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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 87/107

2:30 p.m., July 23, 1987

M. Camdessus, Chairman  
R. D. Erb, Deputy Managing Director

Executive Directors

A. Abdallah  
C. H. Dallara  
A. Donoso  
  
J. E. Ismael  
A. Kafka  
T. P. Lankester  
M. Massé  
Mawakani Samba  
Y. A. Nimatallah  
G. Ortiz  
J. Ovi  
H. Ploix  
G. A. Posthumus  
C. R. Rye  
  
A. K. Sengupta  
K. Yamazaki  
S. Zecchini

Alternate Executive Directors

E. T. El Kogali  
Song G., Temporary  
  
J. Prader  
E. Feldman  
A. M. Othman  
B. Goos  
  
  
L. P. Ebrill, Temporary  
L. Filardo  
M. Fogelholm  
  
  
O. Kabbaj  
L. E. N. Fernando  
M. Sugita  
N. Kyriazidis

L. Van Houtven, Secretary and Counsellor  
K. S. Friedman, Assistant  
J. K. Bungay, Assistant

1. Surveillance - Use of Indicators - Analytical Issues;  
and Review of 1977 Decision . . . . . Page 3
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Also Present

IBRD: P. R. Scherer, Latin America and the Caribbean Regional Office.  
African Department: M. G. Kuhn. Asian Department: W. S. Tseng.  
European Department: M. Russo, Director; M. Guitián, Deputy Director;  
M. Z. Khan, T. M. Ter-Minassian. Exchange and Trade Relations Department:  
L. A. Whittome, Counsellor and Director; J. T. Boorman, Deputy Director;  
C. Atkinson, J. Berengaut, B. C. Stuart. External Relations Department:  
H. O. Hartmann. Fiscal Affairs Department: V. Tanzi, Director. Legal  
Department: W. E. Holder, Deputy General Counsel; A. O. Liuksila,  
J. V. Surr. Research Department: J. A. Frenkel, Economic Counsellor and  
Director; A. D. Crockett, Deputy Director; M. Goldstein, Deputy Director;  
R. R. Rhomberg, Deputy Director; M. C. Deppler, F. Larsen, P. R. Masson.  
Secretary's Department: C. Brachet, Deputy Secretary. Treasurer's  
Department: R. A. Feldman. Western Hemisphere Department: S. T. Beza,  
Director; M. Caiola, Deputy Director; H. Arbulu-Neira, C. V. A. Collins,  
D. N. Lachman, P. Neuhaus, F. van Beek. Personal Assistant to the Manag-  
ing Director: R. M. G. Brown. Advisors to Executive Directors:  
A. Bertuch-Samuels, L. P. Ebrill, A. R. Ismael, G. Pineau, I. Puro,  
D. C. Templeman, A. Vasudevan. Assistants to Executive Directors:  
N. Adachi, A. R. Al-Abdullatif, F. E. R. Alfiler, J. R. N. Almeida,  
O. S.-M. Bethel, H. S. Binay, E. C. Demaestri, F. Di Mauro, W. N. Engert,  
S. K. Fayyad, M. A. Hammoudi, M. Hepp, G. K. Hodges, S. King,  
M. A. Kyhlberg, M. Lundsager, V. K. Malhotra, R. Manfredi Selvaggi,  
T. Morita, C. Noriega, S. Rebecchini, S. Rouai, G. Seyler, H. van der Burg,  
D. A. Woodward, Yang W., I. Zaidi.

1. SURVEILLANCE - USE OF INDICATORS - ANALYTICAL ISSUES; AND REVIEW OF 1977 DECISION

The Executive Directors continued from the previous meeting (EBM/87/106, 7/22/87) their consideration of staff papers entitled "The Use of Indicators in Surveillance--Analytical Issues" (EBS/87/135, 6/24/87) and "The Use of Indicators in Surveillance--Review of 1977 Decision on Surveillance over Exchange Rate Policies" (EBS/87/136, 6/24/87; and Cor. 1, 6/29/87).

