and to implement that plan in a systematic fashion that avoided large swings in the fiscal balance. He welcomed the recent reduction in the size of the special investment program.

For any fiscal stimulus to achieve more permanent gains, further measures must be taken to promote structural change, Mr. Hodgson continued. Some efforts had been made in that direction, but greater efforts were needed to deregulate the Venezuelan economy, including reductions in the scope of price, import, and export controls and the elimination of interest rate ceilings. Making such changes would not be easy, given the long history of controls in the economy and the care that would be required not to adversely affect income distribution and the overall price level. Nonetheless, the present system had hampered efforts to diversify away from heavy dependence on petroleum and might be affecting the confidence of private investors. Prospects for sustained growth in both the short term and long term would be well served by liberalization efforts.

Monetary and credit policy might have to be tighter than contemplated under the Quantified Economic Program if monetary policy was to be consistent with the target for international reserves, Mr. Hodgson remarked. He welcomed the monetary authorities' interest rate stance, which had maintained positive real interest rates, but he urged the authorities to eliminate maximum lending and deposit rates in order to increase interest rate flexibility and thereby help to improve resource allocation. He also hoped that the authorities would consider gradually eliminating the preferential interest rates on loans to the agricultural sector.

The staff's medium-term outlook indicated that considerable progress had already been made toward achieving a sustainable balance of payments position, Mr. Hodgson went on. However, meeting the medium-term targets would require the maintenance of strong and consistent macroeconomic policies and a flexible approach toward the exchange rate. It would be unfortunate if the hard-won gains made over the past few years were lost or jeopardized through excessive reliance on short-run reflation of the economy. The medium-term balance of payments goals would also be served by a shift away from import controls in favor of a broad system of tariffs, which might simultaneously encourage allocative efficiency in the economy and strengthen the Government's revenue base.

The controlled exchange rates should be unified by year-end, and, ideally, Venezuela should pursue a more flexible, or perhaps even unified, exchange rate policy, especially if non-oil exports were to grow rapidly, Mr. Hodgson said. However, he would be concerned if the exchange rate were affected unduly by transitory factors in the oil market, which might induce costly investment and consumption decisions that were not easily reversed. Indeed, the free market rate had fluctuated widely over the past six months, ranging from Bs 12 to Bs 15 per U.S. dollar. Although that market was admittedly very thin at present, such wide fluctuations were not likely to be conducive to restoring stable growth. He therefore hoped that in the next consultation report, the staff might address more extensively the complications affecting exchange rate management introduced by the high degree of dependence of export earnings on the oil sector.

He welcomed the improvements that had been made in eliminating external arrears, Mr. Hodgson stated. However, full settlement without further delay was essential if Venezuela was to fully restore its creditworthiness with both private and public creditors. Given the relatively large size of Venezuela's reserves, there was no reason why the stock of external arrears should not be completely eliminated as soon as possible.

Venezuela had made generous assistance available to a number of Central American and Caribbean countries under its joint oil facility with Mexico, Mr. Hodgson added.

Difficult adjustment measures had been undertaken over the past two years, Mr. Hodgson concluded; if Venezuela undertook the supporting measures that he had mentioned and if the world petroleum market did not take a significant turn for the worst, Venezuela's medium-term goal should be well within reach.

Mr. Fujino remarked that Venezuela had made substantial progress in its adjustment policies over the past two years, and it was reassuring to note that the major targets of the 1985 economic program had so far been achieved with ample margins. The targets for the fiscal and external positions and the inflation rate had all been revised favorably, reflecting developments in the first half of the year. However, the authorities were concerned about the recent sluggishness in economic activity, particularly the slow growth in nonpetroleum GDP, and about the high and still rising unemployment rate. They were considering the adoption of a three-year special investment program and a more expansionary monetary policy to stimulate domestic demand.

