IV

Evolution of the Institution

17

Fund Finances: Balancing Demand and Supply

THE IMF IS THE LINCHPIN OF THE INTERNATIONAL financial system. . . . I have an unbreakable commitment to increased funding for the IMF. . . . The stakes are great. This [quota increase] legislation is not only crucial to the recovery of America's trading partners abroad and to the stability of the entire international financial system, it is also necessary to a sustained recovery in the United States.

Ronald R. Reagan
President of the United States
September 27, 1983[1]

The summer of 1983 brought an unprecedented squeezing of the IMF's resources. Demand for Fund lending was at an all-time high as a result of the Fund's efforts to help countries cope with the international debt crisis. To finance that activity, the Fund's governors had agreed to a major increase in quotas and to an enlargement of the pool of resources available to the Fund through the General Arrangements to Borrow (GAB). The effectiveness of both of those increases, however, depended on their approval by the U.S. Congress, which was raising a host of political objections to it and tying it to unrelated domestic issues. The Managing Director, Jacques de Larosière, tried to get the major creditor countries to provide additional short-term loans to the Fund to cover the possibility of a liquidity shortage if the quota and GAB increases continued to be delayed. When that effort failed in September, de Larosière decided that the Fund could no longer conduct business as usual.

The venue for the Managing Director's effort to secure additional loans to the IMF was the Bank for International Settlements (BIS) in Basel, Switzerland. The governors of the BIS included the central bank governors of most of the major creditors, and the BIS would have been the natural intermediary for a short-term loan to the Fund. At the beginning of September, de Larosière was confident enough of success that he told the Executive Board that to prevent a "dramatic" and "worrying" situation from developing—in which the Fund might be unable to meet its own commitments—a loan from the BIS was "of critical importance." Two

[1]IMF, *Summary Proceedings*, 1983, pp. 4–5.

weeks later, on returning from Basel, he had to report to the Board that the talks had failed. Although he declined to elaborate on the reasons, it was clearly understood that the BIS governors did not want to take action that would make it easier for the U.S. Congress to continue to delay approving the more permanent increases in the Fund's resources.[2] A political game of cat and mouse was being played, and the Fund's liquidity was the bait.

In response, de Larosière announced that he was immediately instructing the staff not to discuss any new lending arrangements with member countries unless the credits could be financed without the use of borrowed resources. Since most arrangements at the time were drawing heavily on borrowed resources, and strict limits were in effect on the use of the Fund's own money, that decision was nearly tantamount to a moratorium on new lending. Never before had the Fund had to refuse to lend on the grounds that it was running out of money. A more dramatic circumstance could scarcely be imagined for the world's primary source of conditional balance of payments financing.

The impasse induced the president of the United States to endorse the quota increase in the strikingly strong language quoted at the heading to this chapter. Within a few months, the quota-GAB package was approved, the crisis passed, and the backlog of demand for new arrangements was soon cleared.

This episode, although unique in the history of the Fund, illustrates the institution's continuing dependence on timely quota increases. Even though the Fund has occasionally and temporarily met the rising demand for its resources by borrowing, quota subscriptions have provided its permanent assets. The process of increasing quotas, however, requires political commitments that are difficult to secure in the absence of a demonstrable crisis. Consequently, the history of the Fund's resources has taken a bumpy path, marked by long periods of declining liquidity, interrupted by sharp increases. This chapter reviews the major developments of the late 1970s and the 1980s.

Quotas and the Size of the Fund

As a financial institution, the IMF comprises three separate units: the General Department, the SDR Department, and a set of Administered Accounts. The core, and what is usually meant by the "Fund," is the General Department. The SDR Department is the subject of Chapter 18, and the Administered Accounts (such as the Trust Fund and the ESAF Trust) are examined above, in Chapter 14.[3]

[2]Minutes of EBM/83/129 (September 2, 1983), pp. 13–14; EBM/83/139 (September 14, 1983), pp. 3–5; and (on the reason for the governors' refusal to lend to the Fund) the statement by Gerhard Laske (Germany) at EBM/83/145 (October 3, 1983).

[3]For a detailed discussion of the Fund's financial accounts, see IMF Treasurer's Department (1998). Appendix I of this chapter gives an alternative presentation that consolidates the two departments and the Administered Accounts into a single table. For another alternative that stresses the potential role of the SDR in Fund operations and criticizes the Fund's liquidity concept, see Polak (1996, 1999).

The overall level of resources in the General Department more than doubled during the period covered by this History, from SDR 46 billion ($60 billion) at the end of 1978 to SDR 99 billion ($130 billion) 11 years later (Table 17.1).[4] That increase resulted almost entirely from increases in members' quotas. The other two major sources of assets—gold and borrowings—declined.[5] This pattern continued the broad pattern since Bretton Woods, in which quotas increased by an average of 5¾ percent a year (aside from the effect of the addition of new members and a few ad hoc increases, which added another 1 percent a year), but in uneven spurts rather than steadily over time (Table 17.2).[6]

A clearer picture of the "size of the Fund"—the amount of lendable resources provided to or available for member countries—is gained by netting out the stock of "currently unusable" currencies held by the Fund and other nonliquid assets. When a country pays in its quota subscription (whether as a new member or in acceptance of a quota increase), it normally pays three-fourths of the total in its own currency. Since many countries have weak balance of payments positions or have currencies that are not fully convertible, the Fund regularly reviews the status of each currency in its portfolio to determine whether it is currently usable for Fund operations. If not, holdings of that currency are excluded from the list of liquid assets. The effective size of the Fund thus varies with the overall quality and distribution of external positions. By this measure (credit outstanding plus cash and other liquid investments), the Fund's usable assets increased at an even faster rate, from SDR 16 billion in 1978 to SDR 51 billion in 1989 ($20 billion to $66 billion).[7]

The 131 percent increase in Fund quotas from the end of 1978 through 1989 reflected two rounds of increases for all members and the addition of 14 new member countries. The Seventh General Review, which took effect in 1980, raised quotas by just over 50 percent, to SDR 60 billion. The Eighth General Review raised quotas by just under 50 percent in 1983, and the total stock of quotas gradually

[4]The form of the balance sheet shown in Figure 17.1 on p. 877 differs from the Fund's own presentation in the *Annual Report*, primarily by including the distinction between liquid and nonliquid assets and liabilities. The classification of items as liquid follows the Fund's own practice for the purpose of measuring the "liquidity ratio." (The liquidity ratio was devised by de Larosière in 1980 as a ready reckoner for determining whether the Fund might need to borrow in the near future.) For further details on the balance sheet, see the relevant *Annual Report*.

[5]From 1976 to 1980, the Fund sold or distributed one-third of its stock of gold (initially 150 million ounces). Half of that amount was sold at auction, and the profits were used to finance the Trust Fund (Chapter 14). The other half was sold back to member countries at the official price (SDR 35 per ounce) in proportion to quotas; see de Vries (1985), pp. 625 and 658–59.

[6]The original Articles of Agreement provided for a review of quotas every five years. That provision was modified in the First Amendment (1969) to allow for the possibility of more frequent reviews. The first two reviews were concluded without a general increase.

[7]The category "liquid cash assets" in Table 17.1 comprises currencies, securities, and SDRs held in the General Resources Account (GRA), plus liquid deposits held in the Special Disbursement Account (SDA). The GRA and the SDA are the two principal accounts in the General Department; see IMF Treasurer's Department (1998), pp. 13–15. The sources of the GRA holdings are broadly disaggregated in the table. The SDA also held claims in the form of SAF loans, which are shown separately.

Table 17.1. Balance Sheet of the General Department
(Billions of SDRs; see text for explanatory notes)

	December 31, 1978		December 31, 1989		Change	
Assets						
Liquid cash assets		5.3		26.7		21.4
Quota subscriptions	39.0		90.1		51.1	
Less reserve tranche positions	–8.5		–22.0		(13.5)	
Less nonliquid holdings	–26.4		–43.0		(16.6)	
SDA investments			0.8		0.8	
Nonliquid cash assets		26.4		43.0		16.6
Currently nonqualifying currencies	20.8		28.6		7.8	
Undrawn credit commitments	3.2		4.3		1.1	
Required working balances	2.4		10.1		7.7	
Loans and credits		10.3		23.8		13.5
GRA credits	10.3		22.3		12.0	
SAF loans	0.0		1.5		1.5	
Receivables		0.1		1.4		1.3
Current charges and interest	0.1		0.5		0.4	
Deferred charges			0.9		0.9	
Gold (at SDR 35 per ounce)		4.1		3.6		(0.5)
Other assets		0.1		0.2		0.2
Total assets		46.3		98.7		52.4
Liabilities and Net Worth						
Liquid liabilities		14.9		25.5		10.6
Reserve tranche positions	8.5		22.0		13.5	
Borrowings	6.4		3.5		(2.9)	
Balance of quota subscriptions		30.5		68.1		37.6
SDA resources				2.3		
Other liabilities		0.2		0.4		0.2
Reserves, etc.		0.7		2.4		1.7
Ordinary reserves	0.7		1.4		0.6	
SCA			0.2		0.2	
Deferred charges			0.9		0.9	
Total liabilities and net worth		46.3		98.7		52.4
Memorandum items:						
Gold at market prices		45.9		31.6		–14.4
Unused and available credit lines	5.5		15.3		9.8	
Liquidity ratio (in percent)	36		105			

crept up by a further 4 percent as new members came on board through April 1990.[8] Over the same period, international trade increased at a comparable pace, so the rapid drop in quotas relative to world imports recorded in the 1960s and 1970s was at least interrupted.

Both the Seventh and the Eighth General Reviews brought a few large ad hoc adjustments to the quotas of individual countries. The most notable changes were the increase for China after the People's Republic began representing the country

[8]In relation to the initial stock of SDR 39 billion in quotas for 138 member countries, the Seventh and Eighth Reviews represented increases of 52.4 and 74.4 percent, respectively.

Table 17.1 ***(concluded)***
(Billions of U.S. dollars, at end-year exchange rates)

	December 31, 1978		December 31, 1989		Change	
Assets						
Liquid cash assets		6.9		35.1		28.2
Quota subscriptions	50.8		118.4		67.6	
Less reserve tranche positions	–11.1		–28.9		(17.8)	
Less nonliquid holdings	–34.4		–56.5		(22.1)	
SDA investments			1.0		1.0	
Nonliquid cash assets		34.4		56.5		22.1
Currently nonqualifying currencies	27.1		37.6		10.5	
Undrawn credit commitments	4.2		5.7		1.5	
Required working balances	3.1		13.3		10.1	
Loans and credits		13.4		31.3		17.9
GRA credits	13.4		29.3		15.9	
SAF loans	0.0		2.0		2.0	
Receivables		0.1		1.8		1.7
Current charges and interest	0.1		0.6		0.5	
Deferred charges			1.2		1.2	
Gold (at SDR 35 per ounce)		5.4		4.8		(0.6)
Other assets		0.1		0.3		0.2
Total assets		60.4		129.7		69.4
Liabilities and Net Worth						
Liquid liabilities		19.4		33.5		14.1
Reserve tranche positions	11.1		28.9		17.8	
Borrowings	8.3		4.6		(3.7)	
Balance of quota subscriptions		39.7		89.5		49.8
SDA resources				3.0		
Other liabilities		0.2		0.5		0.3
Reserves, etc.		1.0		3.2		2.2
Ordinary reserves	1.0		1.8		0.8	
SCA			0.3		0.3	
Deferred charges			1.2		1.2	
Total liabilities and net worth		60.4		129.7		66.4
Memorandum items:						
Gold at market prices		78.8		54.5		–24.3
Unused and available credit lines		7.2		19.9		12.8

in 1980, and two increases for Saudi Arabia to reflect that country's substantially greater role in the Fund and in the world economy (see below, p. 889).[9] Following

[9]Before 1970, the Fund approved several requests for ad hoc quota increases apart from the general reviews. From then on, such requests normally were postponed until they could be considered as part of the next general review. The requests from China (between the Sixth and Seventh Reviews) and Saudi Arabia (between the Seventh and Eighth) were the only exceptions. As explained in Chapter 19, China's quota was increased twice in 1980: an ad hoc increase in August and a further increase in December as part of the Seventh Review. Saudi Arabia's quota also was increased in two large steps: first as part of the Sixth Review (1978) and again in 1981, shortly after the general increases from the Seventh Review took effect.

Table 17.2. General Reviews of Quotas, 1950–92

Review	Originally Scheduled	Effective	Agreed Increase	Number of Members	Stock (Billions of SDRs)	World Imports	Ratio (Days)
		1946		40	7.5	61.7	44
First	1950	1950	0%	49	8.0	62.6	47
Second	1955	1955	0%	58	8.8	93.7	34
Third	1960	1959	61%	69	14.6	129.8	41
Fourth	1965	1966	31%	102	20.9	185.4	41
Fifth	1970	1970	35%	116	28.8	314.0	33
Sixth	1975	1978	34%	133	39.0	715.3	20
Seventh	1980	1980	51%	141	59.6	1537.3	14
Eighth	1985	1983	48%	146	89.2	1909.3	17
Ninth	1990	1992	50%	175	141.4	2561.5	20
Average annual increase:			5.7%		6.6%	8.4%	

Sources: IMF Treasurer's Department (1998), Tables 1 and 2; IFS; and author's calculations. Imports are at five-year intervals, except that the initial datum is for 1948.

the 1979 revolution in Iran (which changed the country's name to the Islamic Republic of Iran), the government became preoccupied with the reconstruction of the economy and the war with Iraq, and Iran declined to accept either of the recommended quota increases in the early 1980s.[10] Consequently, Iran's quota slipped from the fourteenth largest to the twenty-seventh. Other individual changes in rank were generally minor.

The overall distribution of quotas among major groups of countries showed little change during the 1980s (Table 17.3). The share of developing countries rose slightly, but the ad hoc increases for China and Saudi Arabia more than accounted for that shift.[11] Both the large industrial countries and the small low-income countries lost shares, in amounts that roughly offset the large ad hoc increases. Smaller industrial countries and middle-income developing countries approximately maintained their aggregate shares. Quotas for all member countries from 1979 through 1989 are listed in Appendix II to this chapter.

Winning approval for general quota increases has always been a politically contentious task. Several reasons may be cited. First, a country's quota serves four separate functions: it determines the member's voting power in the Fund,[12] its access (bor-

[10]See "Ninth General Review of Quotas—Islamic Republic of Iran—Request for an Ad Hoc Increase," EB/CQuota/90/3 (January 12, 1990).

[11]As shown in Table 17.3, the developing country share rose by 1.6 percentage points. Without China and Saudi Arabia, the share declined by 1.7 points (from 32.4 percent to 30.7). For a long-term analysis of the distribution of quotas between industrial and developing countries, see Officer (1991).

[12]The effect of quotas on voting power is modified by the use of "basic votes." Under Article XII, Section 5, each member country has 250 basic votes, plus one vote per SDR 100,000 of quota. This provision was inserted at Bretton Woods as a nod in the direction of the "one member, one vote" principle used in some other international organizations, and to place a floor under the voting power of the smallest member countries (then Liberia and Panama). For the background, see Gold (1972), Chapter 2. Without basic votes, those two members would have held 0.006 percent of the expected voting power; with basic votes, they held 0.258 percent. As the size of the Fund

rowing) limits, its share in any SDR allocations, and its financial contribution to the institution.[13] Each of these functions is important, politically and financially, and the multiplicity leads to intrinsic conflicts. The more quota increases are allotted to potential borrowers, the more that group will obtain in terms of its voting power and its share of access to resources, but the smaller will be the stock of usable resources.

Second, a decision to increase quotas requires an 85 percent majority of the voting power. Quota reviews thus command an extraordinarily high degree of consensus, and resistance by a few major creditors (or even one, since the United States holds more than 15 percent of the voting power) can block action.

Third, despite changes in the Fund's financial structure that eliminated the systematic cost of quota increases, political debates continued to be framed as if costs would be incurred. Before the Second Amendment in 1978, subscription to a quota increase required countries to transfer reserve assets (normally gold or U.S. dollars) to pay the gold tranche portion of the subscription, and the process generated a direct cost to the subscribing country, measured by the lost interest on the unremunerated portion of the increase in the gold tranche. The Amendment froze the absolute level of the unremunerated portion of the reserve tranche (as the former gold tranche was renamed), so that interest would be paid on the entire increase; and it eliminated the requirement that a reserve tranche drawing would have to be repaid, so that countries could immediately offset the transfer of reserve assets.[14] Hence there was no longer any ex ante cost of investing resources in the Fund.[15] Nonetheless, opponents—especially in the U.S. Congress—continued to cite imagined costs as a justification for resistance.

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increased, the share of basic votes in the total decreased from 11.1 percent as calculated in 1944 to 4 percent in 1989, and the floor sank quite close to the ground. By 1989, the smallest member (Maldives) held 0.029 percent of the voting power, and without basic votes would have held 0.002 percent. To restore the original balance would have required raising the number of basic votes to approximately 740 per member. Since the Articles made no provision for changing the number of basic votes, the perennial effort by small countries to restore or at least maintain their share in total votes centered on the general reviews of quotas (see below, p. 868).

[13]Mikesell (1994), pp. 37–38, discusses and criticizes the background to the decision at Bretton Woods in 1944 to use a single set of quotas for multiple purposes. As complex and lengthy as the quinquennial quota reviews have been, one shudders to imagine the process if the Articles had provided for four independent quotas.

[14]For a country with outstanding debt obligations to the Fund, the requirement was a bit more complex. Rules in effect at the time of the Second Amendment required that payments to the Fund, including quota subscriptions, be applied first to outstanding debts. Assuming that the member had to borrow the foreign exchange or SDRs to pay the reserve tranche portion of its subscription, the net effect was to substitute other external debt for obligations to the Fund. That exchange often involved a significant increase in borrowing costs. In 1981, the Fund modified that rule and allowed countries to apply the payment directly to the reserve tranche. From then on, creditors and debtors had the same options available for eliminating the systematic cost of a quota increase. See also footnote 76, p. 877.

[15]Ex post, for a country that retains its reserve tranche, the marginal cost of a quota subscription is the difference between the country's own borrowing cost and the remuneration rate (both measured in the same currency), which is a function of both interest and exchange rates and could be positive or negative. Aside from differences between the remuneration rate and market interest rates, any risk of a marginal cost can be eliminated by an appropriate reallocation of net foreign exchange reserves or by permanently drawing out the reserve tranche. For a review of the evolution of the remuneration rate in relation to market rates, see below, pp. 900–04.

Table 17.3. Distribution of Quotas, 1979–89
(Billions of SDRs and percent)

	Sixth General Review 1979–80			Seventh General Review 1981–83			Eighth General Review 1984–89		
Group	Countries	Amount	Percent	Countries	Amount	Percent	Countries	Amount	Percent
Industrial countries	22	25,297	64.7	22	37,946	63.2	22	56,866	63.1
G-7	7	19,661	50.3	7	29,492	49.2	7	44,072	48.9
Developing countries	119	13,820	35.3	124	22,054	36.8	130	33,267	36.9
Small low-income	42	1,972	5.0	44	2,954	4.9	45	3,854	4.3
Largest Quotas:									
1	United States	8,405	21.5	United States	12,608	21.0	United States	17,918	19.9
2	United Kingdom	2,925	7.5	United Kingdom	4,388	7.3	United Kingdom	6,194	6.9
3	Germany	2,156	5.5	Germany	3,234	5.4	Germany	5,404	6.0
4	France	1,919	4.9	France	2,879	4.8	France	4,483	5.0
5	Japan	1,659	4.2	Japan	2,489	4.1	Japan	4,223	4.7
6	Canada	1,357	3.5	Canada	2,036	3.4	**Saudi Arabia**	**3,202**	**3.6**
7	Italy	1,240	3.2	Italy	1,860	3.1	*Canada*	*2,941*	*3.3*
8	India	1,145	2.9	**China**[a]	**1,800**	**3.0**	Italy	2,909	3.2
9	Netherlands	948	2.4	India	1,718	2.9	*China*	*2,391*	*2.7*
10	Belgium	890	2.3	Netherlands	1,422	2.4	Netherlands	2,265	2.5
11	Australia	790	2.0	*Belgium*	*1,335*	*2.2*	*India*	*2,208*	*2.4*
12	Brazil	665	1.7	Australia	1,185	2.0	Belgium	2,080	2.3
13	Iran	660	1.7	**Saudi Arabia**[b]	**1,040**	**1.7**	*Australia*	*1,619*	*1.8*
14	Venezuela	660	1.7	*Brazil*	998	*1.7*	Brazil	1,461	1.6
15	Saudi Arabia	600	1.5	*Venezuela*	990	*1.7*	Venezuela	1,372	1.5
16	Spain	557	1.4	Spain	836	1.4	Spain	1,286	1.4
17	China	550	1.4	Argentina	803	1.3	Mexico	1,166	1.3
18	Argentina	535	1.4	Mexico	803	1.3	*Argentina*	*1,113*	*1.2*
19	Mexico	535	1.4	Indonesia	720	1.2	**Sweden**	**1,064**	**1.2**
20	Indonesia	480	1.2	Sweden	675	1.1	*Indonesia*	*1,010*	*1.1*

Note: Countries in bold increased in rank and share from the previous review; those in italics moved down.
[a]The increase in China's quota was approved after the general review but took effect simultaneously.
[b]In September 1981, the quota of Saudi Arabia was raised to SDR 2,100 million.