Mr. Yamazaki said that he wished it to be clearly understood that his authorities continued to fully support the positions in the latest Interim Committee communiqué and the Venice Economic Declaration. The concern that he had meant to express in his statement at EBM/87/105 was that the staff paper on analytical issues seemed to suggest that the Executive Board should agree in excessive detail on a sustainable or desirable path for the key variables and compare actual developments with the intended path. That approach was somewhat more ambitious than had been envisaged in the Interim Committee's communiqué and the Venice Economic Declaration and could introduce excessive rigidity into the Fund's surveillance procedures. As he understood it, his position was close to the positions that had been taken by Mr. Posthumus, Mr. Goos, Mr. Massé, and other Executive Directors.

The Chairman made the following summing up:

Our discussion of indicators has dealt with a subject that is at the very heart of the Fund's responsibilities. As many Directors have pointed out, strengthening the process of economic surveillance and policy coordination is central to an effectively functioning international monetary system, and was strongly stressed by the Interim Committee. The Committee's communiqué endorsed a strengthened use of indicators, in particular through the suggestion that actual policies should be looked at against an evolution of economic variables that could be considered desirable and sustainable. Subsequently, as was noted in our discussion, the Venice Economic Declaration underlined the role that the Fund could play in helping to promote a constructive use of indicators to review and assess current economic trends and to determine whether there are significant deviations from an intended course that require consideration of remedial actions.

In summarizing the discussion I will deal first with the views that were expressed on the staff paper on analytical issues in the use of indicators. Then I will turn to the questions that arise in connection with the review of the 1977 Decision on Surveillance over Exchange Rate Policies.

# 1. Analytical Issues in the Use of Indicators

In commenting on the staff's proposed analytical approach, Directors generally agreed that the focus of analysis should be on points of interaction among major economies. For this purpose, emphasis had to be given to the sustainability of balance of payments positions and of the factors underlying payments flows. A key variable, whose importance was particularly stressed, is the exchange rate. In addition, many Directors noted that in providing this focus for the Fund's surveillance activities, it would also be necessary to give appropriate consideration to the evolution of indicators of domestic policy and performance. They pointed out that a stable and sustainable evolution of domestic variables was a prerequisite of a satisfactory external position.

It was agreed that a limited list of variables should be selected for primary attention in any indicator-based approach to surveillance. However, a number of Directors observed that a full understanding of economic developments would require consideration of a wider range of variables. Therefore, the limited list of indicators that was selected for primary attention should not preclude the staff from taking into account additional indicators when this was necessary to provide a balanced appraisal of economic developments.

Directors agreed that the list of principal indicators should evolve with experience and in view of changing circumstances. A preliminary list to be focused upon in staff analysis should include the rates of growth of output and demand; unemployment; inflation rates; current account and trade balances; fiscal policy indicators; monetary growth rates; exchange rates; and interest rates. It was agreed that these indicators should be looked at for each of the major industrial countries. Interest was expressed in examining whether over time the application could be extended to a wider range of Fund members. Directors also commented on the issue of how to establish standards for the variables to be monitored, so that it might be determined whether indicators appeared to be moving outside a range that could be considered desirable and sustainable. Most speakers felt that caution was called for in this area, but that it was nevertheless possible to develop some criteria that could be helpful in judging sustainability and desirability, although it was noted that these two concepts have a different underlying rationale and have to be defined and used with appropriate care. The staff was encouraged to pursue the analysis that was sketched in its paper and to use scenarios based on alternative developments of policy and performance variables. At the same time, Directors noted the considerable uncertainties and complex causal relationships involved in such projections. They underlined the need for adjustment and for the use of a variety of alternative techniques. Several Directors also noted the importance of taking full account

of members' own views on the desirable values of key indicators for their economies. Lastly, there was a broad consensus to avoid any attempt to "fine tune" economic management.

A key aspect of yesterday's discussion has been how to develop procedures for monitoring economic indicators, and how to use monitoring techniques so as to enhance policy dialogue and policy coordination. It was agreed that the world economic outlook exercise is a critical component in the application of an indicator-based approach. The world economic outlook should provide a quantitative assessment of the implications of current policies for the evolution of key economic variables. This should be set in a medium-term framework and, where appropriate, should include alternative scenarios based on different assumptions concerning economic policies and market reactions.

