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UPDATE ON THE WORLD BANK/INTERNATIONAL MONETARY FUND JOINT ANNUAL MEETING, 1980

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UPDATE ON THE IMF-WORLD BANK JOINT ANNUAL MEETING

I am happy to say that my memoranda of September 8, 1980 and September 12, 1980, on the IMF and the World Bank, respectively, were quite accurate in anticipating the major issues that were raised in the September 28 - October 3 joint annual meetings of the IMF and IBRD.*/ However, since it was impossible to perfectly anticipate all aspects of the meetings, I would first like to update and correct the original material, where appropriate. I will then follow with some general observations.

The Specific Issues

(a) The PLO

At the time of writing the memoranda, it appeared that the Governors' vote on observer status for the PLO would not reach a quorum, thereby allowing the Chairman of the meetings, Mr. Amir Jamal of Tanzania, to decide upon the issue. He, of course, has always been in favor of inviting the PLO to the meetings. At the prospect of having the PLO attend the meetings, powerful members of the U.S. Congress put great pressure on the Carter Administration to ensure a quorum and a negative vote on the observer status. The Congress threatened that should the PLO be permitted to attend, it would then refuse to pass pending legislation for U.S. subscriptions related to a capital increase at the World Bank and a quota increase at the IMF.

The Administration panicked and then began to put great pressure on the Governors to support a negative vote. A quorum was reached in time and the PLO observer status was rejected. This threatened to throw the meetings into turmoil; the negative vote won by a very slim margin, reportedly because some PLO supporters misunderstood the ballots, thereby accidentally voting on the anti-PLO platform.

*/ This report represents a follow-up on the material already presented in the two aforementioned memoranda and therefore should be read only in conjunction with them. (See CEPAL/WAS /R.18 & R.19)

Some Arab countries threatened to make a floor fight at the meetings, and, of course, their financial support of the Bank and Fund became even more problematical.

At the last minute a compromise was reached. It was decided to have no observers attend the meetings this year. Meanwhile, all debate on the PLO issue was held behind closed doors in the meetings of the Procedures Committee. Out of this grew an agreement to form a new committee of finance ministers to study the matter and report back by the end of the year. The new committee is to have 7 instead of 6 members and will be headed by Mr. R. Muldoon of New Zealand. Importantly, neither the U.S. or Saudi Arabia will be on the committee.

(b) A food facility

In the memoranda I did not anticipate a proposal for a Food Facility at the IMF. The idea apparently originated at the FAO and has had an enthusiastic reception from the Managing Director of the Fund. It would help to compensate countries for shortfalls in domestic food production and sharply higher prices for food imports. While details for a facility must still be worked out, such a program would no doubt assist the Fund in its efforts to soften its image *vis-a-vis* the Third World; the concept also represents a positive response to some proposals made by the G-24. It should be noted that a number of industrialized countries object to formation of a new facility, as such, and urge that the program be put into the already operating Compensatory Finance Facility.

(c) The SDR

There was almost unanimous support for a more important role for the SDR. The view was very positive on the decision to simplify the SDR currency basket to five currencies (U.S. dollar, Deutsche Mark, French franc, the Japanese yen, and the pound sterling). Most countries seem to want measures to create an even more attractive SDR, e.g. by giving it a commercial interest rate, by promoting its use in the private sector, etc. There also seems to be a general feeling that another round of SDR allocations is merited in the fourth basic period beginning in 1982, largely because when the allocations for the third basic period were planned in 1978, there were no perceptions of the current economic difficulties. Just how much should be allocated in the fourth basic period is a matter of debate, with the developing countries probably pushing for larger allocations than many industrialized countries might want to see. (The G-24 proposed a 6 billion supplementary allocation during this basic period and has mentioned the figure of 10 billion SDRs for the beginning of the fourth basic period in 1982). As a side note, one of the few dissenting views on the role of the SDR came from Greece, which proposed the creation of a "more effective" reserve asset which it has designed and termed the "metron".

(d) The SDR Link

This proposal may be slowly coming of age. There seems to be renewed support for a link and indeed the Interim Committee has asked the Executive Director of the Fund to carry out a "comprehensive" study of a possible link. A major obstacle to overcome in establishing the link is the continued opposition of the U.S., which was publicly expressed in the meetings by Treasury Secretary Miller. The U.S. feels that a link will undermine the SDR as a reserve asset.