Fourth, discussion of quota increases became part of the perennial dialogue on the appropriate balance between financing and adjustment for deficit countries. Some creditor countries sought to limit the size of quotas as an indirect way of limiting access to Fund resources and thus forcing stricter adjustment on borrowing countries. Such concerns were mitigated, however, by the reality that reduced financing from the Fund might have to be offset by greater bilateral support to prevent a breakdown in the debtor's economic and social fabric.

Fifth, the level of potential demand for Fund resources is very difficult to assess with any accuracy. Management recommendations for quota increases have been based partly on benchmark relationships between quotas and world economic activity, trade, and reserves; and partly on projections of the balance between demand and available resources. Differences of opinion about the relevance of various indicators can reasonably be, and often have been, quite large.[16]

During the prolonged debates that preceded agreement on general quota increases, the distribution of quotas also excited passions. General reviews of quotas offered an opportunity for countries to try to raise their own relative quotas, with an eye toward increasing their voting power, their borrowing limits, their shares in any SDR allocations, and their prestige among their peers. In addition, both the general reviews and discussions of quotas for new members became an occasion for countries to support their friends and occasionally to punish their enemies; assignments of quotas to new members offered an opportunity to define their position in the international political and economic hierarchy.[17]

One should not strain too hard to rationalize these political pressures on economic grounds. Political battles over quota increases sometimes escalated to dimensions far out of proportion to the economic values at stake. What is important for an understanding of this History is simply that political concerns and economic and financial uncertainties, from whatever source, have combined to prevent Fund resources from increasing *pari passu* with world trade. Even so, the Fund has enjoyed a widespread support from creditor countries, and it generally has been able to secure an essential level of resources when the demand has been most acute.

Quota reviews comprise four distinct stages. First, Executive Directors engage in extensive debates on whether a general increase is warranted, the optimum size of the Fund under current and expected conditions, and how any increase should be allocated among members. Those debates usually focus on technical issues, but political considerations are never far below the surface. That stage concludes with approval of a formal resolution to be submitted to the Board of Governors. Although approval technically requires only a simple majority of votes cast, there would be no point in doing so without an expectation of much broader support. Second, Governors vote on the resolution. When the required majority—85 percent of the total voting power—is achieved, the proposal to increase quotas becomes effective.

[16]In 1997, a former Executive Director opined that "the IMF falls from its normally very high analytical standards . . . when the case is made for higher quotas" (Evans, 1997, p. 10).

[17]For a striking example, see the discussion in Chapter 19 (pp. 986–92) of Poland's reaccession to membership.

Third, each member country must consent to its proposed increase. Procedures for doing so vary from country to country and may require parliamentary approval and appropriations. Usually, no member's quota increase can become effective until a critical mass of consents (the "participation requirement") is received. That requirement is specified in the resolution and varies from one review to the next. Fourth, each member's increase becomes effective when it pays in its subscription.

Seventh General Review

Technical preparations for the Seventh General Review, which took place in 1976–77, led to a staff and management recommendation for an increase of 75 to 100 percent. Political discussions then produced a broad consensus for a compromise increase of 50 percent, but the United States and Germany (with a combined vote of just under 25 percent) blocked action for about a year. They dropped their opposition suddenly in the fall of 1978, shortly after the Bonn Summit of major industrial countries highlighted the dangers of sluggish economic growth in many countries around the world. As part of a consensus package negotiated by de Larosière, the Interim Committee agreed in September 1978 to increase quotas by 50 percent, to have a new allocation of SDRs, and to require that the reserve-asset portion of the quota subscription be paid in SDRs. The Board of Governors approved a formal resolution soon thereafter. So as the period of this History began, all that remained was for member countries to ratify the proposed increases.[18]

Although the administration of U.S. President Jimmy Carter supported the quota increase, it failed to get quick action from congress in 1979 and then found the request caught up in the politics of the presidential and congressional election campaigns of 1980.[19] That delay could well have killed the whole process: since the United States held 21.5 percent of the base-period quotas, almost every other member country would have to consent for the increases to take effect without them. No general increase had ever taken effect without the Fund's largest member, and the prospect that this one *could* do so raised interesting possibilities. For one, if quotas were raised for the rest of the membership, the U.S. role in the Fund

[18]For a detailed review of the process through 1978, see de Vries (1985), pp. 529–39. The resolution specified that the quota increases would become effective only when members holding not less than 75 percent of the total quotas as of November 1978 consented to them. This participation requirement was set by the Executive Board, as a means of pressuring members to respond quickly and of ensuring that most increases would take effect simultaneously and thus avoiding temporary shifts in voting power.

[19]Although quota payments represent an exchange of assets and do not call for an expenditure by the government, the U.S. Congress demanded that the process involve approval of an appropriations bill. For the administration position on the increase, see the testimony by Anthony M. Solomon, Under Secretary of the U.S. Treasury for Monetary Affairs, before the Subcommittee on International Trade, Investment, and Monetary Policy of the Committee on Banking, Finance, and Urban Affairs; U.S. House of Representatives (February 4, 1980). Solomon's testimony was circulated to the Fund's Executive Directors as "United States—Statement by the Under Secretary of the Treasury for Monetary Affairs," EBD/80/32 (February 6, 1980).

would be greatly diminished until it consented. Its share in the total voting power would drop from nearly 20 percent to about 14 percent, which would imply a loss of veto power over decisions requiring an 85 percent majority (such as future quota increases). Second, the SDR allocation scheduled for January 1981 would be substantially smaller, and no easy remedy was available for making up the gap at a later date. Third, the supply of U.S. dollars for use in Fund operations would be smaller, which could create problems for financing large drawings.

Despite the dangers of these untested waters, de Larosière was eager to push ahead with or without the U.S. increase, and he directed the staff to make an all-out effort to persuade other countries not to wait. An intense lobbying campaign ensued, and it eventually paid off. On November 28, 1980, with the receipt of an official consent from Tunisia, the Fund had the consent of 127 out of 133 eligible countries, accounting for 75.15 percent of the total. The Executive Board approved an implementing decision the same day, and the increases took effect on November 29.

By then, the U.S. elections were over, and congress was in a lame-duck session. That circumstance, coupled with the pressure from the fact that the general quota increase had already taken effect for other countries, created a window of political opportunity. Opposition faded away, and the United States consented to its quota increase in mid-December.

The Seventh Review raised IMF quotas from SDR 39.8 billion to SDR 60 billion ($51 billion to $77 billion), with most of the increment distributed as 50 percent increases in proportion to members' previous quotas.[20] In addition to the large extra increases for China (total increase of 227 percent) and Saudi Arabia (73 percent) mentioned above, eight other countries received bonus increases that reflected a strengthening of their roles in the world economy.[21] Five of those were major oil exporters that received increases ranging from 61 to 69 percent: Iraq, Kuwait, Libya, Qatar, and the United Arab Emirates.[22] Two were East Asian countries that had recorded strong growth in output and exports in the preceding years: Korea (60 percent increase) and Singapore (88 percent). Lebanon, which for many years had declined to accept increases to which it was entitled and whose quota had thus become the lowest relative to calculated values, completed the list with an increase of 133 percent.

Eighth General Review

Work on the next general review began as soon as the 1980 increases took effect. The report completing the Seventh Review had indicated that the next one

[20]Increases were rounded upward for several, mostly small, countries. The largest proportional effect from rounding was for the country with the smallest absolute quota (Maldives), which received an increase of 55.6 percent (from SDR 0.9 million to 1.4 million).

[21]No increase was proposed for Cambodia (then known as Democratic Kampuchea), with which the Fund had no formal means of communication at the time (see Chapter 16).

[22]The resolution approved by the Board of Governors also provided selective increases for Iran and Oman, but those recommendations were declined. Iran did not consent to any increase, and Oman consented only to the equiproportional increase.

should include a thorough reexamination of the distribution of quotas to see whether it was still broadly appropriate in the modern world.[23] Consequently, staff preparation for the Eighth Review began with a review of the formulas used to calculate baseline figures for individual and aggregate quotas.

Forty years earlier, the technical staff preparing for the July 1944 Bretton Woods conference had calculated quotas for most prospective members by means of a nonlinear equation based on data for national income, international trade, and official reserves. That equation was calibrated so as to yield an aggregate quota of the size agreed upon during preliminary negotiations among the major countries (about $8 billion for participating countries) and to rank countries in a way that was both politically acceptable and reflective of relative positions in world trade and finance. It was not derived from theory or econometrics, and it was neither discussed nor even officially disclosed during the conference. Nonetheless, it did produce reasonable results for most countries, and no superior alternative was presented. With a few major exceptions, the original quotas of Fund members were set approximately by the Bretton Woods formula.[24]

With technical modifications, the staff continued to use the Bretton Woods formula as a notional device for calculating updated quotas, as a starting point for general reviews of quotas. Beginning with the Fourth Review in the mid-1960s, the coefficients were cut approximately in half to reflect the fact that the actual aggregate stock of quotas was far below the level produced by the original formula. Also, more comprehensive data were introduced, and several auxiliary equations were specified to reflect different views on the relative importance of each determining factor.[25]

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[23]See section 5 of "Report of the Executive Board to the Board of Governors" (October 25, 1978), in de Vries (1985), Vol. 3, pp. 258–61.

[24]See Horsefield (1969), Vol. 1, pp. 94–98; Altman (1956); Mikesell (1994), pp. 37–38; and "The Working of the Quota Formulas," EB/CQuota/94/2 (February 28, 1994), pp. 53–54. (Raymond Mikesell, as a member of the secretariat preparing for the Bretton Woods conference, derived the quota formula.) The original equation (with all data measured in U.S. dollars) may be written as

$$Q = 0.09 * (0.2Y + 0.5R + M + V) * (1 + X/Y),$$

where Q = the member's quota; Y = national income in 1940; R = gold and dollars held on July 1, 1943; M = average annual imports, 1934–38; and V = maximum variation in exports (X), 1934–38 (i.e., the difference between the highest and lowest of the five annual values).

[25]The revised and reduced Bretton Woods formula was

$$Q = (0.01Y' + 0.025R' + 0.05M' + 0.2276V')*(1 + X'/Y'),$$

where Y' was measured by GDP rather than national income, R' was measured by more comprehensive data on international reserves, M' and X' were expanded to include services and other current account payments and receipts, and variability (V') was redefined to better reflect volatility:

$$V' = \sqrt{\Big(\sum_{t=3}^{11} (X'_t - \bar{X}'_t)^2\Big)/3}$$

where $\bar{X}'$ is a five-year moving average of X'.

Until the Eighth Review, two versions of the reduced equation were used, one with the original data definitions and the other with these more inclusive variables. See de Vries (1985), pp. 514–17.

What did the Bretton Woods formula, as previously revised and "reduced," imply about the overall adequacy of quotas for the early 1980s? The previous review had been based on data through 1976, and when the staff began its work data were available through 1979. During those three years, world trade had grown by a little over 50 percent, while incomes and reserves had grown by a little less than 50 percent (all measured in SDRs, without adjustment for inflation). The reduced Bretton Woods formula implied that quotas should be raised by 50 to 80 percent to restore the relationship between actual and calculated quotas established for the Seventh Review, depending on the selection of data for the computations; by 140 to nearly 200 percent to make actual quotas equal to the calculated total;[26] and by some 350 percent to make them equal to the total derived from the original 1944 formula.[27]

Even the bottom end of this range of estimates suggested that a substantial increase was in order, and few thought that the calculations overstated the case. As the demand for stand-by and extended credit arrangements grew in 1979 and 1980, the Fund had to borrow from creditor countries to finance its operations (see below, p. 884–85). All those involved in the review agreed that borrowing by the Fund was a temporary expedient, that the debts already incurred should be repaid as quickly as possible, and that quotas should remain the primary source of financing for Fund lending. Assuming that demand for Fund resources would remain strong, management and most Executive Directors viewed an increase in quotas by something close to 100 percent as a high priority that had to be addressed with some urgency.

A second and equally clear message from these initial calculations was that the actual distribution of quotas no longer bore a clear relationship to calculated values. After normalizing the calculated values on the actual total, eight countries had quotas that were less than half the calculated value; eight others had quotas that were more than four times the calculated value; and only 26 countries out of 140 were within 20 percent of the adjusted calculated quota.[28] These massive anomalies resulted from the practice of awarding almost all members at least the agreed minimum percentage increase and making only a limited number of selective increases at each review. Rather than revising the distribution of quotas every five years in response to shifts in the distribution of income, trade, and finance, the Fund had favored inertia.

The Executive Board's work on the Eighth Review began in July 1981, at which time de Larosière set the agenda on the basis of these initial findings. In his view, a "substantial increase in quotas was warranted," and quotas were so "far out of line" with reality that a "significant adjustment in relative positions" was also needed. Although most members of the Executive Board concurred with those assessments from the outset, the opening remark by Donald Syvrud (Alternate—

[26]Actual quotas under the Seventh Review were just 59 percent of the total calculated from the reduced Bretton Woods equation.

[27]"Eighth General Review of Quotas—Quota Calculations," SM/81/151 (July 2, 1981), pp. 7–8.

[28]"Present and Calculated Quotas," SM/81/91 (April 23, 1981), pp. 6–10.

United States) was that "the United States does not agree that, at the present time, a substantial increase is warranted."[29]

This initial negotiating position by the United States was noteworthy, because the history of quota reviews shows that the effective constraint on general increases is the consent of the Fund's major shareholders. For most countries, any costs or drawbacks of a quota increase—for themselves, the Fund, or the international monetary system—are greatly outweighed by the benefits. For a few of the largest creditor countries, the calculus is more complex, because they supply the bulk of the Fund's lendable resources. The U.S. position, of course, is predominant in this calculus, because the United States has always held veto power over quota increases (which, as noted above, require an 85 percent majority in the voting by the Board of Governors).

Detailed discussions followed throughout the rest of 1981 and all of 1982,[30] primarily on the two questions of how large the overall increase should be and how it should be distributed. On the question of the optimum overall increase, the staff produced a large number of calculations under different assumptions, which yielded a bewildering array of results. All calculations suggested that quotas should be increased substantially, and a few methods indicated that quotas should be raised severalfold.[31] The bottom line, however, was that the indicators of the determinants of demand for Fund resources had increased, on average, by about 16–17 percent a year. Over five years, quotas would have to rise by about 80 percent to keep pace. Taking account of estimates that the starting point was precariously low added anywhere from 20 to a few hundred percentage points to that figure. Everyone involved understood that a political agreement on doubling the Fund's resources would be extremely difficult, especially since the U.S. administration of President Reagan was then opposing any substantial increase. Technical discussions on whether quotas should rise by 100 percent or by much more took up a lot of staff and Board time in 1981 and 1982 but were essentially meaningless for the eventual outcome.

Technical work on the optimum distribution of quotas focused on the implications of a large number of auxiliary or "derivative" equations.[32] Although the Bretton Woods formula was accorded a central position in the exercise because of its historical role in determining the initial distribution, both the staff and many Directors wanted to examine the consequences of changing the relative weights as-

[29]Minutes of the Executive Board Committee of the Whole on Review of Quotas, Meeting 81/1 [hereinafter given in the form EBCQM/81/1] (July 27, 1981), p. 5 (de Larosière); and EBCQM/81/2 (same date), p. 15 (Syvrud).

[30]In May 1981, the Interim Committee asked for "intensified" work on increasing quotas but did not set a date for completion of the review. In July, the Executive Board established a "Committee of the Whole on Review of Quotas," which enabled Directors to debate the issues more freely than in a formal Board meeting. Discussions on the Eighth Review took place in that forum until the time came for final decisions.

[31]See, in particular, "Eighth General Review of Quotas—Quota Calculations," SM/81/151 (July 2, 1981) and "Eighth General Review of Quotas—Calculated Quotas," EB/CQuota/82/4 (April 7, 1982).

[32]The added equations were termed "derivative" because they were normalized to produce the same aggregate result as the Bretton Woods formula.

signed to the various determining factors (income, trade, reserves, and the volatility of trade).[33] After the first few months of discussions, more than 30 equations were being used to generate alternative lists of prospective quotas. Much of the later debate in the Board involved ways to reduce that number. The nature of that process is illustrated by the discussions on the key variable: the role of variability in international trade.

The case for including trade variability as a determinant of quotas was that fluctuations in export receipts affected a country's need for financial assistance from the Fund. Countries with above-average variability might need relatively large quotas to cover their balance of payments requirements. That case had been weakened over time by the establishment of the Compensatory Financing Facility (CFF) as a separate means of covering such fluctuations and by exempting CFF drawings from the conventional limits on access to Fund resources (see Chapter 15 and the section below on access policies). Moreover, in practice the link between variability and demand for Fund resources was not all that strong, and some Directors saw this variable as a source of distortion in the distribution. The staff accordingly specified some equations and generated some alternative quota lists based on a reduced or eliminated role for the variability term. That exercise concluded that the main effect would be to redistribute quotas from major oil-exporting countries to industrial countries.[34] A majority of the Board favored doing so, but the Managing Director attempted to dissuade them from pursuing the idea, primarily on the grounds that the oil-exporting countries at the time were important contributors to the supply of liquid assets to the Fund.[35] After further discussion, Executive Directors accepted a compromise proposed by A.R.G. Prowse (Australia) in which variability played a somewhat smaller role in the derivative equations than it had in previous reviews.[36]

In the end, the Board decided to use four derivative equations along with the reduced Bretton Woods formula (see Appendix III).[37] Relative to the Bretton

[33]The use of auxiliary equations began in the early 1960s, when derivative equations with relatively high coefficients on the variability of international trade were used to justify a shift in the distribution of quotas toward developing countries. See Horsefield (1969), Vol. 1, pp. 537–38.

[34]This effect was a consequence of the mathematical property that a large jump in export receipts—such as occurred twice for oil exporters in the 1970s—registered in the formulas as high variability. Variability had the same effect on the calculations regardless of whether it raised or lowered the country's current account balance.

[35]". . . one has to bear in mind the impact of any modification to the definition of variability on the calculated quotas and what effect this would have on the liquidity of the Fund." Minutes of EBCQM/81/4 (October 16, 1981), p. 25.

[36]For the initial review of the issue, see "Variability in the Quota Formulas," EB/CQuota/81/2 (August 11, 1981) and minutes of EBCQM/81/3–4 (October 16, 1981). For the follow-up, see "Variability in the Quota Formulas—Further Considerations," EB/CQuota/82/7 (May 6, 1982) and minutes of EBCQM/82/7–8 (June 4, 1982).

[37]For the five formulas, see "Eighth General Review of Quotas—Calculated Quotas," EB/CQuota/82/11 (November 24, 1982), p. 3. On the discussion and selection of the formulas, see EB/CQuota/82/7, Sup. 1 (June 14, 1982), Appendix I, pp. 19–24; and minutes of EBCQM/82/9–10 (June 23, 1982), EBCQM/82/11–12 (August 4, 1982) and EBCQM/82/13 (August 13, 1982).

Woods equation, the alternatives all gave a smaller weight to GDP and a larger weight to variability. The weights on the other variables were made both smaller and larger in the various equations, and two equations removed the nonlinear term (the ratio of exports to income). The agreed procedure was to compute the notional "calculated quota" as the higher of (1) the quota from the reduced Bretton Woods formula and (2) the simple mean of the two lowest values from the four derivative formulas.

Resolution of the two issues—the size of the overall increase and the distribution of quotas among member countries—was closely linked, since quotas could be changed only in one direction.[38] Without a general increase, no redistribution was possible; the larger the increase, the more (in principle) could be accomplished on improving the distribution by allocating increases selectively. The idea emerged during these discussions of first deciding on the appropriate size of the overall increase and then dividing it between two categories: an equiproportional increase for all members and selective increases for members (or groups of members) with quotas that were particularly low relative to calculated values. Determining those two numbers—the total and the ratio—took the debate beyond technicalities and into politics.

A third, more technical issue, also had to be settled: the form in which members would be required to pay their quota increases. Article III of the Fund's Articles of Agreement specifies that 25 percent of any increase is to be paid in SDRs, unless the Board of Governors prescribes that payment may be made, in whole or in part, in currencies specified by the Fund. For the Sixth General Review, in 1978, members were given the option of paying in currencies, and most did so. For the Seventh, in 1980, in the midst of a series of new allocations of SDRs, members were required to pay in SDRs.[39] The Fund sought to maintain a reasonable balance between SDRs and major currencies in its own portfolio, for reasons related to liquidity, ease of operations, promotion of the SDR as a reserve asset, and avoidance of unusually large or small holdings of a particular currency or of SDRs. In general, the Fund regarded SDRs as more liquid than individual currencies, so the principal issue was whether requiring payment in SDRs would lead to a shortage of SDRs available to member countries. The staff paper on this issue concluded that a shortage could result, and it recommended that countries be given the option to pay in currencies unless a decision was taken to allocate additional SDRs. The Executive Board, however, could not readily reach a consensus on the issue. A majority preferred to use it as a lever to argue for fur-

[38]Article III of the Fund's charter specifies that quotas can be changed only with the consent of the member. Normally, countries have no incentive to request or accept a reduction. Even before the Second Amendment of the Articles, when a quota increase required a transfer of real assets, only one country (Honduras in 1948) ever requested a reduction in its quota. See Horsefield (1969), Vol. 1, p. 196; and Gold (1972), p. 17n.

