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How Helpful is Compensatory Financing?

by Marie Hulsman-Vejsová, Rotterdam *

In INTERECONOMICS, No. 11/12, 1977, Klaus-Peter Treydte discussed the European Communities' "STABEX" system for export earnings stabilisation. The following contribution compares Stabex with the Compensatory Financing Facility for IMF member countries.

Two international arrangements provide for loans or grants to developing countries faced with a sudden fall in their export earnings. These arrangements are:

☐ STABEX, an EC scheme available to the 52 countries in Africa, the Caribbean, and the Pacific (ACP) associated with the EC countries in the Lomé Convention, and

☐ the Compensatory Financing Facility (CFF) for IMF member countries; these countries have reached an understanding that the 26 Fund members classified as industrial countries or oil exporters will abstain from using CFF.

STABEX and CFF, in their present form, have been operating since the beginning of 1976. Recently, data on their first year of operation became available, allowing a first analysis of the schemes' practice. Experience with both instruments is undoubtedly useful for the present-day search for solutions to (export) problems of developing countries.

The Provisions of the Schemes

In principle, STABEX works as follows. For the exportation of 12 products (product groups) from individual ACP countries to the EC, trend earnings are specified, calculated as a moving average of the export earnings realized in the four years preceding the year of application. If the actual earnings in trade with the EC fall behind the calculated ones, the ACP country concerned may apply for a compensation, provided that the exports of the product involved represent a certain minimum proportion (7.5 %) of the country's total export earnings in the past, and the difference between actual and calculated earnings exceeds an agreed share of the latter (7.5 %). In that case, the application will be considered by the EC Commission in conjunction with the ACP country in the light of that country's overall trade performance. If the application is admitted, the country will obtain a loan equal to the full difference between the calculated and the actual earnings. For the poorest countries, both percentages are 2.5; they receive the compensation in the form of grants. The Lomé Convention sets a limit to the amount of compensations transferable per year. It describes fairly precisely what statistics are relevant for STABEX, and under what conditions transfers will be disbursed and repaid. STABEX started working in 1976, when it was applied to export earnings of 1975.

CFF was established by the IMF as far back as 1963, but it was not until its conditions were liberalized by the Executive Board Decision No. 4912 (75/207) of December 1975 that substantial assistance to IMF members could be given. While increasing the amounts available, that decision did not alter the logic of the facility, which can be described as follows.

The shortfall in export earnings on which the compensation is based, is the amount by which total export earnings in the shortfall year stay below the average export earnings in the five-year period centered around the shortfall year. To calculate the shortfall, export earnings in two post-shortfall years must be forecast; the 1975 decision discarded previously applied forecasting limits, so that the calculated shortfalls could increase. IMF members can draw a portion of the calculated shortfall not exceeding a specified percentage of their IMF quota within a 12-month period (50 % at present, 25 % before December 1975). Moreover, there is a ceiling on outstanding drawings (raised from 50 % of the quota to 75 % in December 1975). Finally, the 1975 decision enables members to acquire their compensation at a shorter delay: data for up to six months of the shortfall year can now be estimated. The 1975 decision did not affect the validity of two provisions; first, for shortfalls to qualify for compensation they must be temporary and largely beyond the control of the member involved; second, the country must have a balance-of-payments deficit, and has to cooperate with the IMF to find ways to overcome its difficulties in that respect.