(e) More resources for the Fund and Bank

There was strong support in most circles for increased resources for the Fund and World Bank.

In order to support lending up to 600% of quotas -which was formally endorsed- the IMF has been authorized to seek new resources. There is a general preference among the industrialized countries that increases come via quotas, and for this purpose the Fund was given a mandate to prepare for the Eighth General Review of Quotas, even though subscriptions under the Seventh Review have yet to be fulfilled. However, recognizing the Fund's immediate need for resources, it received continued support to borrow abroad. The preferred source of funding would be direct loans from OPEC, both because of principle and the fact that it probably would prove to be more economical than securing resources in private markets. However, private markets may be the only recourse if the PLO issue is not resolved. If private markets are used, then it must be determined whether borrowing will be direct, or through the international commercial banks, which of course would be eager to lend to the Fund. It is important to note that borrowing from private markets has some legal roadblocks which the IMF would first have to overcome.

Robert McNamara dramatically pointed out the Bank's need for new resources. Among the arguments given were: (i) the 1981-1985 lending program increase of 5% a year in real terms was designed in 1977 and could not anticipate the surge in inflation and new financing requirements of LDCs, (ii) the new structural financing loans must now come from current resources while they should be additional to existing loans, (iii) the Bank now sees a need for it to roughly double its lending in energy and (iv) the admission of China to the Bank will place large new demands on the Bank that will have to reduce the availability of loans to other countries, unless new resources are made available to it. There seemed to be broad consensus for supporting more Bank lending, particularly in the areas of energy and structural adjustment. It remains to be seen just how this will be done. The Brandt Commission's idea of changing the gearing ratio of the Bank to 2:1 received much consideration and indeed it was even suggested by Mr. McNamara as a possible way to increase the Bank's resources. Other ways suggested by Mr. McNamara were creation of an energy affiliate (which would not necessarily have to have a 1:1 gearing ratio) and an increase in callable, but not paid-in capital of the Bank. A number of industrialized countries seemed to be inclined towards the more conservative route of increasing callable capital, so as not to erode the Bank's creditworthiness, while many developing countries argued for a change in the gearing ratio. Still other countries suggested a combination of all the possibilities.

(f) Subsidy Account

There will be subsidies for IMF lending which probably will be financed by a combination of voluntary contributions and repayments from the Trust Fund. The effective liquidation of the Trust Fund was opposed by the G-24, which sought to have it maintained for exclusive lending to low income LDCs. The G-24 wants the subsidy account to be additional to existing Fund resources, but under the proposal to draw resources from the Trust Fund this would not be the case.

(g) Voting Rights

The G-24 wants increased voting rights for developing countries. With regard to the IMF, it wants LDCs' position in the quotas to rise from 33% to 45%, which would enhance their decision making power; in the upcoming 8th Review of Quotas they would like to see such a quota realignment undertaken (Saudi Arabia has been very vocal on this issue). The IMF's Interim Committee, interestingly, has urged the Executive Board to give further consideration to the matter. The issue of voting rights probably will be a major matter of debate with regard to the proposed energy affiliate at the World Bank; if the OPEC countries are the main source of funds, they will undoubtedly seek a bigger voice in the Bank and/or the affiliate. Of course there are some who question whether the energy affiliate should be controlled by oil producers.

(h) IMF/World Bank Cooperation

There was general recognition that the two institutions will have to collaborate more closely in the future. The U.S. even suggested a formal review of past collaborative efforts in order to arrive at concrete guidelines for future joint operations.

(i) Substitution Account

There seemed to be renewed interest in the substitution account, and the Interim Committee recommended further study of the matter. Importantly, the U.S. appears willing to reconsider the concept, although it would prefer to use the term "monetary reserve account". On the other hand, the U.S. publicly stated that it sees little possibility for rapid adoption of any measures in this area.