[39]A few member countries at that time were not participants in the SDR Department; they were required to pay in specified currencies. As noted above, the requirement for participants to pay in SDRs was a critical element of the package proposal under which SDR allocations were approved for 1979–81; see de Vries (1985), pp. 880–82.

ther allocations, but others were prepared to resist that linkage strenuously (see Chapter 18).[40]

By the spring of 1982, technical work had proceeded far enough that the locus of the Eighth Review began to shift to the political arena. In the first substantive report on the Review to the Interim Committee, which was to meet in Helsinki in May 1982, the Managing Director noted that the "staff analysis" suggested that "roughly a doubling of present quotas would be required . . . to meet the justified demands on the Fund's resources that are expected to prevail in late 1984." The Executive Board, however, had not reached a consensus on whether that figure was too large (as argued by a few creditor countries) or too small (as argued by some potential borrowers). Similarly, no consensus had been reached on how extensive a redistribution would be desirable, nor on whether to revise the methodology for calculating quotas.[41] In those last few months before the onset of the international debt crisis, some of the largest creditors were still focused primarily on what they perceived to be a need for restraint in the Fund's lending activities, not on the need for additional resources to finance expanded lending.

Divisions ran equally deep in the Interim Committee, and ministers showed no inclination to try to break the impasse by themselves. They issued a communiqué endorsing once more the idea of an adequate increase in quotas, asking the Executive Board to give the matter a high priority, and noting that they "hoped" to be able to resolve the main issues at their next meeting, less than four months hence, in Toronto.

After several more meetings during the summer, the Board reported back to the Interim Committee. The report for the Toronto meeting noted the agreement on the five-formula method for calculating notional quotas, as described above. On the more substantive issues, however, consensus was still elusive.[42] The Committee responded by suggesting more firmly that these issues should be resolved by the time of its next meeting, which was scheduled to take place in April 1983.

By this time the squeezing of the Fund's resources was getting serious. A little more than a year remained before the Board of Governors would have to approve a resolution completing the Eighth Review, but it was not clear whether the Fund could continue to meet the demand for credit without a quota increase or at least new borrowing. The eruption of the debt crisis and the consequent traumas of Toronto (see Chapter 7) had pressed home the fact that creditor countries needed the Fund—and the money they had invested in the Fund—to resolve the crisis. Mexico, Brazil, and Argentina soon would have major Fund-supported programs, and several more sizable credit arrangements were in the pipeline. A quota increase now appeared to be in everyone's interest.

[40]"Eighth General Review of Quotas—Payment for Increases in Quotas," EB/CQuota/82/14 (December 17, 1982); and minutes of EBCQM/82/20 (December 22, 1982).

[41]"Eighth General Review of Quotas—Report of the Executive Board to the Interim Committee," ICMS/Doc/82/2 (April 27, 1982).

[42]"Eighth General Review of Quotas—Report of the Executive Board to the Interim Committee," ICMS/Doc/82/7 (August 25, 1982).

Resolving the problem was still not easy. The Board again took up the question of the appropriate size of the Fund on November 10, 1982. All Directors now agreed that an increase was needed and that the Review should be concluded as quickly as possible. If they could agree on the overall size, it would be desirable to advance the date of the next Interim Committee meeting to bring the review to a successful conclusion. All but three Directors agreed that quotas should be at least doubled, to a minimum of SDR 120 billion, but the three dissidents were among the largest creditors to the Fund. The governments of Germany and the United Kingdom supported the idea of at least a 50 percent increase but were not prepared to commit themselves to a much larger amount, and the U.S. government was unwilling to commit to any figure at all. The U.S. reluctance stemmed from the usual political difficulty, that congress would have to approve legislation to authorize the increase and to appropriate funds for it. The administration was just beginning a long process of lobbying and bargaining with members of congress, and it did not want to set a number that could become a target for opponents.[43]

Within a few weeks of that meeting, the dispute over the size of the increase in quotas began to narrow. When the Deputies of the Group of Ten (G-10) met in Paris just before the end of the month to prepare for a meeting of their finance ministers, they agreed that the issue should be resolved very quickly and that the Interim Committee should meet earlier than next April to reach a final agreement. By December 8, when the ministers of the more exclusive Group of Five (G-5) gathered for an ostensibly secret meeting at the Schloss Friedrichshoff castle in Kronberg, Germany (see Chapter 4, p. 196), the rapidly deteriorating financial status of Brazil further galvanized creditors into action. The U.S. Secretary of the Treasury, Donald T. Regan, was thought by at least some participants to have agreed to support a quota increase of close to 50 percent. In the interest of getting a compromise on the table, those who had been seeking to double the total decided to give up that goal. G-10 ministers met the next day in Paris, confirmed the compromise, and made the agreement known to the press.[44]

Despite the apparent G-10 agreement, the Executive Board continued to be split, with the U.S. chair still unwilling to support an increase larger than around 40 percent (to SDR 85 billion) and several Directors adhering to the goal of doubling quotas to SDR 125 billion. The staff provided additional calculations suggesting that an increase to at least SDR 95 billion was needed to prevent recourse to further borrowing by the Fund. On the distribution, a consensus was forming around the idea of devoting a portion of the overall increase to an equiproportional increase for all members and using the rest to move actual quotas partway toward those calculated on the basis of the agreed formulas. Debate continued, however,

[43]That case was set out by Richard D. Erb (Executive Director, United States) at EBCQM/82/14 (November 10, 1982), pp. 4–5.

[44]See Paul Lewis, "Bigger Loan Fund Gets Key Support," *New York Times* (December 11, 1982), p. 42. Regan had mentioned the G-5 meeting to reporters two days before it was to take place, so the usual secrecy was broken. As the host minister, Gerhard Stoltenberg gave a background debriefing for reporters after the meeting. Also see Stoltenberg (1997), pp. 314–15.

on how large the general increase should be and (as a corollary) how large the "adjustment coefficient" (the fraction of the gap to be closed between actual and calculated quotas) should be.[45]

If the Executive Board had taken a decision at the end of 1982 on the basis of a simple majority, it would have voted to raise quotas to SDR 125 billion, with as much as half being distributed equiproportionally among all members and with a small amount being set aside to raise the quotas of countries with extremely small quotas.[46] The final decision, however, rested in the hands of the governors, who had to agree with an 85 percent majority. After 41 meetings over nearly two full years and consideration of some 34 staff papers, the Executive Board still could not reach that degree of consensus.

The February 1983 meeting of the Interim Committee was eventful, even dramatic, in several respects. It was the first time that the committee had scheduled an early meeting to resolve a prickly issue, and it was doing so at a time when many developing countries and even the international financial system were still in crisis. Not only the quota increase but also a major increase in lending to the Fund (see below) was at stake, and the outcome was far from certain. As the meeting progressed on the first day (Thursday, February 10), Regan tried to hold the quota increase to 40 percent, which prompted several governors from indebted countries to revert to their calls for a minimum acceptable increase of 100 percent. To add an extra comedic drama to the scene, that evening Washington was buried under its worst winter blizzard in several years—a storm that de Larosière later remembered in an interview as "of Shakespearean dimensions." Transportation was suddenly frozen, and, for many governors, just getting to and from the meetings was already an achievement. (See, for example, Howe, 1994, pp. 272–73.)

On the quota review, responding to the diplomacy of the chairman—Geoffrey Howe, Chancellor of the Exchequer in the United Kingdom—the governors on the Committee reached agreement on most of the key issues during a snow-bound dinner on Thursday at the F Street Club near Fund headquarters. The next day, at the end of two marathon days of discussions, the Committee formally settled the

[45]The agreed procedure imposed the constraint that each member would receive a quota increase composed of an equiproportional increase (i.e., every member would receive this percentage increase) and a selective increase expressed as the product of a constant adjustment coefficient and the ratio of actual to calculated quota. The second term would vary between countries, and the range of possible coefficients was restricted to guarantee that each member would receive an increase in the amount of its quota. As shown mathematically in Appendix III, that constraint implied that a large adjustment coefficient required a large increase in quotas. For the issues in the debate, see minutes of EBCQM/82/18–19 (December 21, 1982) and "Eighth General Review of Quotas—Report of the Executive Board to the Interim Committee," ICMS/Doc/83/2 (January 14, 1983). For the derivation described in Appendix III, see "Ninth General Review of Quotas—Issues Arising in Connection with the Eighth General Review of Quotas," EB/CQuota/87/4 (December 21, 1987), Appendix II.

[46]From 1955 to 1965, the Fund had a policy of setting a minimum level for quotas. That policy eventually was seen as distorting relationships between very small and slightly larger countries, and it eventually was dropped. Restoration of some form of minimum then became a perennial topic during discussions on quota reviews. See "A Review of Fund Policies on Minimum Quotas," EB/CQuota/82/12 (December 13, 1982).

matter. On the overall size, ministers agreed to raise quotas by 47.5 percent, to SDR 90 billion ($99 billion). That amount was not expected to alleviate the Fund from seeking new loans, but it was as much as the U.S. authorities were prepared to ask congress to approve. On distribution, the Committee agreed that 40 percent of the increase (SDR 11.6 billion) was to be allocated in proportion to existing quotas. The remainder (SDR 17.4 billion) was to be allocated in proportion to calculated quotas. Under this compromise, the non-oil developing countries lost about 1.7 percentage points in voting power, but they would have lost another point if all the increase had been allocated according to calculated quotas. Industrial and major oil-exporting countries reaped the gains in roughly equal shares.[47] On the method of payment, they agreed that the reserve-asset portion of the increase (25 percent of the total) was to be paid either in SDRs or in usable currencies.

One issue—minor from a global perspective but very important to a few countries—could not be resolved by the committee, owing to objections from major creditor countries: how to adjust the quotas of the smallest member countries so as to give them a meaningful share in the total without upsetting relative positions. At the suggestion of Cesar E.A. Virata (Prime Minister and Minister of Finance of the Philippines), the issue was remanded to the Executive Board for a decision. In doing so, the committee signaled clearly that it wanted an adjustment that would improve the situation of the smallest countries. Nonetheless, the stalemate in the Board continued. After lengthy discussion spread over two days of meetings, Directors essentially gave up trying to find a substantive solution. Since lip service still had to be given to the problem, de Larosière proposed that the 17 quotas that were below SDR 10 million be rounded up to the next 0.5 million; all other quotas were to be rounded up only to the next 0.1 million. That suggestion was readily embraced, and the matter was closed until the next review.[48]

To expedite the completion of the process and ensure that the increases were likely to take effect before the end of the year, the Board set the participation requirement at 70 percent (reduced from 75 percent in the Seventh Review). That figure would be a little easier to reach without the participation of the United States, and it was hoped that this fact would expedite U.S. approval.[49] By autumn,

[47]These effects are based on a starting position in which Saudi Arabia had already received a large ad hoc quota increase after the completion of the Seventh Review. As shown in Table 17.3, the distribution between industrial and developing countries shifted very little from the end of the Seventh to the end of the Eighth Review.

[48]See “Eighth General Review of Quotas—Proposed Maximum Quotas,” EB/CQuota/83/4 (February 17, 1983) and the minutes of EBCQM/83/1–2 (February 24) and EBCQM/83/3 (February 25). The effects of the adjustment were distributed randomly among the 17 countries. It raised only 11 quotas, by a total of SDR 2.5 million. The smallest quota (Maldives) was unaffected, as it rose from SDR 1.4 million to 2.0 million both before and after the special adjustment.

[49]As noted above, a participation requirement—consents expressed as a percentage of initial quotas—was normally proposed by the Executive Board for each quota review on the basis of strategic considerations. Of the five general increases prior to the Eighth Review, three required 75 percent, one required 67 percent, and one contained no percentage requirement. On the background of the participation requirement, see “Eighth General Review of Quotas—Draft Report and Resolution,” EB/CQuota/83/3 (February 17, 1983), p. 2. The views of Executive Directors are summarized in the minutes of EBCQM/83/2 (February 24), p. 4.

however, it was beginning to look as if the Reagan administration might not be able to muster enough votes to get the quota increase through the U.S. Congress. The proposal was attacked from the left by those who saw it as a bailout for commercial banks that had lent profligately to uncreditworthy developing countries and by those who seized the opportunity to wrest unrelated political concessions from the administration. It was also attacked from the right by those who saw it as a bailout for indebted countries with excessive governmental intervention in their economies. Approval of the quota legislation would require even more political muscle than its 1980 predecessor.

As described in the introduction to this chapter, the impasse in the U.S. Congress led de Larosière to impose a partial freeze on new lending by the Fund, and it spurred President Reagan to undertake a strong personal campaign to elicit support. Finally, the bill won sufficient support in November 1983, after it was attached to legislation authorizing several billion dollars for investments in domestic public housing projects. That linkage created a package of two dissimilar and controversial measures, which as a combination could receive more votes than either measure would have garnered separately.

The quota increases took effect on November 30, 1983, with 122 out of 146 member countries having consented. Those countries held 72 percent of the initial quotas. The United States had not yet formally consented, but congress had approved the necessary legislation several days earlier. As of December 1, consents totaled 131 (96½ percent of the total). Eleven stragglers accepted by the final deadline of mid-March 1984, and the Eighth Review was completed. That left four countries without an increase. As in the Seventh Review, no increase had been proposed for Cambodia (Democratic Kampuchea), with which the Fund still had no formal channel of communications. Three countries—Iran, Singapore, and the United Arab Emirates—declined the increases that had been proposed.

All that remained was for each member to pay in the reserve portion (one-fourth) of its increase, either in SDRs or in currencies acceptable to the Fund. Almost all of that was paid in SDRs, and payments were completed before the end of April 1984. The world still faced a debt crisis, and the Fund was about to be confronted with a quagmire of arrears, but for the moment its liquidity crisis had been resolved.[50]

[50]Payments of the reserve-asset portion of the quota increases totaled SDR 7 billion. Of that, less than SDR 1 billion was paid in currencies rather than SDRs; *Annual Report 1984*, p. 75. Out of 142 consenting members, 126 paid entirely in SDRs. Eleven paid in foreign exchange, and five paid in a combination of the two. The bulk of the currency payment was shared equally by the deutsche mark and the Japanese yen, with relatively small amounts paid in U.S. dollars and pounds sterling. A bookkeeping arrangement enabled 39 low-income countries to enlarge their quotas without actually paying in scarce reserves (see above, p. 855). Those countries borrowed SDRs from 11 members with large SDR holdings to cover their reserve-asset subscriptions. They simultaneously drew their reserve tranche position from the Fund and used the proceeds to repay the loan. No interest or commission was charged on those transactions.

Ninth General Review

The quotas established in the Eighth Review were maintained for nearly nine years, the longest period without an increase since the 1950s. Work on the Ninth Review began on schedule in 1987, but it proceeded at a leisurely pace because some of the major creditors again started with a view that the Fund had adequate resources for the near future. Then, in the same way that the international debt crisis spurred creditors to raise the Fund's resources in 1983, the ending of Soviet control over Eastern Europe and then the collapse of the Soviet Union itself provided the impetus for raising Fund quotas in the early 1990s.[51]

Normal Fund procedure called for the Executive Board to appoint a Committee of the Whole to begin work on the review about four years after the governors approved completion of the last one, with the goal of maintaining a five-year cycle. The Board took that first step in March 1987, but it did so without much hope of reaching the end of the path in time. The U.S. governor, Treasury Secretary James A. Baker III, used the occasion of the April Interim Committee meeting to express doubts about the need for an increase. ("We believe it is neither financially necessary nor politically feasible to reach an early conclusion to the Ninth Quota Review.")[52] Most other creditors were also prepared to wait, and neither of the Interim Committee communiqués of 1987 encouraged the Executive Board to give the matter much priority.[53]

Faced with high-level insouciance, the Board confronted a choice between extending its work on the review beyond the deadline—possibly for years—or concluding the review without a recommended increase and waiting for the next five-year cycle. Most Directors wanted to maintain some momentum toward an increase, and they agreed to keep working on that basis. They held meeting after meeting (as the Committee of the Whole) and eventually had to extend their work from the original deadline of March 1988, first to April 1989, then to December, then to the following March, and finally to June 1990 when the governors approved their recommendation for a general increase of 50 percent. Not until November 1992, however, would the increases take effect.

To start the discussion, the staff looked at how the determinants of the notional "calculated quotas" had changed during the interval of five years.[54] Foreign exchange reserves had grown at an annual rate of 3¼ percent, nominal world

[51]This pattern was repeated in 1998, when concurrent financial crises throughout East Asia and in Russia finally induced a reluctant U.S. Congress to approve a general quota increase only after a long delay.

[52]IMF/CF; Interim Committee Master File. Verbatim transcript of First Session, p. 31.

[53]"The Committee urged Executive Directors to pursue their work on the Ninth General Review of Quotas so as to be in a position to make appropriate recommendations in due course." Communiqué (September 28, 1987), para. 7.

[54]Collecting macroeconomic and financial data for all member countries inevitably involves lags. The calculated quotas for the Eighth Review were based on 1980 data, and the Ninth Review was based on 1985.

GDP at 7½ percent, trade at 9½ percent, and the variability of trade at 10½ percent.[55] Using the formulas agreed upon for the Eighth Review, these changes—accumulated over five years—increased the aggregate of calculated quotas by 57 percent (from SDR 209 billion to 329 billion) and implied that quotas would have to be nearly quadrupled (from SDR 90 billion) to reach the calculated level.[56]

Notwithstanding the lack of consensus in the Interim Committee, most constituencies responded positively to these findings and favored increasing quotas. As early as September 1987, all but two Executive Directors expressed implicit or explicit support for at least a 50 percent increase, and several argued for a doubling or more. The two exceptions represented the countries with the largest quotas. The U.S. Director (Charles H. Dallara) maintained that the case for a quota increase had not been established, and the U.K. Director (Timothy P. Lankester) maintained that only a minimal increase was warranted.[57]

In addition to citing the obvious fact that quotas had fallen (and were continuing to fall) in relation to world trade and other relevant variables, those who argued for a major increase stressed the implications for the demand for Fund resources of the international debt crisis, the large imbalances among the major industrial countries, and the uncertainties caused by such global imbalances as the sharp declines in primary commodity prices. In response, the U.S. and British resistance stemmed from several arguments. First, these Directors noted that the standard calculations of the Fund's liquidity position allowed for drawings by industrial countries. Since those countries seemed unlikely to draw on Fund resources in the foreseeable future, the Fund could, in their view, take a less conservative approach to its liquidity needs. Second, they wanted the Fund to be more cautious in lending to heavily indebted countries that could ill afford to take on new debts, especially in view of the still-growing problem of arrears to the Fund. Third, they believed that developing countries could obtain more credits from other lenders if the Fund concentrated more on helping countries design adjustment programs and less on lending them money. In other words, the Fund could give greater emphasis to its catalytic role. Fourth, the ESAF—which was just beginning to play a significant role in providing concessional loans to low-income countries—could be

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[55]The formula for measuring variability of trade (see Appendix III) was not normalized. To a first approximation, with no change in the frequency distribution, trade (X') and variability (V') would rise at the same rate. The increase in the variability of trade from 1980 to 1985 was due primarily to the large declines in prices of many primary commodities, including petroleum. Over the period, this "variability" reduced the trade balances of most developing countries and raised those of most industrial countries. The data, however, were applied symmetrically and served to raise the calculated quotas of both groups.

[56]"Ninth General Review of Quotas—Quota Calculation," EB/CQuota/87/1 (June 5, 1987), pp. 5 and 11.

[57]Executive Directors' positions as of September 1987 were summarized by the Managing Director at EBCQM/87/4 (September 17, 1987), pp. 3–5. Lankester's and Dallara's positions were stated at EBCQM/87/3 (same date), pp. 21–24.

expected to take some of the pressure off the Fund's own resources in coming years.

The first real break in these positions came in March 1989 with the announcement of the Brady Plan for relieving the debt burdens of developing countries (Chapter 11). U.S. Treasury Secretary Nicholas Brady (who had replaced Baker a few months earlier), in announcing the plan, signaled a willingness to consider a quota increase "before the end of the year" to help finance the Fund's role in implementing it. He was, however, still unwilling to propose an amount that the United States would be prepared to accept.

The next movement came in November, within days of the opening of the Berlin Wall. The Fund already was considering stand-by arrangements for Hungary and Poland, and the likelihood was rising that other European countries would soon be joining the Fund and requesting financial support. In recognition of the demands that would be placed on the Fund in that event, the U.S. Director (Thomas C. Dawson II) informed his colleagues that the administration was prepared to support a quota increase of up to 35 percent. That level, though, was well below what most others regarded as a bare minimum under the circumstances. Exceptionally, the Saudi Arabian Director (Yusuf A. Nimatallah) averred that even the U.S. suggestion would be "more than sufficient," and the U.K. Director (Frank Cassell) indicated that it was about as much as his authorities could be persuaded to accept. Everyone else (19 Directors, with 70 percent of the voting power) judged that a doubling of quotas was desirable and that an increase of two-thirds was the minimum that was needed, in view of the new demands on the Fund and the delays in concluding the review.[58]

The third step toward resolving the debate came in March 1990. All three of the holdouts then indicated that they could go along with a 50 percent increase, as did most of those who had wanted a much larger increase. Dawson initially tied his acceptance to a request that the next review be postponed, but that idea was resisted and was dropped from the report sent to the Board of Governors. In June 1990, the governors approved the report, which called for a 50 percent increase in quotas, to SDR 135 billion ($177 billion).[59]

As a general issue, the distribution of the increases across the membership was handled with much less controversy than in the Eighth Review. At the outset, Di-

[58]Doubling the stock of quotas would have added SDR 90 billion. An increase of two-thirds represented 60 billion; a 50 percent increase, 45 billion. Dawson's position called for an increase of 32 billion, and Nimatallah expressed a preference for 25 billion. Minutes of EBM/89/154 (November 28, 1989).