These various sets of projections by the staff would become the subject matter of discussions by both the Executive Board and the Interim Committee. Such discussions should enable conclusions to be drawn concerning the expected evolution of economic variables on the basis of current policies, as well as alternative scenarios based on policies that were better or led to a more sustainable outcome. It is to be hoped that the summings up of the discussions on the world economic outlook in the Executive Board as well as discussions on the same subject in the Interim Committee would identify criteria that would permit subsequent judgments of when a significant departure from a satisfactory evolution of variables had occurred. Of course, as a number of Directors pointed out, the use of indicators in the world economic outlook has to be tied in with the use of indicators in the Fund's continuing Article IV consultation work. We shall be discussing this issue soon on the basis of a staff paper.

Concerning what to do when actual developments diverged from expected or desired developments, Directors generally favored the use of discretion by the Managing Director to judge whether the particular circumstances warranted a special review by the Fund and they did not favor introduction of automatic triggering procedures. Even where no specific discussions seemed warranted, the appraisal in each world economic outlook or Article IV consultation would be undertaken against the background of the developments expected or planned at the time of the previous assessment.

I would suggest that, for the time being, monitoring procedures be undertaken on an experimental basis. As the staff has informed us, the forthcoming world economic exercise will contain projections based on alternative scenarios of economic policies. Following our discussions of the staff papers, one possibility would be for me to draw conclusions concerning the expected evolution of policies and economic developments, and the direction of

policy changes favored by the Board. I would then ask the staff to monitor actual developments to track departures from projections that move developments further away from what the Board has perceived as the intended course. Where such deviations from projections seemed substantial I would bring the matter to the Board's attention, in some appropriate and informal fashion. We would then have the opportunity to review whether such a focus for our discussions was helpful in our surveillance function.

## 2. 1977 Surveillance Decision

I turn now to the paper on the review of the 1977 Decision on Surveillance over Exchange Rate Policies. Concerning the question of whether a new decision is necessary to update the existing 1977 document, there was a division of opinion. Some Directors viewed the existing decision as insufficiently broad to cover the range of policies that is now recognized to influence exchange rates. These Directors favored a modification of the current decision that would involve a re-interpretation of the rather restrictive present coverage of the concept of exchange rate policies. Most Directors, however, were reluctant to embark on the task of revising the current decision, in view of the uncertainties involved in the application of indicators, especially those regarding domestic policies and performance. They preferred instead to think in terms of a separate decision providing guidance to members on the conduct of policies that had substantial indirect effects on exchange rates and payments flows. Concerning the timetable for a new decision, most Directors felt that it was premature to attempt to agree on specific language, before more experience had been gained in the practical use of indicators.

Lastly, I would remind the Board that we are asked to submit a "progress report" to the Interim Committee concerning our work on indicators. I would forward this summing up, together with a summary of views expressed on the application of indicators in the world economic outlook discussion, to the Interim Committee.

Mr. Goos noted that the Chairman had mentioned that some interest had been expressed in extending the coverage of the indicators over time beyond the major industrial countries. In his view, it would be useful and desirable to include as many countries as possible in the exercise; however, for practical reasons, the effort to do so would have to begin with a limited list consisting of the more important countries.

The Chairman remarked that the majority of Executive Directors seemed to feel that there was little justification in carrying the indicators analysis beyond the major industrial countries. It was likely that, after some experience had been gained with the application of indicators to the major countries, there would be broad support for widening the application of the indicators.

Mr. Goos commented that there seemed to be widespread agreement that the application of indicators within the context of Article IV consultations would be the basis for the application of indicators in the world economic outlook exercise. Concentrating the application of indicators on only a few Article IV consultations would limit the linkage between the application of the indicators for consultations and the application of indicators under the world economic outlook exercise.

The Chairman said that the words "over time" could be eliminated from the sentence in which he had stated that "interest was expressed in examining whether over time the application could be extended to a wider range of Fund members."

Mr. Dallara noted that the Chairman had mentioned one possible way in which each summing up on a world economic outlook discussion could be handled. It might be helpful also to mention other possible ways in which to handle the summing up. A number of Executive Directors had expressed reservations about any attempt by the Executive Board to identify a particular course for the evolution of policies and economic developments. The Venice Economic Declaration included a reference to "an intended course" but did not address the institutional setting for surveillance and use of indicators, and it was not clear to him that the world economic outlook exercise was meant to be used as a means of identifying a single "intended course." Emphasis had been given to the need to use alternative scenarios, which implied a variety of courses.