(j) Surveillance

Many developing countries, and some industrialized countries, urged the Fund to intensify and make more explicit its surveillance of surplus, as well as deficit countries, in order to ensure more symmetry in the adjustment process. The whole concept of Fund surveillance remains vaguely defined and some countries (including the U.S.) suggested a more explicit and systematic process. It is notable that in the meetings Germany publicly stated that it could live with its current account deficit for awhile, suggesting that it might be under pressure from the IMF not to quickly return to a surplus position.

Some General Observations

In contrast to the U.N. General Assembly, the tone of the Joint Meetings was low-key and not very conflictive. The developing countries did not place any major new demands on the industrialized countries. With respect to past demands, in terms of concrete action the only event of major significance was the increase in loans available from the Fund, up to 600% of quota.

Despite the above, one does gain a sense of progress, no matter how slow that may be. In essence, many of the proposals of the G-24, as reflected in its Program for Immediate Action, appear to be gaining support and/or serious consideration. The IBRD has called for a substantial increase in resources to promote energy development and to make its structural lending more significant and additional to current resources; there probably will be more SDR allocations and the possibility of a "link" at least now appears to be less remote; the Fund is on the verge of aiding countries suffering from shortfalls in food production and/or food price increases -which is rather uncustomary terrain for the IMF-; the issue of increasing LDC voting power has become respectable; the Fund has significantly increased the resources available to anyone borrower for adjustment, while extending the adjustment period itself as well as the repayment period; and the Fund has recently recognized that its conditionality should be modified to take into account the current world circumstances. So, many of the G-24 proposals have not fallen on deaf ears, and this may be one explanation for the rather low-key communique issued by the Group (It is less forceful than in the past and has no real new proposals). Thus, there is a perception of progress, but one must wonder whether it is fast enough to avert a deepening of the crisis in the world economy and more sacrifice of the development objectives of the Third World.

There is a sense of frustration in the world community. Almost everyone at the meetings expressed deep concern for the gloomy world outlook (The Iran-Iraq war had to make everyone feel even more vulnerable); yet no one seemed to have any answers on how to resolve the problem. The remedial solutions were the tired calls (mostly by industrialized countries) for control of inflation, "adjustment" (which in the context of the world crisis now means different things to differente people) and some ill-defined statements about attention to supply matters. Clearly there is a need for a total restructuring of thinking on world economic matters, yet we are dealing with current problems on the basis of the marginal concepts of a by-gone era when energy was cheap and world decision making was concentrated in the hands of a few major industrialized countries. New ideas and bold initiatives are clearly lacking.

Nowhere are the contradictions of the current crisis more apparent than in the IMF. It seems to be facing a real identity crisis. The Fund still lays emphasis on the need to fight inflation and adjustment, yet its orthodox prescription of demand deflation, exchange rate devaluation, etc., have become increasingly suspect in a world already suffering from very low growth rates and high unemployment. Its critics are no longer just the far left, but also include many individuals of a much more central persuasion.

The Managing Director of the Fund knows that he needs to make the IMF more attractive to developing countries if it is to take the more active role in world finance that is being urged upon it by many industrialized countries and their commercial bankers. Thus, the Fund now publicly recognizes that the adjustment process can be prolonged, that domestic social objectives should be respected and that adjustment should consider the "supply side". However, many aspects of this new approach are mentioned only in a second breath, and remain ill-defined, making critics take a wait-and-see attitude. Meanwhile, as the Managing Director attempts to improve its image with the developing countries, he must look over his shoulder at those who are inclined toward the old Fund philosophy, and who openly show their concern about, or opposition to, the new liberal tone. The opposition includes not only the old guard in the Fund staff, but some important industrialized countries and business-financial interests. As examples of the type of opposition the Fund encounters, it can be stated that the Governor of Germany expressed his continued faith in the need to adjust via demand restraint and he cautioned about moving too fast in reforms; the Governor of England also expressed the importance of demand management in adjustment and noted his concern for trends that would convert the IMF into an aid organization; and the Financial Times in its editorial of September 30 worried that the Fund's new liberal approach to conditionality would be a potentially highly inflationary solution to the balance of payments adjustment problems.