[59]The final quid pro quo for U.S. approval of the increase under the Ninth Review was adoption of the Third Amendment of the Articles, which provided for the suspension of voting and related rights of countries with arrears to the Fund that were found not to be cooperating toward resolving the problem (see Chapter 16). Adoption of the Amendment delayed the implementation of the quota increase until November 1992. Work on the Tenth Review eventually was extended beyond its original 1993 deadline. In 1995, the review was concluded without any proposal for an increase, and work began immediately on the Eleventh. A resolution to conclude that review was approved by the Board of Governors in January 1998, with an increase of 45 percent (to SDR 212 billion, approximately $287 billion).

rectors agreed not to fiddle any more with the formulas.[60] They acknowledged that, despite the progress made in the last round, some quotas were still seriously out of line, but they preferred to continue to tackle the problem gradually and with the same tools. The "calculated quotas" therefore were measured as before, and the increases were to be distributed in the same manner but in reversed proportions (60 percent in proportion to existing quotas and 40 percent in proportion to the calculated values).

One new issue had arisen since the previous review: how to treat countries that were in arrears in their payments to the Fund. After some discussion of the possibility of denying increases to such countries (which could have led to complicated procedures after arrears were settled), the Board accepted a staff recommendation to treat the problem as a technical matter involving the prescribed order of payments. That is, a member country would not be allowed to pay for a quota increase until it had repaid any overdue obligations to the Fund's General Resources Account. If arrears were not settled within a limited time frame, the proposed increases would lapse.[61]

The most difficult distributional issue involved a high-profile political battle among the major industrial countries. In January 1988, the Japanese Executive Director (Koji Yamazaki) argued that "the distribution of Fund quotas" was "unjustified" and was "clearly inconsistent with world economic realities."[62] Japan's share in Fund quotas (then 4.7 percent) was among those that were most below calculated levels, and Yamazaki had an unassailable argument that his country's share should be raised substantially. He continued to press the case, as did the finance minister (Kiichi Miyazawa) at the Interim Committee. Japan had begun to play a substantial role as a Fund creditor and provider of official development assistance, which gave the authorities a strong bargaining position. In April 1989, the Interim Committee implicitly acknowledged the point by agreeing that "the size and distribution of any quota increase should take into account changes in . . .

[60]The most serious effort to change the formulas was made by Arjun K. Sengupta (India), who made the case that an index of each country's poverty should be included as a determinant of quotas. That argument was resisted on the grounds that the Fund had other means of providing special assistance to low-income countries and that a shift in the distribution of quotas toward poor countries would weaken the benefits of the increase for the Fund's liquidity. See "Some Issues Relating to Criteria for Determining IMF Quotas—A Technical Note," EB/CQuota/88/4 (March 9, 1988), and minutes of EBCQM/88/3–4 (March 14, 1988). Also see the staff evaluation, in "Ninth General Review of Quotas—Review of a Technical Note on Some Issues Relating to Criteria for Determining Fund Quotas," EB/CQuota/88/9 (October 28, 1988), and minutes of EBCQM/88/10–11 (November 18, 1988).

[61]Minutes of EBCQM/88/4 (March 14, 1988), p. 16. In its final form, this rule specified that a country would not be allowed to consent to or pay for the increase until it had settled its arrears to the GRA. See Board of Governors Resolution No. 45–2 (June 28, 1990); in *Annual Report 1990*, p. 103. As a result of that provision, despite multiple extensions of the allowed period, five countries could not consent to the increases proposed under the Ninth Review: Iraq, Liberia, Somalia, Sudan, and Zaïre (Democratic Republic of the Congo). Four others settled their arrears and consented after the general increase took effect: Haiti, Peru, Vietnam, and Zambia.

[62]Minutes of EBCQM/88/1 (January 11, 1988), p. 3.

members' relative positions in the world economy" since the previous review (communiqué, para. 5; also see Chapter 11, footnote 11, p. 480).

Although Japan's request was viewed sympathetically, it raised two interrelated problems. First, the quota shares of all other members would be reduced proportionally, and the size of the shift would have to be substantial to make a real difference to Japan's position in the Fund. Everyone agreed that reducing the aggregate quota share of developing countries to "pay for" the Japanese request should be avoided if possible. Second, raising Japan's share would require downward adjustments to the hierarchical positions of some other major industrial countries. Japan's quota was the fifth largest, but by any measure it should have been second only to the United States. To raise it to that level without other changes would mean lowering the United Kingdom, Germany, and France (then ranked second through fourth) by one notch. The U.K. quota, however, was most clearly overstated, because the British economy had declined in relative importance since Bretton Woods. Discussions therefore focused on ways to adjust quotas among the major industrial countries to achieve a more modern balance.

The key to both issues was for the United Kingdom to absorb the lion's share of the increase in the Japanese quota. In December 1989, Cassell reported that the U.K. authorities were prepared to reduce the increase in the U.K. quota by enough to eliminate the decreases that would otherwise be forced on developing countries.[63] The effect of that concession was that about half of the effect would be absorbed by the United Kingdom and half by other industrial countries. Germany would then remain in third position, Britain would drop to fourth, and France would drop to fifth. That proposal went a long way toward solving the problem, but the French authorities refused to accept the proposed drop in their position.[64]

Trying to resolve what was rapidly becoming an acrimonious and very public fight between two major countries (the United Kingdom and France) placed Executive Directors in an awkward position (to say the least). In January 1990, the Board agreed reluctantly to allow the distribution of G-7 quotas to be decided outside the institution, by that group alone. In effect, the Board would agree on an aggregate G-7 quota, based on the procedures being applied uniformly to all members, and then would ratify an internal G-7 agreement on the distribution. That solution was inelegant, and several Directors worried about setting a precedent for future decisions, but it was the only way out.

The G-7 finance ministers agreed on a solution at the beginning of May 1990. Showing exceptional delicacy, they decided that Germany and Japan should have equal quotas (6.1 percent of total Fund quotas for each country), second to the United States (19.6 percent), and (as a compromise proposed by the French authorities) that France and the United Kingdom should also have equal quotas (5.5

[63]Minutes of EBCQM/89/16 (December 20, 1989), p. 5.

[64]Letter from the Pierre Bérégovoy (Minister of Economy, Finance, and Budget for France) to Camdessus (May 2, 1990), in IMF/CF (S 1230 "Ninth General Review of Quotas, February 1990–May 1990").

percent), tied for the fourth spot. With some grumbling about the procedure, the Executive Board accepted that distribution later in the month.[65]

Two other requests for ad hoc increases—from Iran and Korea—failed to muster sufficient support. The request from Iran was intended to compensate for their not having consented to either of the previous two increases (see above, p. 854). In making the case for Korea, Charles R. Rye (Australia) pointed out that the Korean economy had grown very rapidly in the 1980s and that the country's quota was even more out of line with the calculations than Japan's. Creditors who sympathized with Korea found it difficult to support that request without taking the politically awkward step of supporting Iran as well. No one spoke out openly against the specifics of either request, but few creditors were willing to endorse either one.[66]

Access Policies

An increase in quotas does not translate automatically into larger amounts that countries can borrow from the Fund. The other variable in that equation is the "access limit," the ceiling on Fund credits in relation to a member's quota. When the Fund was designed in the early 1940s, quotas were conceived primarily as borrowing rights,[67] and each country's access limit was to be equal to its quota. The 25 percent of quotas that all countries would deposit in gold, plus the 75 percent that the United States and the United Kingdom would deposit in dollars and sterling (respectively), plus whatever other deposited currencies would eventually become usable would provide the liquid assets to finance credits to member countries. No one knew in advance how these ratios would work out in practice, but they were thought to be a safe and conservative starting point.[68] If they turned out to be too conservative, then the Fund could use the flexibility allowed by the Articles to waive the credit ceiling.[69]

[65]Minutes of EBM/90/78 (May 21, 1990).

[66]"Ninth General Review of Quotas—Considerations Relating to Special or Ad Hoc Increases in Quotas," EB/CQuota/88/8 (September 16, 1988) and minutes of EBCQM/88/10–11 (November 18, 1988).

[67]The April 1943 version of the British plan for the Fund (the Keynes Plan) put it this way: "Each member State shall have assigned to it a *quota*, which shall determine the measure of its responsibility in the management of the Union and of its right to enjoy the credit facilities provided by the Union" (Horsefield, 1969, Vol. 3, p. 22; original italics).

[68]For example, if the currencies of countries with 50 percent of total quotas were usable for Fund financial operations, then the stock would clearly suffice to finance credits of 100 percent of quota to countries holding the other 50 percent. As a perhaps more realistic initial assumption, if only U.S. dollars were usable, then the stock would suffice to finance credits at that rate to countries holding half of the remainder (since the U.S. quota was just over one-third of original quotas).

[69]Article V, Section 3(b), specifies certain conditions on "purchases" (drawings), one of which is that they "not cause the Fund's holdings of the purchasing member's currency to exceed two hundred percent of its quota." Since holdings equal 100 percent for a country that has drawn its reserve tranche, that provision notionally restricts credit access to 100 percent of the member's quota. Section 4 of the same Article, however, allows the Fund, "in its discretion," to waive that limit.

Policies Before 1980

The history of the Fund's access policies, in a nutshell, shows a loosening of the limits through the early 1980s, in three major steps: the establishment of independent or "floating" facilities in the 1960s and 1970s, the approval of higher limits for extended arrangements in the 1970s, and the use of borrowed funds to finance much larger access beginning in the late 1970s (Figure 17.1).[70] Until that last "enlarged access" policy came into effect, the gradual rise in access limits had roughly compensated for the decline in quotas relative to world trade, so that the amounts that countries could borrow grew *pari passu* with world imports (see the dashed line in the diagram).[71] For a few years in the early 1980s, member countries theoretically could have borrowed up to 775 percent of quota, and potential access in relation to world trade was more than doubled from its historical levels. Access limits then stabilized relative to quotas in the second half of the 1980s and were reduced in the 1990s.

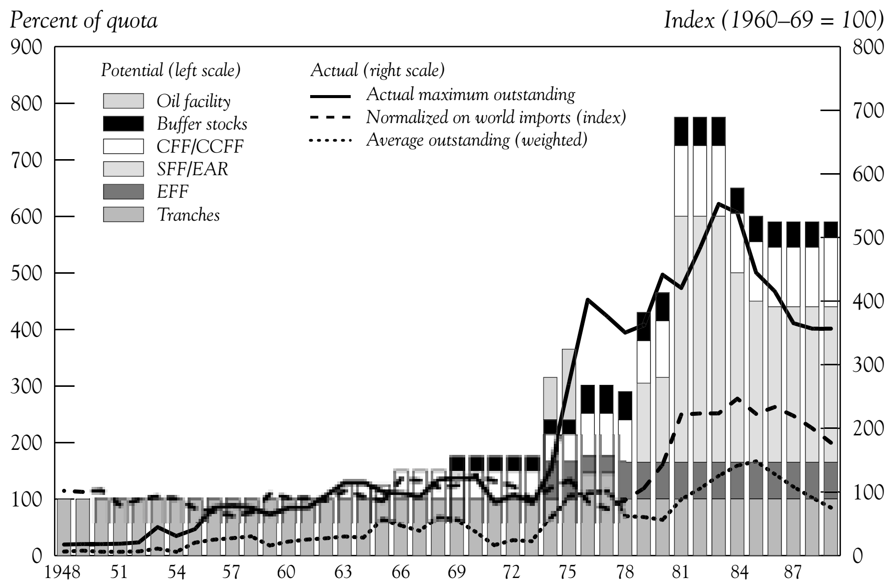
Until 1963, a country's quota placed a binding limit on the amount that it could borrow. When the Fund established the Compensatory Financing Facility (CFF) that year (see Chapter 15), the Executive Board agreed that the 25 percent of quota available under the new facility would not necessarily restrict the member's ability to borrow under ordinary access rules. The rationale was that if borrowing from the CFF was truly to "compensate" countries for temporary declines in export revenues, the facility had to be separate from and additional to any borrowing under the regular tranche policies. Thus the potential use of resources rose from 100 percent to 125 percent. When the CFF was liberalized in 1966, access was raised to 50 percent, drawings were allowed to "float" relative to ordinary usage,[72] and potential total access rose to 150 percent. Three years later, the Buffer Stock Financing Facility (BSFF) was established on similar terms. Although a member could borrow up to 50 percent of quota under either the BSFF or the CFF, the combined limit was set at 75 percent. This decision raised the ceiling on total usage to

[70]Data in Figure 17.1, and the discussion in this section, exclude loans made through the Trust Fund, the SAF, and the ESAF. Those loans are financed from administered accounts that are independent from the Fund's general resources. Total ceilings are not strictly commensurate over time, because of overlapping limits, the presence or absence of a cumulative ceiling, and shifting approaches to flexibility in exceeding the limits. Those complexities are discussed below. For years in which access limits changed, the plotted value is the mode for the year.

[71]The normalized aggregate access limit shown in Figure 17.1 has been calculated by dividing aggregate maximum access in SDRs (A) by aggregate world imports (M) rather than by quotas (Q) and then rescaling to give an average value of 100 in the 1960s. That is, if the access limit (L) in percent of quota is $L = A/Q$, the normalized limit is $L' = L \times Q/M$, converted to an index number.

[72]Specifically, "floating" means that borrowing through the facility does not count toward the country's access limits under the Fund's tranche policies. As explained in Chapter 15 (p. 725), the effect of introducing floating in 1966 was that a country with no other outstanding obligations could borrow 25 percent of its quota through the CFF and then borrow another 25 percent under the regular tranche policies without being subjected to the higher conditionality of an upper-tranche arrangement.

Figure 17.1. Potential and Actual Access, 1948–89



175 percent.[73] As a consequence, the Board began granting waivers of the 100 percent ceiling with increasing frequency.[74]

The oil facilities provided oil-importing countries access to 75 percent of quota in 1974 and 125 percent or more in 1975, in addition to other credits.[75] That access was financed by borrowing from a group of creditor countries (see below). Once those borrowed funds were fully committed, this additional access lapsed.

Under the Extended Fund Facility (EFF), established in 1974, a member country could borrow up to 140 percent of its quota, in addition to drawing on its reserve tranche,[76] the CFF, and the BSFF. Moreover, for two years starting in 1976, the Ex-

[73]On the development of access policies for the CFF, see Horsefield (1969), Vol. 2, p. 421, and de Vries (1976), Vol. 1, p. 262. The BSFF limits are discussed in de Vries (1976), Vol. 1, p. 280.

[74]Through 1973, four countries marginally exceeded the ceiling specified in Article V: Egypt in 1963–64, Chile in 1964, and Sri Lanka and Ghana in 1968–70. Beginning in 1974, waivers became routine and covered much larger deviations.

[75]The terms of the 1975 Oil Facility permitted countries to cover up to one-third of the increase in the cost of their oil imports, regardless of the quota-based ceiling (125 percent). In June 1976, Korea's total indebtedness to the Fund peaked at just over 400 percent of quota, of which more than three-fourths was due to drawings through the oil facilities.

[76]Until May 1981, countries were expected to draw their reserve tranche balance before obtaining Fund credits. The Board then dropped that requirement in order to encourage members to retain reserve tranche positions as an important part of their official international reserves. See "Treatment of Reserve Tranche," SM/81/71 (March 30, 1981); minutes of EBM/81/65 (April 22, 1981); and Decision Nos. 6830- and 6831-(81/65), in *Annual Report 1981*, pp. 162–63. The policy change benefited indebted countries in three ways. First, it raised their gross reserves, which

ecutive Board approved a temporary policy that redefined each of the four credit "tranches" to equal 36.25 percent of the member's quota, instead of 25 percent. That change added another 45 percent of access, to a total of about 300 percent of quota, until the Second Amendment became effective in April 1978 (see de Vries, 1985, pp. 527–29).

This gradual augmentation of access to the Fund's resources was matched by an overall increase in demand. By the mid-1970s, the outstanding obligations of countries that had borrowed from the Fund *averaged* about 100 percent, the original ceiling (see Figure 17.1).[77] By then the oil facilities had already been exhausted, and the temporary augmentation of the credit tranches was about to lapse. If a new shock hit the world economy, the Fund would be hard pressed to meet the demand for credits.

The Fund prepared for the next crisis by establishing the Supplementary Financing Facility (SFF) in February 1979, financed by borrowing from official creditors and expected to have a life of just two years.[78] The SFF permitted countries with a stand-by or extended arrangement to obtain supplementary and parallel credits financed by the borrowed resources. That raised maximum access sharply, to more than 450 percent of quota,[79] and established what became known as the "exceptional circumstances clause." Whatever quantitative ceilings were in place could be exceeded, but only after a determination by the Executive Board that the

improved liquidity since countries obtained a five-year maturity on their liabilities to the Fund and retained a highly liquid asset in their reserve position. Second, at the time the decision was enacted, the rate of remuneration on reserve positions was above the rate of charge on borrowings (see below, section on "Sharing the Burden: Who Pays for the Fund?" pp. 899–910). A substantial portion of countries with outstanding debit balances took advantage of this provision. Third, as discussed above (footnote 14, p. 855), it gave indebted countries a means of eliminating any cost of increasing their Fund quotas.

[77]"Actual maximum outstanding" is calculated as the maximum value of Fund credit outstanding, expressed as a percentage of quota, for any member during the year. "Average outstanding" is the total amount of credit outstanding, as a percentage of the sum of quotas of countries with outstanding obligations.

[78]For the background to the establishment of the SFF, see de Vries (1985), Chapter 28 and Vol. 3, pp. 512–15. The borrowing arrangements are discussed below (p. 886).

[79]The overall access limit was the sum of several overlapping limits on individual facilities and arrangements. A country could borrow up to 150 percent of quota through a combination of CFF and BSFF credits and 140 percent via an EFF arrangement. Supplementary credits through the SFF could double the size of the arrangement, for a maximum EFF access of 280 percent. All of those amounts were additional to a drawing of the first credit tranche (25 percent), so the total available was 455 percent of quota. If the country had outstanding obligations to the oil facilities, its cumulative stock of indebtedness could be even higher. As part of the activation of the SFF in February 1979, a cumulative limit (excluding CFF and BSFF drawings) was set at 202.5 percent unless the country had an EFF arrangement, in which case it was 305 percent. In September 1979, in response to the oil price increases of that year and the general deterioration in the global economy, the Board accepted an increase in the exclusive cumulative limit to 465 percent (without regard to the type of arrangement). The 465 percent limit was established via a statement issued by the Managing Director at the opening of the Executive Board's discussion of the autumn 1979 World Economic Outlook. See minutes of IS/79/7 (September 12, 1979), pp. 3–4.

borrowing country faced what were then called "special circumstances" warranting the exception.[80]

Enlarged Access

Once the second oil shock hit in 1979, even these limits seemed inadequate, at least until the Seventh Quota Review could take effect. As discussed in Chapter 13, the Fund was encouraged—especially at the Annual Meetings in Belgrade in 1979—to increase its lending so as to help "recycle" the growing surpluses of oil-exporting countries. Meeting in Hamburg in May 1980, the Interim Committee backed up that call and authorized the Managing Director to initiate discussions with potential lenders to further augment the Fund's resources. In response, Executive Directors agreed in July that "we should be prepared to respond on a larger scale than in the past to the needs of our member countries," and that access of 600 percent of quota over three years could be approved.[81] They also set out to establish a policy permitting enlarged access on a more sustained basis than before.[82]

The quota increases that took effect in the last months of 1980 raised the Fund's liquidity, but that result was partially offset by the fact that most of the money borrowed to finance the SFF was already committed. Moreover, the staff was projecting a sharp increase in the demand for stand-by arrangements in response to the 1979–80 increase in oil prices. Either the Fund would have to undertake new borrowing on a large scale, or it would have to scale back its access limits. As a lower extreme, if potential access were to be held constant in absolute value, with no effect from the quota increase, then the cumulative access limit would have to be cut from 600 to 400 percent of quota.[83] To strike a balance between the need to main-

[80]Note that the exceptional circumstances clause is separate from the routine waiver that is still required whenever the Fund's holdings of the country's currency will rise above 200 percent of quota. The clause applies both to the size of the arrangement (the flow over a specified period of time) and the cumulative stock of indebtedness, and it relates to excesses of access limits established by the Executive Board rather than to excesses of the limit on the Fund's holdings specified in the Articles. The Executive Board invoked the clause twice in April 1978, in anticipation of the SFF coming into effect: for stand-by arrangements for Turkey (150 percent of quota) and Zambia (177 percent). Under the enlarged access policies of the 1980s, the clause became almost moot. The only time it was invoked during the period covered by this History was for the extended arrangement with Mexico approved in 1989 (see Chapter 11), which had the potential to raise Mexico's obligations to 534 percent of quota while the normal limit on cumulative access was 440 percent.