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Table 1

STABEX Transfers and CFF Drawings on Account of 1975 Export Shortfalls

Country	STABEX transfers			CFF drawings						
	Amount millions of US dollars	Share in merchandise exports 1975 a %	Share in exports of commodity concerned 1974 b %	Amount millions of US dollars	Share in merchandise exports 1975 a %	Share in balance-of-payments deficit 1975 %	Yearly allowed maximum attained	Overall allowed maximum attained	Income group d	Export group e
Argentina				127.3	4	10			V	C
Australia				380.8	3	78	x		V	C
Bangladesh				44.8	14	8			I	A
Barbados				4.1	4	12			V	A
Benin *	8.8	26	25 (groundnuts) 27 (cotton)						I	A
Burundi *	1.8	6	33 (hides) 63 (cotton)						I	A
Cameroon	4.4	1		20.0	4	13	x		II	A
Central African Empire *	.5	1		6.0	13	29			II	A
Chad				7.5	13	14	x		I	A
Chile				90.5	6	16	x	x	IV	B
Congo	9.1	4		7.5	3	21 c	x		III	A
Cyprus				14.9	10	40	x		V	A
Dominican Republic				24.8	3	41	x		III	B
Egypt				107.7	7	8	x	x	II	B
Ethiopia *	17.7	7	15 (coffee) 27 (hides)						I	A
Fiji	.8	½							IV	A
Ghana	6.4	1	11 (timber)						III	A
Greece				66.9	3	7			V	B
Guyana				11.6	3	50	x		III	A
Iceland				13.3	4	10	x		V	A
Israel				74.7	3	3	x		V	B
Ivory Coast	18.4	2		30.1	3	10	x		III	B
Jamaica				30.6	4	11	x	x	V	A
Kenya				27.5	5	15	x		I	A
Korea, Rep. of				45.8	1	2	x		III	C
Laos, P.D.R.				3.7	...	...			I	...
Malaysia				106.8	3	57	x		III	C
Mali *	.9	1							I	A
Mauritania				7.5	4	17	x		II	A
Mexico				213.5	6	5	x		IV	C
Morocco				65.1	4	12	x		II	B
New Zealand				116.6	5	8	x	x	V	B
Niger *	7.3	9	39 (groundnuts) 20 (hides)						I	A
Pakistan				103.6	10	10			I	B
Panama				20.8	6	14	x		IV	A
Papua New Guinea				11.5	...	...	x		III	...
Peru				70.3	5	4	x		III	B
Philippines				89.2	4	10	x		II	C
Portugal				67.0	3	9	x		V	B
Romania				109.4	...	...	x		IV	...
Sierra Leone				14.4	11	23	x		I	A
Somalia *	2.4	3	12 (bananas) 33 (hides)						I	A
South Africa				184.6	2	8	x		V	C
Sri Lanka				18.2	3	17			I	A
Sudan *	2.0	½	16 (hides)	30.5	7	7			II	A
Tanzania *	2.3	1		24.2	6	10	x		I	A
Thailand				76.9	4	13	x		II	B
Togo *	3.3	3	39 (coffee)	8.6	7	253	x		II	A
Turkey				43.4	3	2			III	B
Uganda *	2.1	1		23.0	9	117	x		II	A
Upper Volta *	1.1	2							I	A
Uruguay				30.0	8	15			V	A
Viet Nam, S.R.				35.9	...	...	x		I	...
Western Samoa *	.3	3		1.2	9	105			II	A
Yemen, P.D.R.				2.9	3 c	2	x		I	A
Zaire				65.4	8 c	83	x		I	A
Zambia				21.8	3	4			III	A
Total	89.6			2,702.4						

Source: Commission of the European Communities, Report on the functioning of the system for stabilising export income introduced under the Lomé Agreement for the Financial Year 1975, Com(76)656, Brussels, Dec. 9, 1976. IMF International Financial Statistics, various issues 1976, 1977; IMF Survey, March 7, 1976. STABEX transfers and CFF drawings converted in US $ at the average exchange rate of EC unit of account and SDR in the month of transfer and drawing respectively. Export data available in US $ in IMF balance-of-payments statistics.

* Countries receiving STABEX transfers as grants. a For Burundi, Cameroon, CAE, Niger and Upper Volta share in exports of goods and services. Benin exports for 1974. b As given in Commission of the European Communities, Report on the functioning of the system for stabilising export income introduced under the Lomé Agreement for the Financial Year 1975, Com(76) 656, Brussels, Dec. 9, 1976. c Share in balance-of-payments surplus. d As defined in tables 2 and 3. e As defined in table 4.

A short review of the differences between STABEX and CFF seems in order. While STABEX relates to earnings from exporting particular goods to particular countries, CFF relates to total export earnings. Under STABEX, transfer amounts are based only on shortfall, while the amounts of CFF drawings are determined besides shortfalls, by the quotas of the members applying. To qualify for a CFF drawing, a country must have a balance-of-payments deficit and has to cooperate with the IMF in its balance-of-payments policy; both conditions are absent in the case of STABEX. For STABEX use, the normative trend value is calculated from data of the past only; estimates of CFF shortfalls involve the forecasting of future earnings. CFF drawings are loans at a rate of interest of 4 % for the first year, to be increased annually by 0.5 % until it reaches 6 % in the fifth year; STABEX transfers are free of interest and, in some cases, need not be repaid. The total amount allocated to STABEX is fixed (375 mn units of account, which is about US $ 450 mn, for five years); CFF allocation has not been bound to a maximum so far. Potential beneficiaries are 52 ACP countries for STABEX, and 103 countries in the case of CFF (IMF members other than industrial and oil-exporting countries).