The authorities' concern about output and employment was understandable, Mr. Fujino commented. There might be scope for allowing somewhat higher fiscal spending in the short run, given the large surplus in the public sector and the delays in public investment implementation during the first half of the year. However, he wondered whether such expansionary policies would lead to fundamental solutions of the problems facing the economy of Venezuela. The staff cautioned that previous attempts to stimulate domestic demand in Venezuela through higher fiscal spending, lower interest rates, and larger wage increases had not proved successful and had merely resulted in soaring inflation, currency appreciation, and a decline in non-oil output. The driving force of sustained economic growth must be an autonomous pickup in private investment activities. The stagnation of non-oil output had been an almost continuous phenomenon since the beginning of the decade. While it might be difficult to fully assess the factors behind that development, the staff had made a convincing case in saying that the pervasive application of controls and regulations, such as the multiple-exchange rate system and import and price controls, seemed to have caused underutilization of resources and had created major disincentives to private investment and employment. As pointed out during the previous discussion on Venezuela (EBM/85/84, 5/30/85), there was a need to take prompt and decisive measures to reduce those regulations.

More specifically, Mr. Fujino continued, while the price control system might have played a useful role as a necessary counterpart to wage restraint, any prolonged regulation would create price distortions and inefficiencies. The recent stability in the inflation rate might provide the authorities with a good opportunity to take a major step toward price liberalization.

The authorities believed that the present tight import control system was necessary to change the composition of imports and to protect domestic industries, Mr. Fujino noted. He shared the staff's view that such objectives could be more efficiently achieved by a flexible exchange rate policy and an appropriate import tariff structure. He urged the authorities to complete the current study on tariff reform as soon as possible so that a progressive liberalization of the system would be made possible.

Progress was being made toward the unification of all controlled exchange rates, Mr. Fujino observed. However, the staff pointed out that the bolívar had effectively appreciated by 15-20 percent on average since February 1984, and that the spread between the controlled and free market rates remained large. To realize full unification in the near future, a more flexible policy regarding the determination of the controlled rates, as well as the transfer of additional transactions to the free exchange market, seemed called for.

Although Venezuela's medium-term outlook appeared reassuring, it was predicated on the assumption that prudent financial policies would be maintained, including a balance or even a small surplus in the fiscal position, Mr. Fujino remarked. It would therefore be inappropriate at present to take any measures that would result in a sizable fiscal deficit, and he was reassured that the authorities shared that view.

Broad money had grown very slowly in the first half of the year, while the growth rate of the monetary base was relatively high, which seemed to indicate that an attempt by the Central Bank to expand liquidity had merely resulted in an increase of excess reserve holdings by commercial banks, Mr. Fujino noted. Given the current weak money demand, it would be inadvisable to try to boost the economy through additional money injection. He joined the staff in recommending a somewhat less expansionary credit policy.

In sum, Mr. Fujino concluded, sustained growth would be achieved through financial prudence and progressive deregulation, and he hoped that those would be the main elements of the authorities' 1986 economic program.

Mr. Ercel observed that since early 1983, Venezuela had made important progress in adjusting its economy. The results achieved in 1983 and 1984 had been encouraging from the standpoint not only of short-term stabilization but of the medium-term outlook. A drastic reduction in the public sector deficit, a substantial decline in the overall balance of payments deficit, and success in containing inflationary pressures and promoting structural changes had all demonstrated substantial progress toward adjustment. However, some areas of concern remained: the weak output performance, the high level of unemployment, and a number of economic restrictions and controls. Those problems were not unexpected considering the rapidity of the adjustment required by the Venezuelan economy, which had depended heavily on oil for many years. He agreed with the staff that the authorities' intention of stimulating domestic economic activity over the short run by adopting somewhat more expansionary fiscal policies should be viewed with caution as only continued adjustment would provide the basis for a sustainable recovery.

The generation of additional financial resources for government use would require an increase in budget revenue through the early implementation of tax reform, Mr. Ercel remarked. The report on recent economic developments indicated that the ratio of revenue from nonpetroleum sources to nonpetroleum GDP was currently low at about 13 percent, of which income tax generated only 4 percent. Policy and strategy with respect to nonpetroleum tax revenue were therefore important for the Venezuelan economy as a whole. For that reason, he regretted the delay in implementing tax reforms, including the modification of personal and corporate income taxes and the introduction of a general sales tax. The special investment program had been reassessed by the Government using a realistic approach, but he hoped that the program would achieve a major part of its original aims.

The primary product sector--including agriculture, livestock, fishing, and forestry--seemed to be a potentially suitable part of a balanced economic structure, as it accounted for about 6 percent of GDP and 15 percent of total employment, Mr. Ercel continued. He welcomed the Government's major drive to expand agricultural output. Policies aimed at stimulating the agricultural sector, such as increased expenditures on irrigation systems and technical assistance and a steep rise in minimum prices, were important in that context. He asked the staff for further information on the World Bank's participation in agricultural policy and implementation in Venezuela.