The World Bank on the other hand, appears to be much better placed to cope with the situation. In contrast to the Fund's hard-nosed image, the World Bank is the "good guy" and everyone has something nice to say about McNamara. The Bank has long been involved in the supply side of the development equation and the new focus on structural problems and supply constraints in the adjustment process should not represent uncomfortable terrain for the Bank. Indeed, even the new Structural Adjustment Facility is just an outgrowth of its earlier "program lending", so the question here is not so much how to lend for structural adjustment, but rather where the additional resources can be secured. And the additional resources are crucial to having the Bank make a significant impact on current financing of balance of payments deficits; their project loans encounter enormous delays in disbursement and the amount of rapidly disbursable resources now available for structural adjustment is rather small, representing only about 800 million dollars this year.

Even assuming the Bank and Fund substantially increase their resource base, it is clear that for Latin America in the immediate future the two institutions will remain only catalysts for other resources that will be derived basically from commercial banks. The commercial banks will continue to mobilize most of resources for developing countries on the short, medium and long term spectrums, with their confidence presumably being boosted by a somewhat greater profile for the Bretton Woods Twins. The real question -if the international economic picture remains gloomy- is just how much lending from the Twins is needed to maintain the confidence of the commercial banks, and assuming that the commercial banks do lend, then, under what terms and conditions will their finance be brought forth. Also, one must be concerned about the reaction of the commercial banks should a big borrower, e.g., Brazil, suffer an open crisis due to the weight of its debt service (For an excellent analysis of possible senarios for the 1980s -some of them very gloomy- with regard commercial banks' response to developing countries deficits, see the September 1980 issue of Morgan Guaranty's World Financial Markets).

During the meetings, the Latin American delegation (via speeches of Argentina and Colombia) expressed its concern about protectionism. It also warned against potential regulation of international lending; understandably it wants to preserve the rather free-wheeling environment of the Eurocurrency market. Nevertheless, the industrialized countries seem to strongly favor more intense supervision of their commercial banks.

There were some proposals aired during the meetings concerning an international credit insurance affiliate at the World Bank or IMF, to guarantee commercial bank loans to developing countries. This is not unsimilar to the Brandt Commission proposal for a credit insurance program for borrowing in bond markets. Personally I am skeptical about insurance schemes because I think they enmesh international institutions too closely in the affairs of private commercial and institutional lenders, reducing the plurality in the sources of world finance. I continue to think it is more reasonable to adjust legislation so that both the IBRD and Fund can better tap directly resources in foreign capital markets, thereby acting as more important low cost intermediaries for developing countries.

Other comments

(a) The human factor

I found very little human element in the environment of the Meetings Everyone discussed inflation, adjustment, and deficits, but there seemed to be little awareness that underlying the issues were people, many of whom were in a marginal state of existence in developing countries. By attending the Meetings, one realizes how "seco" economics, and finance in particular, can be. The outstanding exception to this was McNamara's commentary, which argued that growth and basic needs are not contradictory objectives, but the very essence of development. Anyone interested in economic development should read pages 17-28 of his speech; it helps to put current problems in a more dramatic and humane perspective. Two other eloquent speeches that I think merit attention are the opening remarks of Chairman Amal of Tanzania and the presentation of Hugh Small of Jamaica; they highlight the frustrations and dilemmas of small countries which are seeking to pursue unconventional development strategies during a world economic crisis.

(b) The Brandt Commission

The Commission's report was "reborn" in the Joint Meetings. Its proposals were constantly being aired and reviewed in favorable light in many of the official presentations of developing and industrialized countries. An important exception, however, was the U.S., which refrained from commenting on the report.

(c) Controversy

Aside from the PLO, there were other political issues that entered the Meeting. Vietnam complained that the IBRD has reneged on its commitments to lend to that country (McNamara has reportedly been pressured by the U.S. Congress on this matter); Iran claimed that the IMF overlooked the U.S. freeze of its assets, in violation of its Articles of Agreement; and it has been claimed in some circles that many key rules were twisted in order to have China quickly admitted to the Fund and Bank. Some also have questioned GNP estimates of China which have made the country an IDA client.

(d) The U.S. position

President Carter strongly warned that politics should not enter the affairs of the Bank and the Fund, in obvious reference to the PLO issue. Meanwhile, Secretary Miller gave a speech which was one of the most supportive among the industrialized countries for the new initiatives at the Bank and Fund. He was, however, very much against an SDR link, which represents a serious obstacle to any future progress in this area.