The Schemes at Work

In the text and the four tables given below, "STABEX transfers" stand for payments made available to 18 ACP countries in July 1976, with occasional supplements in October 1976 and February 1977, to compensate them for their setbacks in export earnings experienced in 1975. In analogy, "CFF drawings" represent compensatory financing transactions realized since the 1975 liberalization, more particularly between February 3, 1976, and February 7, 1977, by 48 member countries of the IMF that had experienced shortfalls in 1975. The countries concerned and the amounts involved are listed in table 1. The amounts have been converted into US dollars for the sake of comparison; STABEX transfers are normally expressed in accounting units of the EC, CFF drawings are in terms of SDRs.

Amounts

For the majority of recipient countries, STABEX transfers and CFF drawings represent between 3 and 10 % of total export earnings in 1975.

The CFF drawings of 1976 were a multiple of previous CFF drawings. The upsurge has largely been made possible by the 1975 liberalization: if the rules prevailing until 1975 had remained in force in 1976, the amount drawn in that year would have been SDR 0.5 bn instead of SDR 2.3 bn, i.e. about a fifth of the actual 1976 level. The elimination of the forecasting limit alone is estimated [1] to have raised the level of drawings by SDR 1.5 bn; the increase in quota limits is supposed to account for a further increase of SRD 1.2 bn. Combined, the two types of adaptation have led to an increase in maximum drawings of SDR 1.8 bn.

The total disbursement under CFF is about 30 times larger than that involved in STABEX. One should bear in mind that CFF drawings are financed from the IMF's own resources, while STABEX transfers form part of the financial assistance to which the nine EC members have committed themselves towards the ACP countries under the Lomé Convention. More than half the STABEX transfers (those to countries marked with an asterisk in table 1) are grant transfers.

Beneficiaries

Sixteen of the STABEX beneficiaries are developing countries from Africa South of Sahara, two are countries of the Pacific. Countries profiting from CFF drawings are spread over all five continents: six European countries, seventeen countries in Africa, ten in Latin America, eleven in Asia, and four in Oceania. Some of the CFF recipients, even if they are not industrial or oil-exporting countries, can hardly be considered developing countries (Australia, New Zealand, South Africa, Iceland). Nine out of the 18 STABEX beneficiaries have made use of the CFF as well.

Commodities Involved

Nearly half of all STABEX payments referred to timber; it was followed in importance by coffee, cotton, hides, and groundnuts. Shortfalls in the exports of bananas, cocoa, copra oil, and oil cake were also compensated for.

The EC Commission interprets the STABEX payments as an insurance of the ACP states against two risks, one comparable to unemployment, the other to illness. In analogy with "insurance against unemployment", the EC has compensated losses caused by low demand for goods to be imported in the EC countries, due to economic recession. Payments relating to products hit by recession (timber, hides and skins, cotton) constituted 68 % of all compensatory payments pertinent to 1975. As an "insurance against illness", STABEX has alleviated losses caused by natural disasters in the production of export commodities; such payments have accounted for the remaining 32 % of the total (poor harvests due to disease, drought, storm, etc.). Table 1 shows that STABEX transfers have indeed been important in proportion to the proceeds derived from exporting the particular product to all destinations.

[1] IMF Survey, March 7, 1976.

Table 2

Distribution of STABEX Transfers and CFF Drawings for 1975 over Recipient Groups of Countries with Different GNP per capita

Recipient group of countries a	STABEX transfers				CFF drawings			
	Number of countries	Group's share in total recipient population %	Group's share in total STABEX transfers %	Average transfer per capita US dollars	Number of countries	Group's share in total recipient population %	Group's share in total CFF drawings %	Average drawing per capita US dollars
All recipient countries	18	100 =	100 =	0.71	48	100 =	100 =	3.55
of which: with a per capita GNP of		(126. million)	(US $ million 89.6)			(760. million)	(US $ million 2,702.4)	
I. less than $ 200	8	55	47	0.61	11	36	13	1.28
II. $ 200 – $ 374	6	31	14	0.32	11	24	16	2.42
III. $ 375 – $ 699	3	13	38	2.10	10	16	14	3.08
IV. $ 700 – $ 999	1	1	1	1.35	4	12	16	4.65
V. $ 1000 and more	0	0	0	0	12	12	41	11.75

Source: World Bank Atlas 1976 and table 1.

a Income group classification based on 1973 GNP figures of World Bank. Income brackets chosen in accordance with OECD, Development Cooperation, 1976 DAC Review.