Unlike the authorities' firm implementation of fiscal and monetary policies leading to the substantial and rapid adjustment of the economy, their approach to exchange rate policy and to the elimination of the multiple exchange rate system had been too gradual, and results to date were not encouraging, Mr. Ercel remarked. The present system produced distortions and limited the competitivity gains of the non-oil sectors. He agreed with the staff that the exchange rate system should be unified, that a flexible exchange rate policy should be pursued, and that import controls should be eliminated in order to obtain a more efficient allocation of resources.

The adjustment efforts to correct the imbalances in the Venezuelan economy were satisfactory, Mr. Ercel concluded. In the light of the medium-term projections, however, additional efforts in several aspects of economic policy, particularly the structural area, would be required to revive growth.

Mr. Dallara commented that Venezuela's current economic performance and policy stance continued to have mixed results. Unfortunately, medium-term growth prospects were rather negative. The considerable progress made in strengthening the balance of payments and in reducing inflation was commendable, and the direction of fiscal, monetary, and wage policies was generally restrained and sound. However, he continued to have serious concerns, which were shared by the authorities, about the lack of sustained economic growth and the rising level of unemployment. He shared the staff's reservations about some elements of current fiscal, monetary, and exchange rate policies. The wide use of administrative controls throughout the economy was worrisome, and a number of structural reforms would be essential in coming years if the growth and employment objectives of the authorities were to be achieved. In the absence of such reforms, he had serious doubts that sustainable economic growth could be achieved.

During the discussion for Venezuela's 1985 midyear consultation, some areas of concern had been described, Mr. Dallara recalled. Those included the existence of rather tight trade and payments restrictions, the lack of economic diversification, questions about the proper degree of fiscal and monetary restraint, and the extent of price controls. His own doubts concerning those policy areas had increased since that discussion. For example, import controls, which had already been highly restrictive, seemed to have been tightened somewhat. There had been no general shift in policy stance that would seem to favor more rapid progress toward diversification. Although there had been a lower rate of growth of net domestic assets and there was a small surplus in prospect for the public sector, that performance appeared to be due principally to unforeseen developments, in particular delays in implementing public investment projects and low private credit demand in the face of sluggish growth, rather than to any deliberate shifts in policy. With respect to price controls, there had actually been a small increase--from 150 to 170--in the number of items subject to prior approval.

More generally, the breadth of administrative controls in Venezuela continued to raise serious questions about longer-term prospects for sustainable economic growth, diversification, and external balance, Mr. Dallara stated. The panoply of controls touched on prices, domestic and foreign investment, rents, interest rates, imports, exports, and profit distribution. Even if the authorities administered controls flexibly and adjusted prices and ceilings regularly in line with what they perceived to be appropriate shifts in relative prices and incentives, it was difficult to believe that any authorities could have the requisite knowledge and foresight to ensure that domestic and foreign consumers, savers, and investors actually received the appropriate incentives to maximize economic growth potential and efficiency and to ensure financial stability. The staff correctly warned that such controls could lead to the underutilization of resources, disincentives to private investment, capital outflows, and the creation of rigidities in the economic structure. Indeed, there seemed to be some statistical evidence of such effects. For example, the staff indicated that nonpetroleum GDP had fallen in each of the past three years, although Mr. Pérez had mentioned a slight positive figure for 1985. The ratio of private fixed investment to GDP had generally trended downward in the 1980s to date. In addition, there had been substantial outflows of Venezuelan capital, amounting to approximately 11 percent of GDP in 1983 and 12 percent in 1984, according to national income data, while balance of payments data for short-term capital outflows plus net errors and omissions were negative to the extent of $15 billion over 1981-84.

