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An Agenda for the Interim Committee

When the Interim Committee of the International Monetary Fund meets this month in Libreville (Gabon), members will have on their agenda the financial situation of the developing countries after the second wave of oil-price increases. In 1981 the OPEC surplus is projected to diminish to roughly \$ 80 bn (from \$ 115 bn in 1980). Yet, in spite of this global relaxation the current-account deficit of the non-oil developing countries may well increase from \$ 50 bn to about \$ 60 bn. What are the chances of its being financed?

Contrary to earlier predictions commercial banks have greatly expanded their lending to the Third World. From the beginning of 1979 to end-September 1980, the latest date for which comprehensive figures are available, their net claims to non-oil developing countries, excluding offshore financial centres, increased by \$ 53 bn to \$ 103 bn. This compares with a current-account deficit of \$ 87 bn in 1979/80. The flow of finance from private and official sources enabled the developing countries not only to cover their deficits but to further augment their exchange reserves by roughly \$ 20 bn.

Is the warning of an imminent liquidity shortage of non-oil developing countries simply much ado about nothing? A second look reveals that again, as after the first oil price increase, it was only a small and privileged group of newly industrialising countries which, heavily indebted as they already were, have been able to draw on the highly liquid financial markets: \$ 94 bn, equal to 92 % of the banks' total net claims to developing countries, are accounted for by only five countries (Brazil, Mexico, Argentina, South Korea and Yugoslavia). In contrast to them, low-income countries were net *creditors* to banks to the tune of \$ 3 bn. It is with these countries which, because of their poor growth and export prospects, have practically no access to the private financial markets, that the IMF is mainly concerned.

That there is a demand for more IMF financing is demonstrated by the fact that the Fund in 1980 has tripled its credit commitments compared to 1979 and 1978 to a total of \$ 9.5 bn. The possibility that the commitments have to be honoured, and the exhaustion of the Witteveen facility, had the IMF seek additional finance from its wealthier member countries. The response has been far from enthusiastic. It is ironical that the ability of the IMF to fulfil its tasks should, in the face of highly liquid international financial markets, depend on the willingness and ability of a few countries to increase its resources. A major policy change as regards the supplementary financing of the IMF – over and above the regular quota financing – is therefore called for.

On the liabilities side the Fund should operate more like a commercial financial institution. This implies that it should, depending on the amounts and maturities involved, make use of money-market instruments, raise medium-term syndicated loans and issue long-term bonds. In parallel to this the Fund may wish to offer its member countries investment outlets for their surplus liquidity. However, under a consistent market approach the IMF would no longer *apply* for funds from its member countries but *offer* them an opportunity to invest, on competitive terms, which member countries could accept or decline at will. The cost of such financing would be only marginally higher than under the traditional – and apparently still preferred – approach. The small cost disadvantage would be compensated for by benefits in the form of more financial flexibility and reduced exposure to political blackmail.

As to the Fund's terms of lending, the Group of 24 has demanded that financial assistance to developing countries should be given with minimum conditionality. Up to now, the Fund has largely resisted this demand. Indeed, the present situation is not calling for less adjustment but for more. And it is only appropriate that the Fund should pay regard to its members' adjustment policies. It is true, the course of this policy, and the nature of conditionality, must take account of the fundamental changes that have taken place in the world economy. In view of the partly exogeneous causes of national balance-of-payments deficits the traditional demand-oriented adjustment concept is to be supplemented by supply-oriented policies. Moreover, the time horizon for adjustment has lengthened under the impact of the continuing OPEC surplus. The IMF has already responded to the changes in the world economy. It is now proceeding on a narrow path between the "financing for adjustment", with longer adjustment periods, and "financing for development" which does not fall within its proper scope. The importance attached to conditionality by major industrialised countries will be the more credible, however, the more they are prepared to honour efforts of developing countries to adjust their external economies by allowing imports from developing countries to increase.

Another approach highly favoured by developing countries is substantial allocations of SDRs in the years to come. Their demand is for the creation of SDR 10 bn p. a. over the five-year period 1982-86, and they can count on wide-spread political support of OPEC and many industrialised countries. Indeed, the standard counter-argument – the inflationary impact of massive SDR creation – is less convincing under present conditions of world-wide capacity under-utilisation than in a boom situation. Excessive SDR allocation may however be counter-productive to the objective of making the SDR the primary international reserve asset; the preparedness of reserve-rich countries to purchase SDRs from deficit countries and thus to monetise the SDR could well suffer.

It should also be considered that the larger the amount of annual SDR allocations, the shorter the allocation period will have to be. Massive liquidity creation can, if at all, only be justified by the present OPEC surplus and the resultant deficit of the rest of the world. While this deficit may well persist for many years, this is by no means certain. A five-year allocation period is therefore only acceptable if allocations are modest. Otherwise a new decision will have to be made after three years at the latest, in the light of the then prevailing circumstances.

More fundamentally, the question is legitimate whether there is indeed a global liquidity shortage as the developing countries allege. Evidence rather points to the opposite. If, as is plausible, only the non-oil developing countries are suffering from such a shortage, creation of an aggregate volume of SDRs which is consistent with their needs, would be far too much from a global point of view. It should be remembered that non-oil developing countries receive no more than about 25 % of the total allocation, so that to satisfy a perceived need of, say, SDR 2.5 bn, a total volume of SDR 10 bn would have to be created. This amount could be greatly reduced if the developed and OPEC countries were prepared to transfer (part of) their own SDR allocations to the World Bank and the IMF to finance long-term adjustment programmes. This is not to argue for a formal link between SDR creation and development financing, but for a flexible response to the current extraordinary global economic situation. As SDRs are created *ex nihilo*, balance-of-payments assistance could be given in the form of conditional grants, with repayment obligations arising only in the case of major deviations from the agreed performance criteria. It would be desirable that all major industrial and OPEC countries participated in such a move. Pending agreement, however, individual countries could start on their own transferring half or more of their – previous and/or future – allocations, thereby setting an example to others.

The developing countries' deficit, and in particular the deficit of the low-income countries, is indeed giving rise to concern. Yet there are avenues to give relief in a pragmatic and effective way without overstraining the preparedness of major IMF member countries to co-operate, or further disrupting the international financial system.

Hans-Eckart Scharrer