[81]In addition to limits on total access to Fund credits, the Board has set what might be called "speed limits": ceilings on annual and triennial access. Article V of the original Articles of Agreement limited net annual credit extension to 25 percent of quota, unless waived. That limit was dropped in the 1978 amendments. Thereafter, the Board typically imposed annual limits, triennial limits that were always set at or close to three times the annual limits (and therefore were operationally redundant), and cumulative ceilings that were usually around four times the annual limits.

[82]Chairman's summing up, minutes of EBM/80/107 (July 18, 1980), p. 31.

[83]The Seventh General Review raised quotas by 50 percent; $600 = 400 \times 1.5$. The calculation of potential access, which is the way the matter was presented to the Executive Board, excludes CFF and BSFF drawings, on which the combined access limit of 150 percent was not reduced. To hold total potential access constant would have required reducing the exclusive cumulative limit to 350 percent.

tain liquidity and the desire to meet members' requests for financing, the staff suggested a compromise of 450 percent over three years and 600 percent cumulatively. Since stand-by and extended arrangements were limited to three years, those figures implied that in most cases countries could not add more than 450 percent to existing indebtedness through a single arrangement, but prolonged borrowing could lead to higher indebtedness over time. The Board accepted that proposal in January 1981 and agreed to establish—as a successor to the expiring SFF—the elaborately named and oddly acronymed "Policy on Enlarged Access to the Fund's Resources" (EAR).[84]

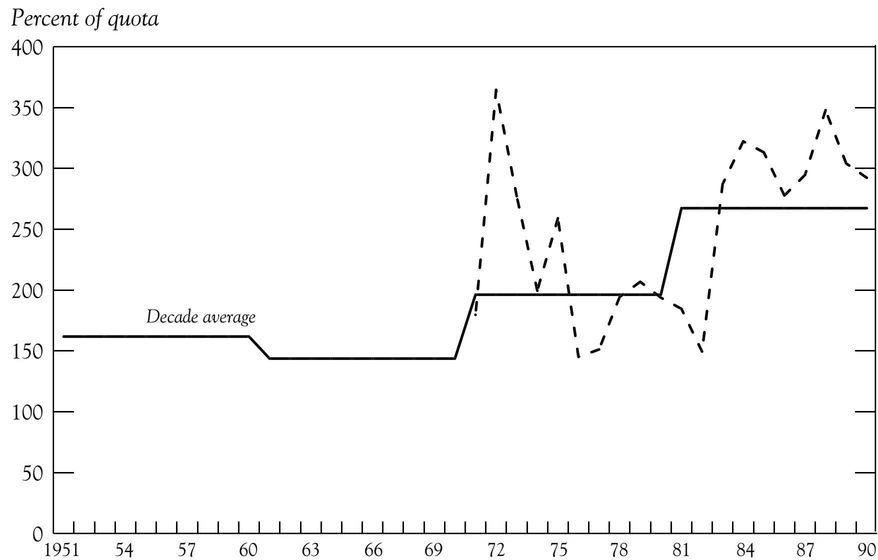
At the time the EAR was established, access limits that high could be sustained only through borrowing by the Fund. As discussed below, no one wanted the Fund to become a permanent borrower. The EAR therefore was established as a temporary policy, and the question arose as to how much access the Fund could allow on a sustained basis, without recourse to borrowing. To answer that question, the staff used the Fund's estimated "self-financing ratio": the ratio of potential demand to potential supply of ordinary (nonborrowed) resources. Forward-looking estimates would have been subject to wide margins of error, so the actual calculations were based on past experience. Suppose, for example, that the Fund's "usable" financial assets were equivalent to 50 percent of quotas, and that the demand for those resources came from countries holding 25 percent of total quotas. The Fund could then allow access to average 200 percent of quota (50/25) without having recourse to borrowing. Since average access will always be less than the maximum, the limit could be set somewhat higher, but how much higher is difficult to determine. The applicability of this approach is limited for that reason, and also because neither the level of usable resources nor the demands on them can be accurately forecast. Even so, a retrospective look at the self-financing ratio provides some insight into the range of sustainable figures for access limits.

The calculated ratio, shown in Figure 17.2, is quite volatile over time, mainly on account of fluctuations in the list of countries with outstanding obligations. In the 1970s, the self-financing ratio ranged from a peak of 365 percent in 1972 down to 145 percent four years later.[85] Taking a conservative view, these data suggested that average access of at least 140 percent could be financed by quota resources alone, while much higher access might require recourse to borrowing by the Fund. Since average access was rising at the time and would soon reach that level (refer again to Figure 17.1), the Fund seemed to be driving close

[84]"Enlarged Access to Fund Resources," EBS/80/262 (December 4, 1980); and minutes of EBM/80/187–188 (December 19, 1980), EBM/81/5–6 (January 9, 1981), and EBM/81/39 (March 11, 1981). The implementing decision was approved in March 1981; see Appendix IV to this chapter.

[85]See "Review of the Policy on Access to Fund's Resources—Financial Considerations," EBS/83/133 (June 28, 1983), Appendix Table V, p. 28; and "Ninth General Review of Quotas—Consideration Relating to the Increase in Quotas," EB/CQuota/88/1 (February 17, 1988), p. 29. The data cited here are updated staff estimates from those tables.

Figure 17.2. Self-Financing Access Ratio, 1951–90



Note: For definition of self-financing ratio, see text.

to the edge of the prudent range. In fact, however, the average ratio was about to rise sharply because no industrial country would be borrowing from the Fund in the 1980s. In retrospect, the self-financing ratio would average 267 percent in the 1980s and would lie above 200 percent in every year from 1983 on.

After the Eighth Quota Review was completed in 1983, the Executive Board reviewed the EAR, decided to retain the policy, but also decided not to raise access in absolute terms. In other words, the direct effect of the 1983 quota increases was to strengthen the Fund's liquidity but not necessarily to allow it to raise the amount of lending except through the "floating" special facilities.[86]

The first discussion on this issue, in July 1983, revealed a deep split in the Board. Three groups of Directors, each holding approximately one-third of the voting power, favored (1) reducing access in absolute terms to protect the Fund's liquidity, (2) raising it to meet the demands of the membership for new credits, or (3) holding it steady to balance those two considerations. Three more days of discussion in late August and early September produced no material change in those views, and the stalemate was then reported to the Interim Com-

[86]Access to credits through the CFF and BSFF was subject to ceilings of 125 percent and 50 percent, respectively, from May 1981 (when the cereals window became effective) through 1983. Those limits were reduced to 105 percent and 45 percent in January 1984, in response to the general increase in quotas. For a country with an average quota increase (47.5 percent) after the Eighth Review, the cut in percentage terms implied an increase of 26 percent in terms of SDRs. See Decision No. 7602-(84/3), January 6, 1984; in *Annual Report 1984*, p. 138.

mittee.[87] The split was not just between creditors and debtors, as one might expect. Within the G-5, the U.S. authorities were holding out for the low end (no increase in absolute terms), while the French were insisting on at least reaching the middle ground with a meaningful increase. The British were trying to craft a compromise under which absolute access would rise but countries would have to meet more difficult conditions to qualify for the increase.

In September 1983, the Interim Committee agreed to the British proposal to establish a temporary two-tier system of access limits, with an upper limit to be applied for countries with particularly serious balance of payments problems and particularly strong adjustment programs.[88] The upper limit permitted cumulative access of 500 percent of quota (reduced from 600 percent), while the lower ceiling was set at 408 percent. The lower limit was set so as to keep access unchanged in absolute terms for countries with an average quota increase.[89] The implication of the two-tier system thus was that countries could get up to 23 percent additional access, or about half the size of the general quota increase, but only by demonstrating that they faced major problems and were implementing strong policies.

The two-tier system was bewildering, especially when viewed in relation to the exceptional circumstances clause, which provided for access above the upper limit. The staff and the Board specifically rejected the idea that access in the upper tier would require a finding of "exceptional circumstances," and they set out to try to define specific criteria for it. Not surprisingly, that attempt failed. What emerged was an agreement that the staff would attempt to provide more detailed justifications for programs with access above the lower limit. In effect, the upper limit would become the operative ceiling, but efforts would be made to keep average access from rising commensurately.[90]

Because the EAR was a temporary expedient, the Board agreed to review the access limits each year. Those reviews became the occasion for a perennial tug-of-war between the defenders of the Fund's liquidity and the advocates for borrowing

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[87]See minutes of EBM/83/110–111 (July 25, 1983), EBM/83/126–127 (August 31), EBM/83/132–133 (September 7), EBM/83/134–135 (September 8), and "Report to the Interim Committee on the Policy on Access to the Fund's Resources," SM/83/198, Rev. 2 (September 9). Also see "Review of the Policy on Access to the Fund's Resources—General Considerations," EBS/83/132 (June 27, 1983) and "Review of Policy on Access to the Fund's Resources—General Considerations," Sup. 1 (July 18, 1983), "Review of the Policy on Access to the Fund's Resources—Financial Considerations," EBS/83/133 (June 28, 1983), "Enlarged Access—Scale of Access and Limits," EBS/83/172 (August 12, 1983), and "Review of the Policy on Access to the Fund's Resources—Legal and Policy Considerations," SM/83/194 (August 19, 1983).

[88]The proposal was introduced during the July Board meeting by the Executive Director for the United Kingdom, Nigel Wicks. It was advanced within the G-5 by the U.K. Deputy, Geoffrey Littler, and was tabled at the Interim Committee by the Chancellor of the Exchequer, Nigel Lawson. According to Lawson (1992, p. 518), the final compromise numbers were worked out during a meeting of the Commonwealth finance ministers in Trinidad the week before the Interim Committee meeting in Washington.

[89]Quotas were increased by an average of 47.5 percent; $408 \approx 600 \div 1.475$. For the full text, see Decision No. 7600-(84/3), January 6, 1984; in *Annual Report 1984*, p. 135.

[90]Minutes of EBM/83/166–167 (December 2, 1983). Also see "Criteria for the Amount of Access in Individual Cases," EBS/83/233 (October 31, 1983).

countries. When the Board met in September 1984 to consider the limits for 1985, some creditors expressed concerns that enlarged access was enabling many countries to become prolonged users of the Fund's resources (see Chapter 13). In their view, the time had arrived to begin phasing out the policy. Mary K. Bush (Alternate—United States), Hirotake Fujino (Japan), Guenter Grosche (Germany), and T.A. Clark (Alternate—United Kingdom) called for reducing the cumulative limit to the range of 350–400 percent of quota, from the prevailing level of 500 percent. De Larosière, however, made a personal appeal to maintain the existing levels, because otherwise the Fund would have to cut off lending to several major borrowers that were nearing the limits and for which the Fund could continue to play a positive role.[91] As a compromise, the Interim Committee agreed on a small reduction, to 450 percent with no reduction in the lower ceiling (408 percent), a few weeks later. An implementing Board decision was adopted in November.[92]

A year later, staff and management expressed a preference for retaining the ceilings at their 1985 levels but accepted that the cumulative ceiling could be cut to 400 percent of quota or even to 375, as a signal that enlarged access would indeed be phased out over time. To go further would be risky. Three countries would soon reach the existing ceiling of 450 percent, and if it were reduced to 350 percent, more than 30 countries would become ineligible for additional credits by 1986.[93] The major creditors, however, took similar positions as in 1984. Dallara, Grosche, and Fujino asked that the cumulative limit be cut to about 350 percent for 1986, but that position was not supported by the majority of the Board.[94]

Meeting in Seoul, Korea, in early October, the Interim Committee decided that the EAR should be retained with "only modest adjustments" in access limits. The Committee decided that the cumulative limit should be set at 440 percent for 1986, down just slightly from 450 percent in 1985. Nonetheless, several committee members—notably the finance ministers for China, France, India, and Italy—objected strongly on principle to the reduction and went along solely to gain consensus on the extension of the EAR. The finance minister for India, Vishwanath Pratap Singh, went public with his reservations and stated in his Annual Meetings

[91]See "Access Limits for 1985—Preliminary Policy Considerations," EBS/84/168 (August 8, 1984), and the minutes of EBM/84/134–135 (September 5, 1984). At the end of 1984, five countries had outstanding credits (exclusive of CFF and BSFF obligations) in excess of 300 percent of quota: Jamaica (367 percent), Turkey (329 percent), Yugoslavia (321 percent), Côte d'Ivoire (304 percent), and Sudan (303 percent). In addition, existing commitments to Uganda, Mexico, Brazil, and Malawi would carry them above 300 percent if the arrangements then in effect were fully utilized.

[92]Minutes of EBM/84/165 (November 16, 1984), pp. 3–4.

[93]"Access Limits for 1986—Preliminary Policy Considerations," EBS/85/174 (July 23, 1985), p. 16. For the detailed calculations, see the attachment to "Access Limits for 1986," memorandum from C. David Finch (Director of the Exchange and Trade Relations Department) to the Managing Director (September 24, 1985), in IMF/RD Managing Director file "Access Limits, 1985" (Accession 88/274, Box 8, Section 269).

[94]Minutes of EBM/85/137–138 (September 11, 1985). The relevant statements by Fujino, Grosche, and Dallara are on pp. 15, 18, and 22, respectively, of meeting 85/137. For the overall distribution of votes, see the Chairman's summing up at meeting 85/138, p. 14.

speech that he, "along with many others," had objected to the cuts during the Interim Committee meeting (IMF, *Summary Proceedings*, 1985, p. 96). The Board, after some further grumbling, implemented the decision in December.[95]

After that battle, an implicit truce was reached, and no further cuts were made in the access limits. The enlarged access policy remained in force until November 1992, when the quota increases of the Ninth Review took effect.

Borrowing by the Fund

Although the primary source of financing for Fund operations has always been its quotas, it also has the option of borrowing from any source—member countries, other official agencies, or private capital markets. While the option of going to private markets was never exercised, the Fund borrowed from official sources on several occasions. Total indebtedness peaked in 1986, at SDR 14.6 billion (Figure 17.3), the equivalent of 16 percent of quotas or $17 billion.[96]

Borrowing by the Fund began with the establishment of the General Arrangements to Borrow (GAB) in 1962. Under those arrangements, the G-10 (and, later, Switzerland) agreed to lend to the Fund, up to a specified maximum, to help finance drawings by GAB creditors. Because those creditors drew on the Fund only occasionally, the GAB was activated only a few times.[97]

On two occasions prior to the 1980s, the Fund entered into bilateral borrowing arrangements to finance specific drawings. The first occasion was in 1966, when the Fund borrowed $250 million in lire from Italy to lend to the United States through a gold tranche drawing.[98] In 1977, the Swiss National Bank extended credit lines under which the Fund borrowed the equivalent of SDR 154 million to

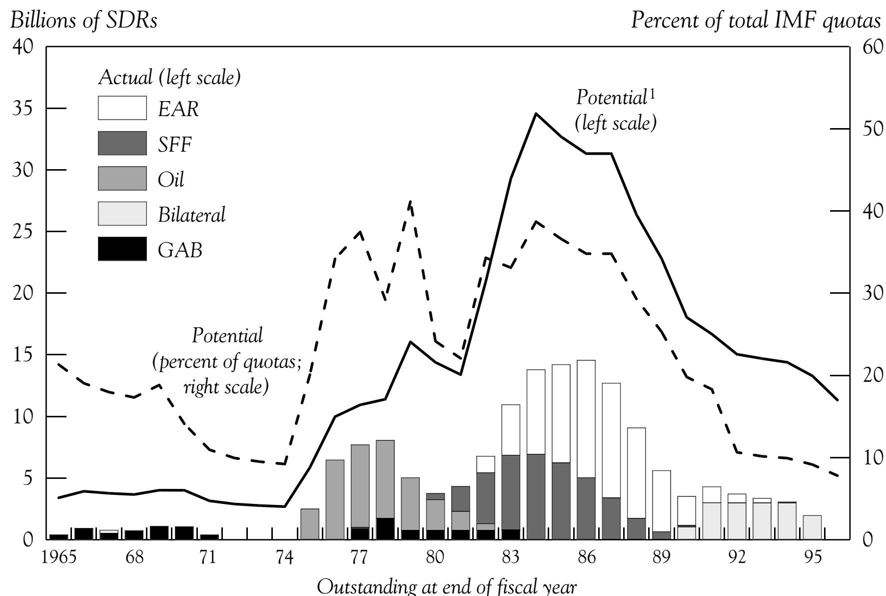
[95]Minutes of EBM/85/177 (December 9, 1985). The Board had a dual decision to take: to extend the EAR for the coming year and to set access limits under that policy. The extension required an 85 percent majority, while the percentage limits required only a simple majority of votes cast. Although Directors with a majority of the votes preferred to keep access limits unchanged, the three chairs that wanted a substantial reduction (the United States, Japan, and Germany) held approximately 30 percent of the votes and thus could have voted down the extension of the EAR and thereby have rendered the second decision moot. The potential impasse from the existence of two blocking coalitions was avoided by a decision to take a single vote on the two elements, with the nominal reduction in access limits.

[96]In addition, the Fund borrowed as a Trustee to finance the Trust Fund, the SAF, and the ESAF. That borrowing is covered in Chapter 14. For the full evolution of the Fund's policies on borrowing, see Gold (1991).

[97]The GAB agreement also specified that it could be activated only after a finding that the international monetary system was threatened with impairment. That restriction, however, was treated as a formality in considering requests for drawings by G-10 countries. Switzerland was not then a member of the Fund and therefore was not eligible to borrow from the Fund.

[98]De Vries (1976), Vol. 1, p. 376, interprets the motivation for the 1966 transaction as a shortage of lire in the Fund's accounts to cover a requested gold tranche drawing by the United States. Polak (1994, pp. 28–29) provides a fuller account and explains the motivation as an accommodation (by the Fund and the United States) to Italy's desire to substitute out of dollar-denominated securities in favor of a gold-guaranteed loan to the Fund.

Figure 17.3. Borrowing by the Fund, 1965–96



[1]Potential = actual + unused and available lines of credit.

help finance stand-by arrangements for Italy and the United Kingdom (de Vries, 1985, pp. 592–93). On that occasion, the purpose was to supplement credits being extended through the GAB.

A third form of borrowing was introduced in 1974–75, when the Fund obtained SDR 6.9 billion ($8.3 billion) in loans from 16 oil-exporting and industrial countries to finance the oil facilities. The facilities were entirely financed with those assets, and the Fund extended an equivalent amount of credit to oil-importing member countries.[99] Both the credits and the Fund's borrowings were repaid from 1979 to 1983.

[99]Two sequential oil facilities were established, in 1974 and 1975, but the distinction between them was of only technical significance. The facilities, established with funds borrowed from 16 oil exporting and industrial countries, were the first lending window at the IMF financed entirely outside the Fund's own resources. In that regard, they resembled the later Trust Fund, SAF, and ESAF, although those operations were established as Administered Accounts and thus were further separated from the normal activities of the institution. (As noted in Chapter 14, the Subsidy Account for the oil facilities was the IMF's first Administered Account.) Like the CFF and the BSFF (see Chapter 15), the oil facilities involved only nominal conditionality. Although legally available to all member countries, they were established on the understanding that they would be drawn upon only by oil-importing countries that lacked ready access to international capital on market terms. The origins and early operation of the facilities are covered in de Vries (1985), pp. 305–60; on the linkage between the increase in a country's cost of importing oil and its access to the oil facilities, see pp. 324 and 343n.

By the time covered by this History, the Fund was examining the possibility of other borrowing as a more general way to supplement quotas. These new sources included the SFF, various arrangements to finance the EAR, and an enlargement of the GAB.

Supplementary Financing Facility

The SFF, which provided supplementary credits to countries with a stand-by or extended arrangement, was financed entirely by stand-by loans to the Fund from 14 governments and central banks. A little over half of the money was lent by industrial countries, and the rest came from developing countries (Table 17.4). Of SDR 7.8 billion ($9 billion) in total lines of credit, the largest share came from Saudi Arabia (SDR 1.9 billion, or $2.2 billion), with the United States second (SDR 1.5 billion, or $1.7 billion).[100] These credit lines were drawn upon from 1979 through 1984; loans carried seven-year maturities, and all were repaid by January 1991.

Borrowing to Finance Enlarged Access

Almost as soon as the SFF came into effect, it became clear that its resources would quickly be exhausted and would not suffice to finance Fund lending into the 1980s. In the wake of the 1979–80 oil shock, projections of demand for Fund resources exceeded by a wide margin the supply available from the Seventh Quota Review and the borrowed resources of the SFF. The problem was not just that a lot of countries were likely to seek to borrow from the Fund. It was that those countries faced serious economic imbalances that would take many years to correct, and the Fund would have to prepare itself for a more sustained rise in its lending than in the past.[101] In the first part of 1980, the Fund's management therefore developed a plan to undertake new borrowing on an unprecedented scale.