The Chairman said that the text in question could read: "I would then ask the staff to monitor actual developments to track departures from projections that move developments further away from what the Board has perceived as intended courses."

Mr. Dallara responded that that change would be helpful. In addition, the Chairman had remarked that following the Executive Board's discussions of the world economic outlook papers, the Chairman could draw conclusions concerning the expected evolution of policies and economic developments, and the direction of policy changes discussed by the Executive Board. It might be best not to focus on a single direction of policy changes. If the Executive Board tried to identify a single direction of policy changes, the general objectives of the use of indicators in surveillance might not be achieved. In addition, it would be helpful to use a word other than "favored" in the same piece of text, such as "considered" or "discussed."

The Chairman said that the word "direction" in the reference to the "direction of policy changes" could be changed to "directions." In addition, the word "favored" could be replaced by "discussed," although the Interim Committee was of course entitled to favor an intended course of action, and the Executive Directors should be careful to avoid watering down the policy coordination exercise.

Mr. Dallara commented that the Executive Board certainly should not deviate in any way from the thrust of the guidance provided by the Interim Committee. However, he doubted whether the Committee had meant to suggest that the Fund should focus on a single set of favored policy changes.

As the Chairman had noted, Mr. Dallara continued, most Executive Directors had indicated that they considered that more experience was needed before an effort was made to revise the decision on surveillance over exchange rate policies. However, some Executive Directors seemed to be willing to move ahead in that area by looking at certain possible approaches to revising the decision as further experience was gained. Accordingly, the idea of eventually revising the text should not be lost.

The Chairman said that the following sentence could be added to the penultimate paragraph of the summing up: "After two world economic outlook rounds have been completed, that is to say, some time in the spring of 1988, it might be possible to proceed to the consideration of a draft decision on this subject."

The Executive Directors concluded their discussion on analytical issues in the use of surveillance and the review of the 1977 Decision on Surveillance over Exchange Rate Policies. 1/

2. ARGENTINA - 1987 ARTICLE IV CONSULTATION; STAND-BY ARRANGEMENT - EFFECTIVE DATE AND REVIEW; AND EXCHANGE SYSTEM

The Executive Directors considered the restricted staff report for the 1987 Article IV consultation with Argentina and the review under the stand-by arrangement approved in principle on February 18, 1987 (EBS/87/155, 7/8/87; Sup. 1, 7/10/87; Cor. 1, 7/23/87; Sup. 2, 7/13/87; and Sup. 3, 7/22/87). They also had before them a background paper on recent economic developments in Argentina (SM/87/162, 7/15/87).

The Executive Board then took the following decisions:

Stand-By Arrangement - Effective Date and Review

1. Argentina has consulted with the Fund as contemplated in paragraph 26 of the Memorandum of Understanding on Economic Policy, annexed to the letter dated January 12, 1987, from the Minister of Economy and the President of the Central Bank of the Republic of Argentina, in order to review the progress made in implementing its economic program and to reach understandings on additional measures, if necessary, to ensure the attainment of the program's objectives.

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1/ The final version of the summing up was subsequently circulated as SUR/87/68, 7/27/87.



2. The Fund finds that satisfactory arrangements have been made for the financing of Argentina's balance of payments needs in 1987, and that corrective policy actions are being undertaken as described in the letter of July 8, 1987 from the Minister of Economy and the President of the Central Bank of the Republic of Argentina.

3. The Fund approves the stand-by arrangement for Argentina as set forth in EBS/87/5, Supplement 3 (2/23/87) for the period from July 23, 1987 to September 30, 1988, and waives the limitation in Article V, Section 3(b)(iii).

4. Paragraphs 1 and 2(a) of the stand-by arrangement shall be amended to read as follows:

"1. For the period from July 23, 1987 to September 30, 1988, Argentina will have the right to make purchases from the Fund in an amount equivalent to SDR 1,113.0 million, subject to paragraphs 2, 3, 4, 5, and 6 below, without further review by the Fund.