Table 3

STABEX Transfers and CFF Drawings for 1975 in Relation to Total Balance-of-Payments Deficits of Recipient Groups of Countries with Different GNP per capita

Recipient group of countries a	STABEX transfers			CFF drawings b		
	Group's transfers	Group's total balance-of-payments deficit	Group's transfers as per cent of its total balance-of-payments deficit	Group's drawings	Group's total balance-of-payments deficit	Group's transfers as per cent of its total balance-of-payments deficit
	millions of US $		%	millions of US $		%
All recipient countries	89.6	1,583.8	6	2,541.9	28,076.4	9
of which: with a per capita GNP of						
I. less than $ 200	42.3	597.9	7	308.5	2,426.2	13
II. $ 200 – $ 374	12.7	665.1	2	435.7	4,171.2	10
III. $ 375 – $ 699	33.9	304.8	11	362.1	6,432.6	6
IV. $ 700 – $ 999	.8	16.0	5	324.8	4,766.0	7
V. $ 1000 and more	0	0	0	1,110.8	10,280.4	11

Source: See table 2.

a See note a of table 2. b Laos, Papua New Guinea, Romania and Vietnam not included in the analysis of tables 3 and 4, due to the lack of recent trade data for these countries.

Table 4

Distribution of CFF Drawings for 1975 over Recipient Groups of Countries with Different Share in World Exports

Recipient group of countries	Number of countries	Group's share in total recipients exports %	Group's share in total balance-of-payments deficit %	Group's share in total CFF drawings %	Average drawing per country millions of dollars	Group's drawings as per cent of its balance-of-payments deficit %	Group's share in exports of non-industrial non-OPEC countries %
All recipient countries	44	100	100	100	57.8	9	48
of which: with a share in world exports of							
A. less than 0.1 %	24	12	13	18	19.0	13	6
B. 0.1 % – 0.24 %	13	31	47	37	72.1	7	15
C. 0.25 % and more	7	57	40	45	164.0	10	27

Source: GATT, International Trade 1975/1976, Geneva 1976 and table 1.

Forty-two out of the 48 members that used the CFF experienced shortfalls with respect to 12 commodities (copper, wool, beef and veal, cotton, rubber, timber, sugar, tin, alumina and bauxite, phosphate, jute and products, coconut products). The IMF estimates[2] that its 42 members have drawn a total amount under the CFF which represents almost two thirds of the cumulative sum of the shortfalls suffered by them in the 12 commodities mentioned. The 42 members accounted for over half the value of world trade in these commodities.

Evaluation

STABEX and CFF are policy instruments for short-term stabilization of export earnings. Though they are not primarily meant to be devices of development assistance, they do have as an indirect aim the acceleration of economic growth of developing countries[3]. CFF in particular is geared to short-term balance-of-payments difficulties of IMF members, which it should help to overcome. Thus, the evaluation of STABEX and CFF impact should be ideally based on information about, among other things, the spending of the transfers and drawings in the recipient countries, and the influence of that spending on, e.g., the continuity of economic development, growth, income of exporters, future exports, and balance-of-payments situation. Such information is not (yet) available. Therefore, an evaluation at this stage necessarily has to be confined to relating STABEX and CFF disbursements to income levels, population, exports, and balance-of-payments deficits of the recipient countries. This is done in the following.

Distribution by GNP per capita

STABEX and CFF recipients have been distinguished into five groups, according to their per capita GNP. For each group, the share of its population, and the share of its transfers and drawings in the respective STABEX and CFF total disbursements, have been specified, along with average disbursement per capita. The results of the exercise are given in table 2; they support the following points.

More than half of the STABEX transfers have indeed been allocated to countries with a per capita GNP of less than US $ 200, the group that also represents nearly half the population in STABEX recipient countries.

The distribution of CFF transfers among the five groups corresponds roughly with the distribution of the population among these groups, with the exception of the lowest and highest groups: the lowest income group was the most populous and obtained the smallest share; the group of countries with a per capita GNP of US $ 1000 and more acquired 40 % of CFF drawings, while representing only 12 % of the population in the CFF recipient countries.

Average disbursement per capita was higher under CFF than under STABEX, though still low in absolute terms.

Relations to Balance-of-Payments Deficits

STABEX transfers and CFF drawings, as a percentage of balance-of-payments deficits of individual recipients, can be seen in table 1. In addition, the recipient countries of STABEX and CFF have again been distinguished into five groups according to their per capita GNP, and for each group the sum of individual balance-of-payments deficits has been related to STABEX transfers and CFF drawings, respectively (see table 3).