The first step was to secure political support from the Interim Committee, which was meeting in Hamburg, Germany, in April 1980. The role of the Fund in "recycling" the growing surpluses of oil-exporting countries was on the agenda, and the committee would have to consider whether the Fund had the resources to do

[100]Loan commitments were denominated in SDRs, but disbursements were made in the currency indicated in Table 17.4. Half of the money was provided in U.S. dollars, and the rest in the currencies of five of the lending countries. For the background on this financing, see de Vries (1985), Chapter 28. Separate financing was contributed by 12 countries to subsidize interest payments by low-income countries on credits supported by the SFF. The SFF Subsidy Account is discussed above, in Chapter 14.

[101]In June 1980, a staff paper argued that the "current and prospective global imbalances, both in kind and size, are different from those which the Fund has been engaged in financing in the past. . . . An effective role by the Fund in the present situation would involve where necessary both larger and longer financing than in the past." The Executive Board endorsed those conclusions the following month. "Fund Policies for Adjustment Under Current Conditions," EBS/80/146 (June 30, 1980), p. 11. Also see minutes of EBM/80/106–107 (July 18, 1980).

Table 17.4. Borrowing Agreements for the Supplementary Financing Facility, 1979–84
(In millions)

	Currency Provided	Amount in SDRs	U.S. Dollar Equivalent[a]	Share (In percent)
Industrial countries		4,550	5,286	59
United States	U.S. dollars	1,450	1,685	19
Germany (Deutsche Bundesbank)	U.S. dollars	1,050	1,220	13
Japan	yen	900	1,046	12
Switzerland (Swiss National Bank)	U.S. dollars	650	755	8
Canada	U.S. dollars	200	232	3
Belgium (National Bank)	francs	150	174	2
Netherlands (Netherlands Bank)	U.S. dollars	100	116	1
Austria (National Bank)	U.S. dollars	50	58	1
Developing countries		3,234	3,758	42
Saudi Arabia (SAMA)	riyals	1,934	2,247	25
Venezuela (central bank)	bolivares	500	581	6
Kuwait (central bank)	dinars	400	465	5
Nigeria (central bank)	U.S. dollars	220	256	3
Abu Dhabi	U.S. dollars	150	174	2
Guatemala (Banco de Guatemala)	U.S. dollars	30	35	0
Total		7,784	9,044	100

[a]Dollar values are calculated at the average exchange rate for 1979–84.

the job. De Larosière acknowledged that the liquidity position was comfortable for 1980, but he argued that the Fund would have to borrow to meet the demand expected in the next few years. The Committee agreed and "encouraged the Managing Director to start discussions with potential lenders on the terms and conditions under which the Fund could borrow funds to increase its resources, if and when the need arises" (see Appendix IV).

The second step was to develop a specific proposal for a borrowing plan that would be large enough to meet the expected demand but modest enough to secure the support of major creditors. After sounding out the main creditor country Executive Directors, de Larosière suggested to the Board that the Fund might need to borrow SDR 6–7 billion ($8–9 billion) a year for the next few years. The Board endorsed that level of borrowing in July 1980, and de Larosière went public with his proposal in the following months.[102]

Third, from whom could the Fund expect to borrow such large sums? The initial intention was to borrow as much as possible from industrial countries via the BIS and from major oil exporters and then, if necessary, to tap private capital markets for the rest. Borrowing in the open market would have been a radical departure for the Fund and was seen as much less desirable than staying within official

[102]See memorandum for files on a meeting of July 11, 1980, in IMF/CF (S 1720 "Use of Fund Resources—Policy, July 1980–November 1980"); and minutes of EBM/80/115 (July 30, 1980), p. 23. For an example of the Managing Director's public advocacy, see his 1980 Annual Meetings speeches, in IMF, *Summary Proceedings*, 1980, pp. 23 and 264.

circles, but it was also thought to be possibly necessary under the circumstances. Few industrial countries had strong enough external balances to be able to lend significant amounts to the Fund in the early 1980s, and the willingness of newly wealthy and still developing oil exporters to take up the slack was still largely untested. As long as the idea was floated as a backup plan and not as a concrete proposal, it received a lukewarm endorsement from most Executive Directors. In the event, even though the amounts raised from official lenders fell short of the expressed goal and the Board continued to discuss the idea on a conceptual level until 1983, no specific proposal for private sector borrowing was ever tabled.[103]

Those who were reluctant to endorse borrowing from the private sector raised several objections. First, it would be more expensive than borrowing from official creditors, because banks and other private creditors would require commitment fees and interest rate spreads as compensation. Second, reliance on private sector borrowing could subject the Fund's lending policies and practices to influence from commercial creditors. Third, the private market for SDR-denominated claims was extremely limited, and the Fund would have to devote considerable effort to the task of developing and sustaining a market for its liabilities. In contrast to the World Bank, for which market borrowing (in currencies) had been a permanent source of financing since 1947, the development of a permanent market for the Fund was seen as incompatible with its quota-based structure. Fourth, raising funds in capital markets would place the Fund in competition with the World Bank, which would further raise borrowing costs for both institutions. Fifth (and most important for the major creditors), the requirement for the Fund to obtain consensus support for quota increases was seen by many as an essential check on the expansion of Fund lending. Large-scale and sustained borrowing could lead to a weakening of that discipline and control. Although those concerns had to be weighed against the obvious advantages, the idea was quietly shelved once the most pressing shortage of resources had passed.[104]

Saudi Arabia

The key to success in this endeavor was Saudi Arabia. In 1980 and 1981, Saudi Arabia had an annual current account surplus of some $40 billion, by far the largest in the world. A loan to the Fund might provide a good investment outlet for part of those assets, and it would help compensate for the difficulty the Fund knew it would face in approaching its traditional industrial country creditors. De Larosière soon found an opportunity to initiate discussions, when he and Sheikh Abdul Aziz Al-Quraishi (governor of Saudi Arabia's central bank, the Saudi Ara-

[103]To some extent, talk of borrowing from private markets was a strategic move to secure favorable terms from official creditors. As de Larosière noted, in summing up the first Board discussion on this issue, "borrowing from governments . . . would not be justified if it were not on terms and conditions at least as favorable as could be obtained from the market." Minutes of EBM/80/114–115 (July 30, 1980). The quotation is from meeting 80/115, pp. 23–24.

[104]For the clearest expression of views by Executive Directors, see the minutes of EBM/81/119–120 (September 4, 1981). The final discussion of the subject in the 1980s was at EBM/83/59–60 (April 8, 1983).

bian Monetary Agency or SAMA) were both participating in an international conference in New Orleans, Louisiana, in June 1980. In private discussions, the governor responded favorably to the Managing Director's suggestion, but only if the loan could be structured so as to make it fit in with his country's budgeting and investing strategy. In particular, the Fund had always borrowed by establishing lines of credit on which it could draw when necessary. That enabled the Fund to pass the proceeds directly to a borrowing country and later to unwind the transaction in the same way, without incurring any exchange or interest risks. The lender, however, had no assurance at the outset on the amounts or timing of any drawdowns. For a multibillion-dollar loan, Saudi Arabia would want a more certain investment vehicle. This technical problem was eventually resolved when the Fund agreed to establish a new set of accounts, known as "borrowed resources suspense accounts," for the deposit of borrowed funds pending disbursal.[105]

A more substantive hurdle derived from Saudi Arabia's quota in the Fund. The country had joined the Fund in 1957 with an exceptionally small quota: $10 million, the seventh smallest of the 62 members at that time. That anomaly was marginally reduced in the next general review, and Saudi Arabia's rank rose to thirty-third in 1960. After the first oil shock in the early 1970s, that level became increasingly out of line and increasingly difficult to defend. The case for a sharply higher quota was enhanced starting in 1974, when Saudi Arabia began lending to the Fund for a variety of purposes. That year, the Saudi government lent the equivalent of SDR 1 billion ($1.2 billion) to the Fund as the lion's share of the financing for the first Oil Facility. The next year, they extended an additional SDR 1.25 billion ($1.5 billion) for the second Oil Facility and began a series of contributions that would make them the largest contributor to the facility's Subsidy Account. As noted above (p. 886), they were the largest single contributor to the SFF as well. In 1978, they volunteered to transfer their share of the distribution of profits from the Fund's sale of gold to the Trust Fund, to be used for the benefit of low-income countries. By then, the Saudi currency, the riyal, had become sufficiently strong to be used in Fund transactions and to be included in the 16-currency basket that constituted the SDR until 1981.

The Fund recognized these contributions in 1978 by agreeing to raise Saudi Arabia's quota to the 14th position in the Sixth General Review. Even before that increase took effect, Saudi Arabia was able to appoint an Executive Director to the Fund (rather than participating in the election of Executive Directors along with

[105]Assets in these accounts were invested in special depository accounts with the BIS and with the central banks of the G-5 countries (the countries whose currencies constituted the SDR), which were denominated in SDRs and which paid a market-based interest rate approximating the SDR rate. In contrast to other Fund accounts, the Fund, rather than the depositors, was responsible for maintaining the SDR value in the accounts (i.e., for managing the exchange risk). In the early 1980s, the accounts with central banks were used mainly for converting Saudi Arabian riyals into G-5 currencies; the BIS was the primary depository for investments. Subsequently, additional accounts were opened with other central banks. See the Fund's *Annual Reports* from 1981 onward. For the establishment of the policy, see Decision Nos. 6844- and 6845-(81/75), May 5, 1981; in *Annual Report 1981*, pp. 168–69.

most other member countries), as it had become one of the two largest creditors (see the discussion of the Executive Board in Chapter 20, pp. 1031–32). When the second oil shock hit shortly afterward, the new quota was already seriously out of line.

In the course of numerous meetings through the second half of 1980 and into 1981, the authorities insisted that their quota was still "extremely unsatisfactory" and should be raised to the average ratio of actual to calculated quotas for all members.[106] It was clear that a failure to meet this request, which was certainly reasonable on its merits, would threaten the loan negotiations and could thereby undercut the whole enlarged access policy. Saudi Arabia's bargaining position was extremely strong. Even so, a jump of that magnitude—to SDR 2.1 billion, from SDR 1.04 billion under the Seventh Review that was just about to take effect—would place their quota sixth in rank, below all of the G-5 countries but ahead of both Canada and Italy (then ranked sixth and seventh, respectively). Some of the major industrial countries reacted negatively to that prospect, and as a group they tried first to hold the increase below Italy's quota and then to fashion a compromise under which the quota would be raised to a level between Canada and Italy. De Larosière fought off that challenge at the last minute by appealing directly to the U.S. Secretary of the Treasury, Donald Regan.

At the beginning of February 1981, de Larosière met with the Saudi minister of finance, Sheikh Mohammed Abalkhail, in Davos, Switzerland. The quota increase was still uncertain, and a few technical details were still in negotiation, but the two men were able to agree in principle on the terms of a major loan to the Fund. On March 27, the Executive Board approved an ad hoc quota increase to SDR 2.1 billion, the full amount that had been requested. Six weeks later, at Fund headquarters on May 7, de Larosière and Al-Quraishi signed what may then have been the largest loan agreement in history. Saudi Arabia would lend the Fund a total of SDR 8 billion (about $9 billion) in two equal tranches (1981 and 1982), with six-year maturities. The loans would be denominated in SDRs, and the interest rate would be set at the SDR interest rate, with no spread or fees charged to the Fund. It was just over half of the total amount that de Larosière had set out to borrow, but it gave the Fund a strong base of financing on which it could safely launch the enlarged access policy.

Other Oil-Exporting Countries

To begin to raise the rest of the targeted SDR 6–7 billion a year, de Larosière turned his attention to other major oil exporters. Following some initial staff contacts, he decided to make a direct appeal to a few Middle Eastern countries with substantial external surpluses. That appeal would be more difficult than in the case of Saudi Arabia, for three reasons. First, Saudi Arabia was unique in the region in wanting to play a leadership role in international economic policy and in its willingness and ability to reach out to industrial countries. An appeal to other Middle Eastern

[106]Letter of December 1, 1980, from Abalkhail to de Larosière; in IMF/CF (E/313 "Executive Directors' Election—19th Regular, 1982").

countries would have to be made on purely financial grounds. Second, because Saudi Arabia was in the midst of a major internal development effort, the authorities were actively seeking good outlets for short- to medium-term liquid investments. Other countries in the region were typically seeking equity and other long-term investments. Lending to the Fund thus would be less attractive to those countries. Third, and ultimately decisively, countries throughout the Middle East were frustrated with the Fund and the World Bank for their failure to get approval for the Palestine Liberation Organization (PLO) to be an official observer at the Annual Meetings of the Board of Governors (see the discussion of the Board of Governors in Chapter 20, pp. 1021–27). Saudi Arabia, as both the largest financial supporter of the PLO and the largest creditor of the Fund, could afford to compartmentalize its support for the two organizations. For others, the two issues were inseparable.

The effort to obtain loans from other surplus countries went forward despite these obstacles and culminated in a personal visit by de Larosière to Kuwait (where he met with the Emir, Sheikh Jaber Al-Hamad Al-Sabah) and Abu Dhabi (where he met with the president of the United Arab Emirates, Sheikh Zaid bin Sultan Al-Nehayan).[107] Although both governments expressed sympathy in principle to the Managing Director's initiative, they responded that they could not lend to the Fund at that time because of the ongoing controversy over the status of the PLO at the Annual Meetings.[108] That impasse persisted throughout the period of heavy borrowing by the Fund and posed an insuperable barrier to what otherwise might have been a significant source of temporary funding.[109]

Industrial Countries

Next on the list were the industrial countries. Although direct lending by governments was precluded in most cases by a combination of economic difficulties resulting from the second oil shock and a growing political reluctance to invest in international assistance, most officials recognized the importance of supporting the Fund's enlarged access policy. Lending by central banks could provide an alternative channel, especially if coordinated and filtered through the BIS. De Larosière again took charge of the negotiations, traveling to Basel in November 1980 to raise the issue with the central bank governors attending the monthly BIS meeting. He got a sympathetic hearing there, and the staff set out to negotiate a specific borrowing arrangement.

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[107]Officials in Iraq declined a visit on the grounds that responsibility for assistance to developing countries lay with industrial countries and that the Fund already had sufficient resources. A planned stop in Qatar was canceled because the principal authorities were away from the country. Later appeals to several other oil exporters with external surpluses were also unsuccessful.

[108]See materials in "Mission to Middle East—De Larosière and Staff," IMF/CF (S 813); and report by the Managing Director at EBM/80/128 (September 3, 1980).

[109]Although Saudi officials were no less displeased at the handling of the PLO affair, they did not allow it to deflect the negotiations on their loan, for the reasons discussed above. Kapur, Lewis, and Webb (1997), p. 980, describe the effect of the affair on the World Bank's borrowing from Middle Eastern countries but incorrectly attribute the prolonged negotiation of the Saudi loan to the Fund to that problem.

Two technical issues dominated those discussions. First, the Fund wanted to borrow in SDRs, while the BIS preferred to lend in individual currencies. That gap was bridged by an agreement that the loan would be denominated in SDRs, with the U.S. dollar as the normal vehicle currency. The BIS could avoid exchange risk by matching its liabilities to the currency composition of its corresponding claims. Second, the Fund was seeking to borrow for several years, while the BIS normally restricted its lending to short periods. That gap was bridged by an agreement that each drawdown would carry a six-month maturity, but the Fund would have the option to roll over the credit up to a maximum period of 2½ years and to delay the initial drawdown by up to two years. The terms of that agreement—for a loan expected to total SDR 550 million ($650 million)—were approved in May 1981, just a few days after the signing of the loan from Saudi Arabia.[110]

Although the BIS loan was not large, it unlocked the door to parallel agreements with individual industrial country central banks, with the notable absence of the United States. Some countries preferred to lend indirectly to the Fund through the BIS; others preferred to lend directly but were willing to do so on the same terms as the multilateral loan. By August, a series of deals involving 18 industrial countries was completed and signed, for a total amount of just over SDR 1.3 billion ($1.5 billion). All of the G-10 countries except the United States participated in a package deal either through or in parallel with the BIS, along with Austria, Denmark, Norway, Spain, and Switzerland. Four other countries—Australia, Finland, Ireland, and South Africa—entered into similar agreements (see Table 17.5).

In just over a year, the Fund had obtained SDR 9.3 billion (nearly $11 billion) in loan commitments and was well on its way toward covering the expected demand for Fund credits at least into 1983. Before de Larosière could embark on the next round of negotiations, to cover Fund lending in later years, the Board turned its attention to the adoption of a ceiling on overall borrowing. That issue had been raised by Saudi Arabian officials in the course of negotiations on their loan to the Fund, and the Managing Director had promised Al-Quraishi to "assure creditors that the Fund's borrowings will be prudently managed" by setting "a limit on the Fund's total indebtedness expressed as a ratio of its total quotas."[111]

Initial discussions revealed a split in views among major creditor countries on the wisdom of imposing a ceiling on borrowings. While some (notably Japan and Germany) shared the Saudi concerns, others (notably the United Kingdom,

[110]Only the initial drawdown could be rolled over for the full 30 months. Subsequent drawdowns were limited to the same ending date as for the first. All loans had to be repaid by that date, which could be no later than January 31, 1985. The Executive Board approved the agreement in principle on May 13, 1981, and the final text (with the amount augmented to SDR 600 million) was approved on June 1. On August 3, the BIS agreement was augmented again, to SDR 675 million, to incorporate a commitment from the Bank of Spain. Pertaining to "Borrowing by the Fund from the Bank for International Settlements (BIS) and from Central Banks and from Monetary Authorities," see "Additional Information," SM/81/109, Sup. 2 (June 2, 1981) and "Additional Information," Sup. 3 (July 30, 1981), and minutes of EBM/81/81 (May 13, 1981) and EBM/81/83 (June 1, 1981).

[111]"Borrowing Agreement with Saudi Arabian Monetary Agency (SAMA)," EBS/81/95 (April 21, 1981), Annex C.

Table 17.5. Borrowing from Industrial Countries to Finance Enlarged Access
(Millions of SDRs)

Creditor	Effective Date	Amount
I. 1981–84		
BIS group		1,175
BIS	June 1981[a]	675
National Bank of Belgium	June 1981	50
Swiss National Bank	June 1981	150
Bank of England	July 1981	150
Government of Japan	July 1981	150
Other		130
Bank of Finland	July 1981	30
Reserve Bank of Australia	July 1981	50
Central Bank of Ireland	August 1981	20
Reserve Bank of South Africa	August 1981	30
Total		1,305
II. 1984–86		
BIS	April 1984	2,505
Government of Japan	April 1984	375
National Bank of Belgium	June 1984	120
Total		3,000
III. 1987–90		
Japan	December 1986	3,000

[a]Initially, SDR 600 million; augmented to SDR 675 million in August.

France, and the Netherlands) had reservations. A low ceiling might unnecessarily limit the Fund's flexibility, while a high one would have little meaning and might even encourage the Fund to undertake excessive borrowing. For several months, the staff argued for a ceiling that was much higher than any expected level of borrowing, while Nimatallah, the Saudi Director, insisted on an effective limit. Finally, in January 1982, the Executive Board adopted formal guidelines that were close to those requested by Saudi Arabia.[112] The new rules (see Appendix IV) imposed a ceiling on outstanding indebtedness plus unused lines of credit[113] of 60 percent of total Fund quotas.[114] This ceiling was well in excess of

[112]Decision No. 7040-(82/7), adopted January 13, 1982; in Appendix IV to this chapter. Bruno de Maulde (France) dissented from the decision on the grounds that it could lead to excessive borrowing; minutes of EBM/82/4 (January 11, 1982), pp. 12–13.

[113]Since, at that time, the GAB could be used only for lines to GAB participants and a member's credit line could not be used to support financing for that member, the guidelines recognized that not all GAB credit lines could be activated at the same time. For 1982–83, only 50 percent of GAB credit lines (or the amount outstanding, if higher) counted toward the ceiling. After the GAB was modified in 1983 to permit support for credits to nonparticipants (as discussed below), the portion was raised to two-thirds.

[114] As John Anson (United Kingdom) observed during the debates, the decision to use total Fund quotas as the denominator had the illogical effect of raising the absolute borrowing limit after the Eighth Quota Review took effect and reduced the need for further borrowing. Minutes of EBM/81/119 (September 4, 1981), p. 10.

the actual level (22 percent at the end of FY 1981) but not much above the levels then being discussed (which ranged up to 49 percent).[115] The rules provided further that if borrowings (as defined) exceeded 50 percent of total quotas, the Board would review the status of unused credit lines with an eye toward maintaining a prudent balance. With occasional modification, these guidelines remained in place until 1991, but they had no discernible effect on actual borrowing. When the Fund's potential indebtedness peaked in 1984, the applicable ratio was still below 40 percent.

When the borrowing agreements with industrial countries were nearing expiration in 1984, the Fund negotiated a replacement package extending through 1986 for a much larger amount (SDR 3 billion, compared with the original 1.3 billion). Also in 1984, Saudi Arabia responded to that package by agreeing to a "third tranche" on its loan, for an additional SDR 3 billion. And in December 1986, Japan agreed to lend SDR 3 billion to the Fund, with a five-year maturity. (See Table 17.5, above.) Overall, during these five years of extensive and heavy demands on its resources, the Fund obtained short- to medium-term commitments from 19 countries that made a total of some SDR 14 billion (15½ percent of total Fund quotas) available to finance enlarged access.[116] Although rather less than the Managing Director's ambitious target, this borrowing sufficed to enable the Fund to meet the demand for enlarged-access credits throughout the 1980s.