Clearly, even if the usual macroeconomic policy tools were managed effectively and price signals were "correct," there would still be serious structural and institutional impediments to sustained growth, Mr. Dallara remarked. In part, it was concern about such structural inadequacies in a number of countries that had motivated his authorities' debt initiative proposed recently in Seoul, Korea. There were not many countries where macroeconomic policies and relative prices were consistently satisfactory, and strong emphasis on such matters remained essential, but additional attention should be given to structural and institutional problems. Venezuela had failed to achieve a significant degree of economic diversification over a long period of years, which suggested the presence of some of those impediments. The staff report cited a number of areas where reforms were desirable: trade liberalization on both the import and export sides, deregulation of domestic and foreign investment, full unification of the foreign exchange system and flexible exchange rate policy implementation following unification, tax reforms in both direct and indirect tax areas, and tariff reform related to import liberalization. Also, given the rapid rise in the unemployment rate and the dearth of knowledge about the labor market, he wondered whether some attention should not be given to the possibility of labor market reforms. He would not attempt to prescribe the steps to be taken, but he hoped that the Venezuelan authorities would devote increased attention to the role that such reforms might play over the medium term in achieving sustained growth. He asked the staff for more analysis and policy recommendations for reforms in future papers prepared for consultation discussions on Venezuela.

It was especially important that the enhanced surveillance arrangements with the Venezuelan authorities be mutually beneficial to Venezuela and the Fund, Mr. Dallara stated. At the previous Board discussion on Venezuela, he had mentioned the importance of the interplay between the policy approach taken by the member country and the policy suggestions offered by the Fund. For enhanced surveillance to succeed, a genuine willingness on the part of the authorities to listen to and be influenced by the suggestions made by the staff and the Board was critical. He did not have the impression that the discussions between the Fund and Venezuela had had as much effect as could be desired. Differences of view between the staff and the authorities arose in a number of specific policy areas--for example, the size of the special investment program, the timing and importance of full exchange rate unification, the long delays in eliminating foreign debt arrears of the private sector, and, in general, the maintenance of widespread administrative controls. Mr. Pérez had said that the special investment program was expected to be smaller than contemplated; he asked the staff for its reaction to that latest development. Although acceptance of Fund views in all areas could not, and should not, be expected, a close collaborative effort between Venezuela and the Fund was necessary.

Progress had been achieved with regard to fiscal, inflation, and balance of payments objectives, but continued attention needed to be given to those areas, Mr. Dallara pointed out; he asked the staff whether the authorities would also be able to focus more on the structural area. Although the staff had already discussed structural matters to some extent, he wondered whether the Venezuelan authorities attached the same degree of importance to those questions as did the staff. There seemed to be scope under enhanced surveillance for added focus on the need for changes in structural areas. For example, he wondered whether it would be possible to establish quantitative targets with regard to import liberalization or items subject to price controls. He asked the staff and Mr. Pérez to comment on that subject.

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/85/179 (12/11/85) and EBM/85/180 (12/13/85).

3. SOMALIA - OVERDUE FINANCIAL OBLIGATIONS - NOTICE OF FAILURE TO SETTLE TRUST FUND OBLIGATION

1. The notice of the Managing Director dated December 6, 1985 on the failure by Somalia to fulfill an obligation under Decision No. 5069-(76/72) on the Trust Fund, in EBS/85/269 (12/6/85), is noted. The notice shall be placed on the agenda of the Executive Board for December 27, 1985.

2. Consideration of the notice of failure to settle the Trust Fund obligation particularly affects Somalia. The member shall be informed by rapid means of communication of this matter and of its right to present its views through an appropriately authorized representative. (EBS/85/269, 12/6/85)

Decision No. 8149-(85/180) TR, adopted
December 11, 1985

4. EDUCATION ALLOWANCE - EXTENSION OF ADJUSTMENTS TO EXECUTIVE DIRECTORS AND ALTERNATES

The Executive Board approves the recommendation to extend to Executive Directors and Alternates recent adjustments in the education allowance policy for staff. (EBAP/85/300, 12/9/85)

Adopted December 11, 1985

5. ASSISTANT TO EXECUTIVE DIRECTOR

The Executive Board approves the appointment of an Executive Director as set forth in EBAP/85/304 (12/10/85).

Adopted December 12, 1985

6. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors as set forth in EBAP/85/303 (12/10/85) and EBAP/85/306 (12/11/85) and by an Advisor to Executive Director as set forth in EBAP/85/306 (12/11/85) is approved.

7. STAFF TRAVEL

Travel by the Managing Director as set forth in EBAP/85/305 (12/11/85) is approved.

APPROVED: AUGUST 4, 1986

LEO VAN HOUTVEN
Secretary