CFF drawings are larger, in relation to balance-of-payments deficits, than STABEX transfers, except for countries having per capita GNPs of between US $ 375 and US $ 699. For countries in the lowest income group, CFF drawings represented about one eighth of their balance-of-payments deficits. Table 1 reveals for thirty-five out of the 48 CFF beneficiaries, CFF drawing attained its yearly allowed maximum, while still representing only a small proportion of the balance-of-payments deficit in the majority of the 35 cases. As the IMF does not publish data on estimated shortfalls that individual drawings are supposed to meet, one cannot say what proportion of shortfalls they cover. Neither can one trace how far drawings are based on shortfall estimates, how far on IMF quotas. From the IMF estimate cited[4] one infers that two thirds of the shortfalls calculated for selected commodities and selected countries were covered by the drawings.

The CFF should also be evaluated from the point of view of its contribution to a more balanced international trade. The countries with a large international sector might find themselves in need of large amounts, in an absolute sense, to finance their balance-of-payments deficits. The IMF quota system, which decisively influences the distribution of CFF drawings, does take into account the countries' participation in international trade. The result of such an evaluation, given in table 4, confirms the following observation.

On an average, the higher a country's exports, the more it has drawn under CFF. The shares in total exports, in the total of balance-of-payments deficits, and in CFF drawings of the groups formed according to export performance of CFF re-

[2] IMF Survey, March 7, 1976.

[3] See, e.g., Article 16 of the Lomé Convention, and Executive-Board Decision No. 4912 – (75/207) of December 24, 1975, Par. 1.

[4] IMF Survey, March 7, 1976.

cipients show a fairly consistent pattern. Note that the group of countries with rather low exports saw a greater proportion of their balance-of-payments deficits covered by CFF drawings than the other two groups.

Final observations

☐ STABEX, in its first year of operating, seems to have been mainly oriented towards the development needs of individual participating developing countries, witness the distribution of transfers among income groups of countries, the terms of transfers, and their financing. The CFF 1976 practice can be explained better in terms of striving for a balanced international trade by providing financing to primary exporters who experience a balance-of-payments deficit, in relation to their participation in international trade. Both arrangements can be said to have contributed towards their respective targets.

☐ The schemes have been criticized on a number of grounds. E.g., STABEX total disbursement has been found limited indeed. Emphasis in STABEX on trade in primary commodities with the EC might discourage domestic processing and regional trade. Only the ACP countries benefit from STABEX. With respect to CFF, trade in services is not taken into account in the calculation of shortfalls. Even after the December 1975 liberalization of terms, shortfalls do not relate to real export earnings. Actual drawings remain a part of the shortfalls as calculated by the IMF now, as only that part of the shortfall can be drawn which does not exceed a certain share of a country's IMF quota.

Such criticisms are valid. To meet them, the funds involved in the financing of STABEX and CFF would have to be increased substantially.

At present, STABEX transfers and CFF drawings compare with some selected capital flows as follows. CFF in 1976 is about one fourth of that year's medium-term Eurocredits to non-oil-exporting developing countries [5]), and more than one tenth of the net flow of private capital from DAC countries to developing countries and multilateral agencies in 1975 [6]). STABEX 1976 transfers represent about 2 % of the total recorded net flow of resources to Africa South of Sahara from DAC countries and multilateral agencies in 1975 [7]).

☐ For all their imperfections and limitations, the two schemes did work in 1976. The ACP countries benefiting from STABEX publicly stated their satisfaction with the scheme [8]). These facts are worth stressing. The 1976 practice seems to support the notion that stabilization of export earnings is an operational instrument at the disposal of the international community, and it justifies further efforts for a workable expansion of the schemes in the future.

[5] IMF Survey, April 4, 1977.

[6] OECD, Development Cooperation, DAC 1975 Review, Paris, November 1976.

[7] ibid.

[8] Communiqué of the Second Meeting of the ACP-EC Council of Ministers, April 13 and 14, 1977, Suava, Fiji.

WASTE MANAGEMENT

Relaxing the Limits to Growth

by André van Dam, Buenos Aires *

The following contribution is essentially based on the author's presentation to the Club of Rome's recently held world conference on "Alternatives to Growth". Dealing with the concept of waste management and its economic and social implications it is meant to stimulate the debate on the limits to growth into an altogether different avenue.

The common thread running through this paper is that the world can afford sustained economic growth to the extent that it manages waste in manufacturing, distribution and consumption. Waste management can reduce physical constraints which hamper economic expansion – in the human environment as well as in the supply of energy, and other critical or scarce resources. In addition, waste management can be instrumental in reducing ethical barriers to sustained economic expansion.

Waste management is envisioned as an agent to change the motivation and direction of economic growth – not necessarily its speed. Waste management is therefore not perceived as an alternative to growth. This is the quintessence of the thesis – which rests upon economic quantifications as well as upon moral considerations.

* Director of planning for Latin America of a US multinational corporation.