General Arrangements to Borrow

The GAB was a valuable resource to the Fund, but more as a safety valve than as a direct source of money. The Fund drew on these lines of credit on nine occasions from 1964 through 1978, but not again for the next 20 years (Figure 17.4).[117]

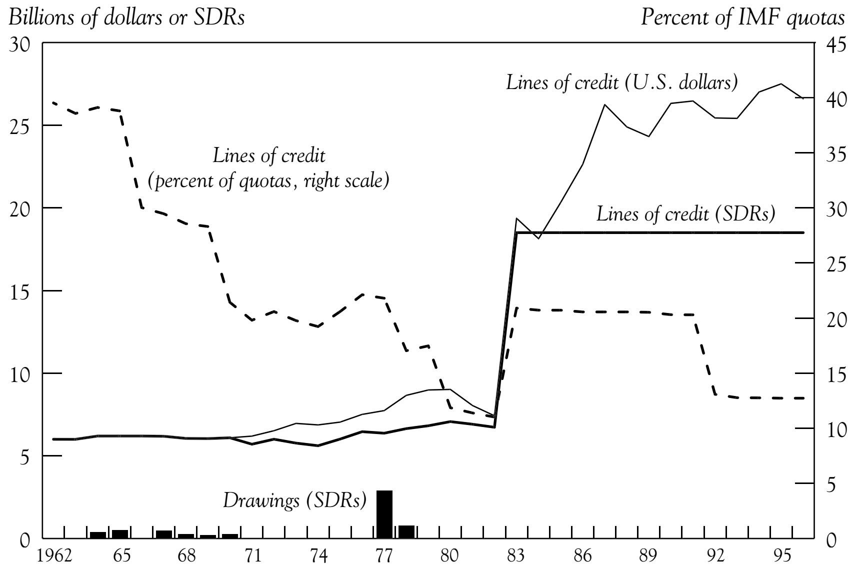
The GAB originated as one of several expedients in the 1960s (including the 1961 Basel Agreement, the establishment of the London Gold Pool, and the creation of swap lines between major central banks) to supplement and protect gold and dollars as official international reserves (see Ainley, 1984, pp. 2–4). It provided a conditional line of credit to the Fund for a renewable period of five years. Throughout the 1960s and 1970s, its provisions were routinely renewed without

[115]The quoted percentages are from "Guidelines on Borrowing by the Fund," EBS/81/174 (August 19, 1981), Table 3, p. 19 (as corrected on September 9).

[116]This amount is the sum of the SDR 11 billion in medium-term commitments from Saudi Arabia and the maximum amount (SDR 3 billion) available at any one time from the various shorter-term agreements with industrial countries. During the period of peak usage in the mid-1980s, the equivalent amount in dollars was only slightly larger than the amount in SDRs.

[117]The history of the GAB is covered in Horsefield (1969), Vol. 1, pp. 510–15 and 567–70, and Vol. 2, pp. 373–77; de Vries (1976), Vol. 1, pp. 370–76; de Vries (1985), pp. 587–92; and Ainley (1984). The GAB was next activated in July 1998 to finance the augmentation of an EFF arrangement with the Russian Federation.

Figure 17.4. General Arrangements to Borrow, 1962–96
(Includes associated agreements)



major modification, and the available amount of money gradually declined in relation to quotas and world trade.[118]

Complacency vanished quickly after the debt crisis of 1982 hit while negotiations to increase Fund quotas were at a standstill. At the Interim Committee meeting in Toronto that September, U.S. Treasury Secretary Regan called for creation of "an additional new permanent borrowing arrangement that would be available for use by the Fund only under extraordinary circumstances."[119] Although this general U.S. proposal envisaged creation of a new arrangement, the seed germinated over the next two months into a plan to enlarge the GAB.

Enlarging the GAB was not the obvious choice under the circumstances, because of limitations on its activation. As noted above, the Fund could call on GAB credit lines only to finance a credit arrangement for a GAB participant (i.e., a G-10 country) and even then only if the arrangement was expected to alleviate a problem that threatened the stability of the international monetary system.[120] If

[118]The only changes in size or composition before 1983 were the addition of an associated agreement with Switzerland in 1964 and an increase in the credit line from Japan in 1976. Those additions augmented the resources of the GAB by about 19 percent (from $6.3 billion to $7.5 billion, as of 1976).

[119]Minutes of ICMS/Meeting 19, September 4, 1982), p. 15. Regan announced the proposal publicly a few days later in his Annual Meetings speech, in slightly altered language; IMF, *Summary Proceedings*, 1982, p. 51.

[120]For the text of the GAB agreement that was in effect from 1978 through 1982, see de Vries (1985), Vol. 3, pp. 527–33.

creation of a whole new agreement was to be avoided, new flexibility would have to be introduced.

Despite the ambiguities, a broad agreement on the expansion developed quite quickly. The G-10 Deputies, chaired by Lamberto Dini (Italy), met at the Fund office in Paris on November 29, 1982, for a preliminary exchange of views on Regan's proposal. By then, discussions among ministers had already ruled out trying to create a new mechanism. Extension of additional lines of credit to the Fund would have to be made, if at all, through the GAB or possibly the SFF. Oddly, although the proposal was a U.S. initiative and its passage was designed in part to help the U.S. government further its objectives in stabilizing the economies of several countries in Latin America, the U.S. delegates at the November meeting insisted that the expansion be adopted only as part of a package.[121] The complete deal should include a cutback in enlarged access, a tightening of CFF conditionality, and an increase in effective remuneration rates for Fund creditors. Those issues, however, were set aside for the moment, and in a series of meetings through mid-January, the Deputies agreed to expand the GAB almost exactly as proposed by the United States.[122]

The G-10 agreement would expand the GAB in three directions: it would greatly increase its size, from less than SDR 7 billion to 17 billion ($17.8 billion), make it available to support Fund credits to nonparticipants, and open the door for other countries to make associated credit arrangements.[123]

Just how big the GAB should be was debated for several weeks. Most of the G-10 preferred to aim for SDR 20 billion, but the United States fought to keep it closer to 15 billion. The final compromise emerged over lunch at a meeting of G-10 ministers in Paris in mid-January.[124] An equally delicate issue that could have derailed the whole effort concerned how to apportion commitments among the G-10. The existing distribution dated essentially from 1962 and no longer reflected the relative importance of the G-10 countries. Fortunately, a ready meas-

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[121]IMF/CF (S 371 "Group of Ten Meetings and Studies, 1981–1982"); cable from the U.S. Deputies (December 3, 1982).

[122]The United States eventually obtained substantial victories on all counts. A cutback in enlarged access was agreed upon toward the end of 1983, after substantial debate (see above, p. 881). CFF access and conditionality were tightened around the same time (see Chapter 15), and an increase in remuneration rates was approved in January 1984 (see below, p. 904). The U.S. delegation at the Deputies' meetings was headed by Beryl W. Sprinkel, the Under Secretary of the Treasury for Monetary Affairs, and Henry C. Wallich, Member of the Board of Governors of the Federal Reserve System.

[123]The amendment also introduced three technical changes. First, the denomination of borrowings was changed from individual currencies to SDRs. Second, the interest rate, which had been based on the Fund's rate of charge, was set equal to the SDR rate. Third, the rules were tightened on funds borrowed to finance reserve tranche drawings, since countries were no longer required to repay those drawings. Previously, the Fund's borrowings had carried a five-year maturity. Now, if the purchaser was "included in an operational budget" (i.e., if the Executive Board determined the country's currency to be "sufficiently strong" pursuant to Article V), the Fund had to make repayment equal to the net amount of the purchaser's currency sold in the preceding quarter.

[124]Notes by de Larosière on the January 18 meeting; in IMF/RD Managing Director G-10 Folder (Accession 87/27, Box 19, Section 536).

Table 17.6. Expansion of the GAB, 1983
(In millions)

	Previous Commitment			New Commitment			
Participant	Local currency	SDR equivalent	Share (In percent)	SDRs	Dollar equivalent	Share (In percent)	Percentage Increase
United States	2,000.0	1,910	30	4,250.0	4,450	25	222
Germany (Deutsche Bundesbank)	4,000.0	1,496	23	2,380.0	2,492	14	159
United Kingdom	357.1	517	8	1,700.0	1,780	10	329
France	2,715.4	340	5	1,700.0	1,780	10	500
Italy	343,750.0	216	3	1,105.0	1,157	7	511
Japan	340,000.0	1,367	21	2,125.0	2,225	13	155
Canada	216.2	168	3	892.5	934	5	533
Netherlands	724.0	242	4	850.0	890	5	351
Belgium	7,500.0	140	2	595.0	623	4	425
Sweden (Sveriges Riksbank)	517.3	64	1	382.5	400	2	594
Switzerland (Swiss National Bank)				1,020.0	1,068	6	
Total		6,460	100	17,000.0	17,799	100	263
Associated Agreements:							
Switzerland (Swiss National Bank)	865.0	394					
Saudi Arabia				1,500.0	1,570		
Total including associated agreements		6,854	18,500.0	19,369.0			

Note: Equivalent values are computed at average exchange rates for 1983.

ure was available, since the shares in the ongoing quota review were viewed as reasonable and were accepted by all participants. The effect, after some smoothing and other adjustments, was to even out the distribution somewhat, as the shares of the three largest creditors all declined (Table 17.6).

On the second issue, the G-10 agreed to drop the requirement that the GAB only be activated to support a drawing by a participant but to retain the requirement that it be used only to cope with a systemic problem and to add a requirement that activation for nonparticipants be restricted to upper-tranche (i.e., high-conditionality) arrangements. From the Fund's vantage, the restriction to systemic problems posed a political problem because it implied that the arrangements could benefit large countries more than small ones. To mitigate the force of this limitation, the agreement was written to permit the Managing Director to initiate a call on the GAB if the Fund's resources were inadequate to deal with "balance of payments problems of *members* of a character or *aggregate* size that could threaten the stability of the international monetary system" (emphasis added). This wording acknowledged that problems affecting several smaller countries could trigger an activation of the borrowing arrangements.

The third issue—allowance for associated agreements—was intended primarily to enable the Fund to negotiate a parallel arrangement with Saudi Arabia. The G-10 Deputies agreed in December 1982 to invite Saudi Arabia to participate in

some fashion in the GAB, and the chairman of the G-10 Ministers, Jacques Delors (France), met with senior officials in Riyadh later that month. De Larosière and Geoffrey Howe (who had just been elected chairman of the Interim Committee) then flew to Riyadh in early January for more specific discussions on the matter.[125] Finally, the top Saudi officials—Abalkhail and Al-Quraishi—met with Dini in London at the end of January and then with de Larosière in Washington in early February to complete the deal.[126]

Although the Saudis were responsive from the beginning, negotiations were delicate. Some of the G-10 countries were reluctant to expand their club, and full participation in the GAB also would have created political problems for Saudi Arabia. To support the Fund's lending to developing countries was one thing; to become part of the industrial country establishment was quite another. Moreover, Saudi Arabia's leadership role in the Middle East might require it to opt out if the GAB should ever be activated to support Fund lending to countries with which it or its neighbors had serious conflicts or differences (such as Israel or South Africa). For both the Fund and the G-10, however, a special opt-out clause would have raised questions of equal treatment.

Two possible solutions to this dilemma were considered. First, the discussions during January were predicated on the assumption that the Saudi authorities would accept a parallel status that would require it to be bound by group decisions but would give it voting rights on GAB decisions.[127] Saudi Arabia would not become a member of the group, and the precise nature of its role would remain secret. When that overture was rejected, the G-10 Deputies agreed to consider a much looser relationship. The accepted solution was to negotiate a separate but associated agreement under which some symmetry with the GAB could be retained. Saudi Arabia would have the right to accept or reject any call for activation of the arrangement, independently from the GAB.[128] Saudi officials would not vote or participate in G-10 meetings, but the G-10 would establish regular communication channels for consultations, and the Chairman of the Deputies would debrief senior Saudi officials after each meeting.

A related amendment to the GAB enabled Switzerland to become a full participant. The Swiss National Bank had had an associated creditor agreement since

[125]Minutes of EBM/83/10 (January 12, 1983), pp. 3–4.

[126]Reports on the meeting with Dini in London and other G-10 meetings in this period may be found in the Research Department of the Bank of Italy (file H.1.3, "Gruppo dei Dieci, Riunioni"). See in particular Dini's letter of January 28, 1983, to Jacques Delors (Chairman of the G-10); and his February 10 report to G-10 ministers and governors. On Howe's role, see Howe (1994), pp. 270–71.

[127]See January 25, 1983, telex from de Larosière to Abalkhail; in IMF/CF (S 1773 "General Arrangements to Borrow, Participation of Saudi Arabia").

[128]Paragraph 23 of the amended GAB agreement provides either for a closely associated agreement under which calls "shall be treated as if they were calls . . . in respect of a participant" (which would preclude opting out) or for separate agreements "involving an association with participants" without such a provision. The agreement with Saudi Arabia fell in the latter category.

1964, and it now signaled its desire to become a full participant.[129] Since Switzerland was still not a member of the IMF, the GAB could not be used to support lending to it, but Switzerland's financial position was strong enough that this detail had no foreseeable practical consequence. The proposed amendment to the arrangements was hastily revised in February 1983 to incorporate this upgrading of the relationship.

As soon as the Deputies reached agreement on their strategy in December, the Fund got involved both in negotiating the contentious issues just discussed and in drafting the revised agreement. Drafting also proceeded quickly, driven by the early date of the spring 1983 meeting of the Interim Committee. The amended GAB was approved by the G-10 Deputies and then by their Ministers at meetings in Paris on January 17–18, 1983, by the Interim Committee on February 11, and by the Executive Board later that month.[130] The Swiss National Bank became a full participant in April, and an associated arrangement with Saudi Arabia for a credit line of SDR 1.5 billion ($1.6 billion) was finalized in May.

Although the expanded GAB was not activated in the years that followed, it was periodically renewed without substantive change for subsequent five-year terms, beginning in November 1987.

Sharing the Burden: Who Pays for the Fund?

As a cooperative public institution, the IMF has generally sought to manage its finances so as to maintain an adequate reserve to back up its operations and to apportion costs fairly and equitably among its member countries. During the 1980s, the Fund's efforts to achieve these financial goals raised contentious political issues.

Through 1977, the Fund frequently incurred net losses in its operations, including two long streaks of continuous deficits (fiscal years 1949–56 and 1972–77). The early losses, which resulted from a combination of low demand for Fund credits and a low interest rate charged on outstanding balances, were reversed largely because of an investment program carried out from 1957–72 that funded a substantial reserve balance.[131] When increased lending at low interest rates in the

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[129]IMF/CF (S 1771 "Inclusion of Switzerland in Borrowing Arrangements, 1980–1983"); cable to the Fund from Pierre Languetin, President of the Swiss National Bank (January 28, 1983).

[130]For the original and revised GAB agreements, the associated borrowing agreement with Saudi Arabia, and related documents, see the appendices in Ainley (1984).

[131]In the early years of Fund operations, income from charges on outstanding credits was insufficient to cover administrative expenses. In 1956–60, the Fund sold $800 million worth of gold to the United States, invested the proceeds, and used much of the interest income to establish a Special Reserve account. By 1972, the balance in the account exceeded $400 million, and the Fund had unwound the investment program by repurchasing the gold. Total reserves (the sum of the General Reserve and Special Reserve accounts) peaked in 1971, at SDR 784 million ($784 million), and fell to SDR 687 million in 1977 as a result of the Fund's operating losses in those years (although it rose in U.S. dollar terms, to about $825 million). For an overview, see "Factors Relating to Burden Sharing in the Fund," EBS/85/126 (May 14, 1985), pp. 8–9.

1970s led to renewed problems, the main lever available for stanching the losses was the interest rate (the "rate of charge"), which contained a substantial element of concessionality. The Fund moved cautiously, however, as it was reluctant to force its borrowers to pay higher costs without passing on part of the burden to creditors.[132] Charges had to be not only reasonable and fair, but also low enough to encourage countries to seek early assistance from the Fund when problems arose. Although procedures were put in place to review the rate of charge when necessary, the staff remained uneasy about the prospects for the Fund's financial strength in the 1980s.

Concerns about maintaining an operating surplus came to a head in 1980. After just two years of comfortable surpluses, the Fund barely covered its expenses in FY 1980 (Table 17.7), and the staff projected a deficit for the coming year. Part of the problem was that the Fund was a victim of its own success: because its margin of interest was too low to cover other expenses, the more lending it did, the more it strained its net income. When market interest rates rose sharply, as they did in 1980, income was squeezed further. The problem was compounded even more when the Fund's lending was accelerating, as it did at that time, because the rate of charge rose only gradually with the length of time that credits were outstanding, and the schedule of charges was adjusted infrequently. What was needed, in the absence of some means of subsidizing the gap, was either a reversal of the trend toward paying a high rate of remuneration to creditors or an agreement to set the rate of charge more flexibly so as to cover costs. Neither option, however, was very attractive. Lower remuneration carried the risk that creditors would become less willing to finance the Fund and to hold reserve tranche balances, while higher charges would impose additional costs on borrowers and might decrease the willingness of some countries to seek help from the Fund.

Remuneration to Creditors

The main source of net income to the Fund is the difference between market interest rates and the effective rate of remuneration on member countries' reserve tranche positions. Historically, that difference arose from two sources. First, until 1987 the rate of remuneration was below the market rate on SDR-denominated assets (Figure 17.5). Second, remuneration was paid on only a portion of a country's credit balance in the Fund.

Until 1968, the Fund did not compensate countries for creditor positions, which were considered as being made available by countries in strong balance of payments positions for the benefit of those in need of temporary assistance. In the late 1960s, when the Fund's income and reserve positions were becoming stronger, creditors seized the occasion of the discussion of the First Amendment to the Ar-

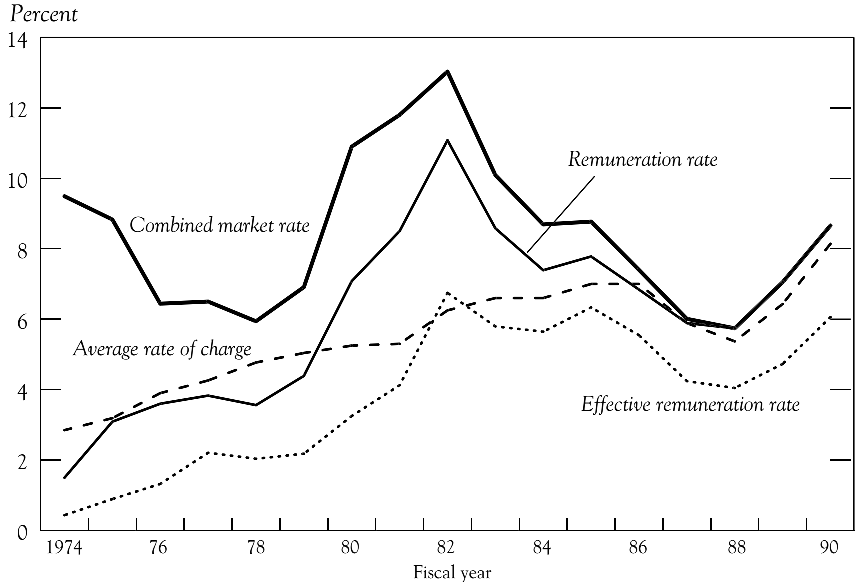
[132]On the history of the Fund's net income and related policies through 1978, see Horsefield (1969), Vol. 2, pp. 363–73; de Vries (1976), Vol. 1, pp. 383–97; and de Vries (1985), pp. 599–603.