2(a). Purchases under this stand-by arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 285.5 million until October 20, 1987; the equivalent of SDR 451.0 million until December 20, 1987; the equivalent of SDR 616.5 million until February 20, 1988; the equivalent of SDR 782.0 million until May 20, 1988; and the equivalent of SDR 947.5 million until August 20, 1988."

5. The letter of July 8, 1987 from the Minister of Economy and the President of the Central Bank of the Republic of Argentina shall be attached to the stand-by arrangement, and the letter of January 12, 1987 from the Minister of Economy and the President of the Central Bank and the Memorandum of Understanding on Economic Policy annexed thereto shall be read as supplemented and modified by the letter of July 8, 1987.

6. Paragraph 4(a), (b), (c), (d), and (e) of the stand-by arrangement shall be amended to read as follows:

"Argentina will not make purchases under this arrangement that would increase the Fund's holdings of Argentina's currency in the credit tranches beyond 25 percent of quota or increase the Fund's holdings of that currency resulting from purchases of borrowed resources beyond 12.5 percent of quota:

(a) during any period in which the data at the end of the preceding two-month period indicate that:

- (i) the limit on the combined deficit of the non-financial public sector and the Central Bank described in paragraph 9 and Table 2 of the attached letter of July 8, 1987; or
- (ii) the limit on the cash deficit of the nonfinancial public sector described in paragraph 9 and Table 2 of the attached letter of July 8, 1987; or
- (iii) the limit on treasury outlays described in paragraph 9 and Table 2 of the attached letter of July 8, 1987; or
- (iv) the ceiling on the net domestic assets of the Central Bank, described in paragraph 12 and Table 3 of the attached letter of July 8, 1987; or
- (v) the targets for changes in net international reserves described in paragraph 18 and Table 4 of the attached letter of July 8, 1987, have not been met; or

(b) during any period in which the data at the end of the preceding three-month period indicate that the understandings on regulated interest rates described in paragraph 13 of the attached letter of July 8, 1987 have not been observed; or

(c) during any period after November 30, 1987 in which:

- (i) the intentions regarding the elimination of external payments arrears and the avoidance of incurring new external payments arrears as described in paragraph 20 of the attached letter of July 8, 1987 have not been observed; or
- (ii) the Central Bank is not providing foreign exchange automatically at the official exchange rate for the transfer of profits and dividends, as described in paragraph 20 of the attached letter of July 8, 1987; or

(d) if Argentina fails to observe the limits on the total outstanding disbursed external debt of the public sector and the cumulative net short-term disbursements of external debt of the public sector, as described in paragraph 23 and Table 5 of the attached letter of July 8, 1987; or

(e) during any period after November 30, 1987 in which the comprehensive review referred to in paragraph 24 of the attached letter of July 8, 1987 has not been completed, or understandings on performance criteria for the remaining period of the stand-by arrangement are not reached, or performance criteria established in that review are not being observed; or"

7. The Fund finds that the review contemplated in Paragraph 26 of the Memorandum of Understanding on Economic Policy, annexed to the letter dated January 12, 1987, has been completed.

Decision No. 8653-(87/107), adopted  
July 23, 1987

#### Exchange System

Argentina maintains exchange restrictions and multiple currency practices as described in Appendix IV to EBS/87/155, Supplement 1. The Fund welcomes the intention of Argentina to eliminate the restrictions evidenced by external payments arrears and the multiple currency practice relating to profits and dividends, and encourages Argentina to further simplify its exchange system and to eliminate the remaining exchange restrictions and multiple currency practices as soon as possible. In the meantime, the Fund approves exchange restrictions and multiple currency practices of Argentina as described in parts 1 and 2(a), (b), (c), (d), and (f) of Appendix IV to EBS/87/155, Supplement 1, until November 30, 1987.

Decision No. 8654-(87/107), adopted  
July 23, 1987

DECISION TAKEN SINCE PREVIOUS BOARD MEETING

The following decision was adopted by the Executive Board without meeting in the period between EBM/87/106 (7/22/87) and EBM/87/107 (7/23/87).

3. EXECUTIVE BOARD TRAVEL

Travel by an Executive Director as set forth in EBAP/87/130, Supplement 1 (7/21/87) is approved.

APPROVED: February 8, 1988

LEO VAN HOUTVEN  
Secretary