Table 17.7. Income, Expenses, and Reserves: General Resources Account, FY 1979–90
(Millions of SDRs)

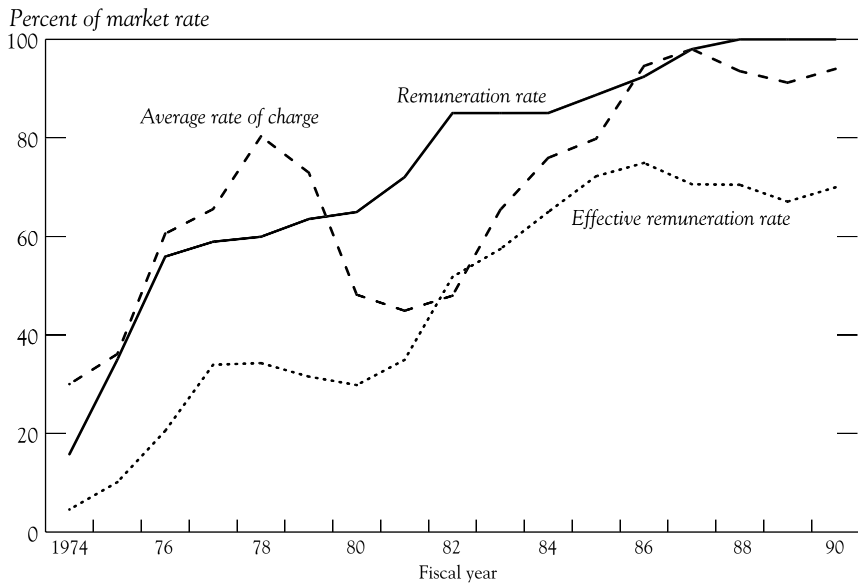
	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990
Income												
Periodic (interest) charges	678.1	519.4	592.7	1,092.1	1,545.4	2,363.8	2,969.1	2,739.6	2,088.9	1,865.0	1,719.4	1,825.1
Service charges	6.2	11.1	21.9	34.8	51.3	50.8	30.3	19.7	15.8	20.6	10.6	22.2
Interest on SDRs	57.1	81.8	265.8	657.2	444.3	371.6	478.3	263.2	143.9	66.0	61.3	88.2
Misc. income, net	8.0	1.9	1.8	4.8	4.3	5.7	4.3	6.9	2.1	2.8	2.0	4.8
Total gross income	749.4	614.2	882.2	1,788.9	2,045.3	2,791.9	3,482.0	3,029.4	2,250.7	1,954.4	1,793.3	1,940.3
Expenses												
Remuneration	171.7	241.0	372.8	908.6	981.1	1,286.3	1,721.2	1,452.1	1,020.0	895.2	988.6	1,256.2
Administrative expenses	73.4	86.1	99.9	153.3	191.4	192.8	224.2	223.4	190.9	175.1	172.7	188.6
Interest on borrowing, net	458.1	284.0	329.5	634.9	807.4	1,239.8	1,566.5	1,275.8	927.2	774.6	515.0	345.0
Allocation to SCA									26.5	60.4	62.9	65.0
Total expenses	703.2	611.1	802.2	1,696.8	1,979.9	2,718.9	3,511.9	2,951.3	2,164.6	1,905.3	1,739.2	1,854.8
Net Income	46.1	3.1	80.1	92.0	65.4	73.1	–29.9	78.1	86.1	49.1	54.2	85.5
Reserves, end of period	760.1	763.2	843.3	935.4	1,000.7	1,073.8	1,044.0	1,122.1	1,208.2	1,257.3	1,311.5	1,397.0
Memorandum items:												
Net income as percent of initial reserves												
Target				0.0	3.0	3.0	3.0	5.0	7.5	7.5	5.0	5.7
Outturn	6.5	0.4	10.5	10.9	7.0	7.3	–2.8	7.5	7.7	4.1	4.3	6.5
Reserves as percent of credit outstanding	8.6	9.5	8.8	6.3	4.2	3.4	3.0	3.2	3.8	4.5	5.5	6.3

Source: IMF *Annual Reports*; and IFS.

Figure 17.5. Selected IMF Interest Rates, 1974–90



Charges and Remuneration (In percent of market interest rate)



ticles to call for a system of compensation. A discretionary distribution of net income was made in 1968 and 1969, and the First Amendment then provided for regular remuneration of creditor positions and established an initial fixed rate of 1½ percent a year. However, no return was paid on the gold tranche (later called the reserve tranche); the base for remuneration was the amount by which the

Fund's holdings of the country's currency were below 75 percent (rather than 100 percent) of quota. The remuneration rate was raised in 1974 to 2½ percent, was set at 3½ to 3¾ percent in 1975–76, and from mid-1975 through 1978 was set equal to the official SDR interest rate (which varied between 3½ and 4½ percent).[133] The 1974 increase thus marked the beginning of remuneration to creditors as a major expense for the Fund.

The Second Amendment to the Articles brought a further major increase, through two changes in the system of remuneration. First, remuneration was to be paid on a portion of the reserve tranche position and not just on creditor positions below 75 percent of quota. The remunerable portion would be determined by reference to a "norm" for each country, as explained below. Second, the rate of remuneration was to be set between 80 and 100 percent of the official SDR rate. Both of these changes were necessary for consistency with other elements in the amendments. Unless the reserve tranche was made into a financially attractive asset to hold, countries with credit positions could be expected to draw on their reserve tranche balance and to hold SDRs or foreign exchange instead, with even more serious adverse effects on the Fund's income and liquidity.

By introducing a norm for determining the base on which remuneration was to be paid, the amendment to Article V fixed the absolute amount of the unremunerated creditor position at the size of a country's reserve tranche in 1978. (For countries joining after the amendment took effect, this amount was to be determined by reference to the average norm for all existing members.) Any subsequent increase in the reserve tranche through enlargement of quotas would be fully remunerated as long as it was retained in the Fund. As a result of this policy shift, the point at which remuneration started rose from 75 percent of quota in 1978 to an average level of nearly 92 percent after the Eighth Quota Review took effect at the end of 1983.[134] Moreover, the amendment also permitted the Executive Board to set the norm at a higher level (as high as 100 percent of quota), in which case it could not be lowered subsequently. The intention was that eventually all or nearly all creditor positions would be fully remunerated, but a possibly lengthy transition period would allow the Fund to absorb the cost increase gradually.[135]

Although the effect of this amendment would be to raise the Fund's remuneation costs over time, it had no immediate effect and therefore raised no

[133]In 1974–75, remuneration was paid at 5 percent on any positions below 50 percent of quota. The Second Amendment to the Articles eliminated that possibility by requiring that a single rate be paid on all balances on which remuneration was paid. The official SDR interest rate was set below the market interest rate until May 1981 (see Chapter 18). In 1976–78, the market rate ranged from 5.7 to 6.9 percent, and the official rate was set periodically at 60 percent of the average market rate.

[134]See "'Norm' for Remuneration," EBD/84/51 (February 17, 1984).

[135]For the official commentary on the amendment to Article V, Section 9, on remuneration, see de Vries (1985), Vol. 3, pp. 341–43.

great objections from the developing countries that would eventually be hurt by it.[136] When the debates on the amendment took place, in 1975 and 1976, no one could foretell which countries would be creditors and which ones debtors two or three decades later. Not until the 1980s would the membership become more clearly aligned on that axis.

Tying the remuneration rate to market interest rates had an even greater quantitative effect on remuneration costs. Initially (effective at the beginning of 1979), the Executive Board set the rate at 90 percent of the official SDR rate, which in turn was set equal to 80 percent of the market rate. That raised the remuneration rate to 72 percent of the market rate, from 60 percent previously. Then, throughout the 1980s, the ratio to market rates was steadily raised under pressure from the major creditor countries: to 85 percent in 1981, to 97.5 percent in gradual steps from 1984 to 1986, and to 100 percent in 1987 (Figure 17.5).[137] By the end of the decade, about one-half of the Fund's remuneration costs and one-third of its total expenses were due to the policy changes introduced through the 1978 amendments to Article V. As a result, the Fund had to take measures to generate an equivalent amount of additional income.

Charges to Borrowers

Until 1974, the Fund was able to keep its interest charges quite low and stable. At the beginning of that year, interest on outstanding credits was charged at rates starting at 2 percent a year and rising to 5 percent, depending on the size and duration of the balance.[138] U.S. treasury bills, in contrast, were paying nearly 8 percent. That generous policy was made possible by the Fund's large stock of interest-free resources in the form of unremunerated reserve positions. Later, as remuneration costs rose, so did the rate of charge.

The Fund's initial response to rising costs, in the 1970s, was to try to maintain stability by raising charges selectively and avoiding a direct linkage to changes in market interest rates. By the end of the decade, a complicated and still-rigid system of charges was in place (Table 17.8). As market interest rates rose sharply in 1979–80, the Fund's net income deteriorated, and the Executive Board decided to consider making the system both simpler and more flexible.[139]

The first major step in that direction was to replace the whole sliding scale of charges on credit-tranche drawings with a single unified rate of charge. Al-

[136]For a later lament, see Patel (1992), pp. 10–11. Another ameliorating consideration in the late 1970s was the expectation that continuing gold sales by the Fund would generate additional income to help cover the rising cost of remuneration.

[137]For details on the progression during 1984–86, see *Annual Report 1986*, p. 70.

[138]For an overview of the evolution of policies on the rate of charge through 1978, see de Vries (1985), pp. 559–66.

[139]In addition to the interest rates discussed here, the Fund imposes one-time service charges on drawings (other than reserve-tranche drawings) and periodic commitment fees on undrawn balances under stand-by and extended arrangements. See IMF Treasurer's Department (1998), p. 36.

Table 17.8. Rates of Charge on the Use of Fund Resources, 1977–90
(In percent a year; fiscal years)

I. In effect 1977–81: rates vary with the length of time drawings are outstanding[a]		
Basic rates	4⅜ to 6⅜	
Rates on EFF drawings	4⅜ to 6⅞	
Rates on drawings under 1974 Oil Facility	6⅞ to 7⅛	
Rates on drawings under 1975 Oil Facility	7⅝ to 7⅞	
Rates on drawings financed by SFF borrowings	Rate paid by Fund plus margin of 0.2 to 0.325	
Rates on exceptional use of resources	Yield on U.S. treasury securities with five-year maturity, plus margin of 0.25	
II. 1981–89: single basic rate		
Basic rate, including EFF and other facilities	Set annually in accordance with income target, subject to periodic revision	
Rates on drawings under EAR	Rate paid by Fund plus margin of 0.2	
Rates on Oil Facility drawings and on drawings financed by SFF borrowings	As above; all Oil Facility drawings were repaid by 1983	
Basic rate (before burden-sharing adjustments):	Initial	Final
1982	6.25	
1983–84	6.60	
1985	7.00	
1986	7.00	
second half	7.87	7.00
1987	6.00	5.82
1988	5.80	5.38
1989	5.50	
second half	7.38	
III. 1990		
Basic rate (before burden-sharing adjustments)	96.3 percent of the SDR interest rate	
Other rates	As above	

[a]The Second Amendment to the Articles changed the amount on which charges were levied. Prior to the amendment, the base was the amount by which the Fund's holdings of a country's currency exceeded its quota. After April 1978, the base was the amount of holdings resulting from drawings other than those on the reserve tranche. See de Vries (1985), Vol. 3, pp. 339–40.

though obviously desirable, such a move was not easy to make, because the Fund's Articles of Agreement specified that "rates of charge normally shall rise at intervals during the period in which the balances are held" (Article V, Section 8). Moreover, any change in the schedule required a 70 percent majority of the total voting power on the Executive Board.[140] The legal difficulty was finessed by a decision that moving to a more flexible approach created circumstances that were not "normal" in the sense of the Article, and that a sliding scale was

[140]Until the 1978 amendments, Article V included a list of specific charges related to the size and duration of outstanding balances, which could be changed by a 75 percent majority.

not required under those circumstances.[141] With that out of the way, consensus was reached in April 1981 on a unified rate, which was set initially at 6¼ percent.[142]

The new unified rate of charge represented an increase in the average rate of about 95 basis points. During the next year, however, because market interest rates continued to rise, the rate of charge actually fell relative to the market. The Board raised the rate again in 1983, to 6.6 percent, and in 1985 to 7 percent. After that, declines in market interest rates and an improvement in the Fund's net income relieved some of the pressure on the rate of charge.

Targeting Net Income

From 1981 on, the major determinant of the rate of charge was the Fund's net income relative to target levels agreed upon by the Executive Board. Toward the end of 1980, the staff circulated a proposal for setting a target for net income each year, which was to be achieved through appropriate adjustments to the interest rates charged on outstanding obligations. The Executive Board held a preliminary discussion of the issue in January 1981 and agreed in principle that the existing system was unsustainable. Without a change in the rules, the Fund was then expected to face an operating deficit in the coming fiscal year of more than SDR 200 million ($250 million). The most troubling aspect of the staff proposal was that charges on Fund credits might have to be set so high as to eliminate the concessional element, discourage countries from borrowing, and aggravate the financial difficulties of already troubled economies. Bernard J. Drabble (Canada) offered an alternative: to set the rate of charge at a fixed percentage of the remuneration rate. That idea generated a lot of interest but foundered on the danger that it could generate volatility and uncertainty in the Fund's charges and still leave the Fund short of revenue. Drabble and some other Directors from creditor countries also offered to support a reduction in the ratio of the remuneration rate to market rates, but the largest creditor countries were reluctant to endorse such a move.

Following two more meetings in March and April, the Board adopted a package that incorporated most of the staff's original proposals. Principally, the Fund would set a target for its net income each year, equivalent to 3 percent of the initial balance of the Fund's reserves. As noted above, the remuneration rate would be raised to 85 percent of the combined market interest rate. The rate of charge would then be determined residually, with the aim of achieving the target in light of the remuneration rate and projections of other relevant data. To achieve a measure of

[141]Statement by George Nicoletopoulos (Director of the Legal Department) at EBM/81/4 (January 7, 1981), pp. 28–29. The official commentary on the quoted phrase explains that "it is not mandatory that there shall be a progression of the periodic rates over time, although it is assumed that a progression will be the normal practice." De Vries (1985), Vol. 3, p. 340.

[142]See Decision No. 6834-(81/65), adopted April 22, 1981; in de Vries, 1985, Vol. 3. The unified rate applied only to the use of the Fund's ordinary resources.

stability, the rate of charge would be set for the financial year as a whole, subject to review after six months in the event of a shortfall in income.[143]

For a while, this new system worked well. The Fund's gross income swelled as a result of several years of heavy lending, and modest increases in the rate of charge sufficed to generate unexpectedly large flows of net income (Figure 17.5 and Table 17.7). Nonetheless, by 1985, it became apparent that trouble lay beneath the surface, for two reasons. First, credit outstanding was growing much more rapidly than the Fund's reserves. From a peak of 9½ percent in 1980, reserves fell to just 3 percent of outstanding credit in 1985. Second, the quality of the Fund's claims was deteriorating as a result of the emergence of substantial and prolonged arrears.

Sharing the Burden of Arrears

As soon as the arrears problem[144] emerged, the Fund's external auditors began alerting management to the need to acknowledge the risks in the published financial statements and to take steps to protect the institution from the effects of potential losses. The Executive Board adopted two of the recommended measures quickly. First, in March 1985, Directors agreed to exclude income that was in arrears by six months or more (SDR 56.4 million in FY 1985) from the official figures.[145] That is, overdue charges were to be reported as "deferred" rather than "accrued" income. Consequently, the IMF had its first annual deficit in net income since 1977 (SDR 30 million). Second, in June, the Board raised the target for annual net income, from 3 percent to 5 percent of beginning-of-period reserves. As the amount of arrears continued to pile up (see Chapter 16), the income target was raised further on a temporary basis, to 7½ percent for FY 1987 and FY 1988, and then was pegged again at 5 percent.[146]

The direct effect of these changes in accounting procedures and financial goals was to raise the rate of charge still further, which put an extra burden on indebted countries at a time when many of them could ill afford it. Concerns over that

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[143]See "Review of the Fund's Charges," SM/80/282 (December 24, 1980), "Revised Pages 24–27," Sup. 1 (January 7, 1981), "Additional Information," Sup. 2 (February 23), and "Charts 1 and 2," Sup. 3 (March 6); "Review of Fund's Charges," SM/81/63 (March 20) and "Additional Information," Sup. 1 (March 27); "Rule 1—Charges on Transactions and Holdings in the General Resources Account," SM/81/89 (April 20); and minutes of EBM/81/3–4 (January 7, 1981), EBM/81/37–38 (March 9), EBM/81/57 (April 15, 1981); and EBM/81/65 (April 22). The new rules also provided for a further review at the end of the financial year and a consideration of how to use or dispose of any excess in net income. For the full set of rules on charges adopted in May 1981, see *Annual Report 1981*, pp. 163–67 and 171.

[144]Also see the final section of Chapter 16, where the development of special charges on overdue obligations, burden-sharing policies, and special reserve accounts is discussed.

[145]Decision No. 7930-(85/41), adopted March 13, 1985; *Annual Report 1985*, p. 115.

[146]The increase to 5 percent was effected through an amendment to Rule I-6(4) adopted on June 5, 1985. The temporary increase to 7.5 percent was implemented as part of the July 1986 decision on burden sharing. For FY 1990, an amount equal to the shortfall in net income for FY 1989 was added to the target, making it 5.7 percent.

prospect came to the fore during the Executive Board's routine review of the Fund's income position in December 1985. The standard calculations implied that the rate of charge would have to be raised immediately from 7 percent to 7.87 percent, which would be above the SDR interest rate.[147] The staff suggested that the burden could be shared in part by creditors if the rate of remuneration were lowered, and in part by the Fund if the target level of net income were lowered. Either action required a 70 percent majority of the votes in the Board. Lowering the income target was widely rejected as financially risky, and creditor countries were split on the prospect of lowering the remuneration rate. Several were sympathetic to the notion of equitable burden sharing, while others argued that even if the rate of charge rose above the SDR rate, borrowers were still getting credits on reasonable and equitable terms (terms that were better than they could obtain from financial markets). Four countries (the United States, Japan, Germany, and the United Kingdom) were opposed to lowering the remuneration rate, and they had enough votes (36 percent) to block it. Consequently, the rate of charge was raised to 7.87 percent, effective November 1, 1985.[148]

Events took an unexpected turn over the next few months. The Fund's net income for FY 1986 turned out to be sharply higher than projected, which made it possible to reverse the increase in the rate of charge and restore it retroactively to 7 percent for the full fiscal year. That action was taken on April 30, 1986, the day the fiscal year ended. The problem of sharing the burden thus was effectively postponed.[149]

A major roadblock in the way of an agreement on burden sharing was that the U.S. Executive Director (then Charles Dallara) was mandated by U.S. law to work toward raising the remuneration rate to the SDR interest rate.[150] Moreover, as Dallara noted during the Board debates, burden sharing by creditors was "anathema" to the U.S. authorities (the Reagan administration).[151] Since no one wanted to impose a solution that would create political problems for the

[147]At that time, the Fund's Rule I–10(d) called for a review of the remuneration rate whenever the rate of charge was projected to rise above the SDR interest rate.

[148]Minutes of EBM/85/176 (December 6, 1985) and EBM/85/180 (December 13). The staff's review of the issue and available options is in "Review of the Fund's Income Position," EBS/85/258 (November 20, 1985). Mtei's intervention was at meeting 85/180, p. 3.

[149]Subsequently, net income for FY 1986 turned out to be even higher. The rate of charge could have been reduced retroactively to 6.73 percent for the second half of the fiscal year, but a majority of the Board preferred to add the excess income to the Fund's reserves. Minutes of EBM/86/73–74 (April 30, 1986). On subsequent developments, see "The Fund's Net Income for FY 1986 and FY 1987—Disposition of Net Income for FY 1986 and Determination of the Rate of Charge for FY 1987," EBS/86/116 (May 28, 1986), and minutes of EBM/86/100 (June 20, 1986).

[150]The remuneration rate at the end of FY 1986 was equal to 92 percent of the SDR interest rate. Under Rule I–10(d), it was being raised from 85 percent in FY 1984 to a level between 95 and 97.5 percent by the end of FY 1987.

[151]Minutes of EBM/86/122 (July 25, 1986), p. 75.

Table 17.9. Burden-Sharing Adjustments to the Rates of Charge and Remuneration, FY 1987–90
(In percent, except as noted)

Period Ending[a]	Deferred Charges (SDR millions)	Basic Rate of Charge	Adjustment	Adjusted Rate of Charge	Basic Rate of Remuneration	Adjustment	Adjusted Rate of Remuneration	Remuneration Coefficient
October 1986	73.1	5.82	0.46	6.28	5.89	0.45	5.44	90.1
January 1987	66.8	5.82	0.77	6.59	5.77	0.76	5.01	85.0
April 1987	41.8	5.81	0.57	6.38	5.87	0.56	5.31	90.5
July 1987	39.8	5.38	0.52	5.90	5.64	0.51	5.13	91.0
October 1987	39.2	5.38	0.52	5.90	6.09	0.52	5.57	91.5
January 1988	47.0	5.38	0.64	6.02	5.70	0.64	5.06	88.8
April 1988	39.3	5.38	0.79	6.17	5.52	0.83	4.69	85.0
July 1988	61.3	5.50	0.92	6.42	5.91	0.88	5.03	85.0
October 1988	46.5	5.50	1.01	6.51	6.86	0.94	5.92	86.3
January 1989	53.9	7.38	0.92	8.30	7.39	0.86	6.53	88.7
April 1989	53.0	7.38	0.96	8.34	8.06	0.90	7.16	88.8
July 1989	59.4	7.67	1.00	8.67	8.17	0.93	7.24	88.6
October 1989	56.9	7.85	0.96	8.81	8.35	0.92	7.43	89.0
January 1990	59.1	8.42	1.00	9.42	8.95	0.92	8.03	89.7
April 1990	59.8	8.62	1.06	9.68	9.16	0.99	8.17	89.2

[a]The initial period ending October 1986 covers six months; all others are three months. For explanation of terms, see text.

Fund's largest member (and one of its largest creditors), a consensus solution was imperative. By July 1986, after a long and occasionally bitter debate, a compromise framework emerged in which the remuneration rate would be raised permanently to 100 percent of the SDR interest rate, subject to a temporary discount as a creditors' contribution toward covering the cost of outstanding arrears.

Beginning in May 1986, the rate of charge on the use of ordinary resources was adjusted upward, and the rate of remuneration was adjusted downward, by roughly equal amounts, to cover the value of deferred charges each quarter (Table 17.9). The burden-sharing agreement provided that half of the required amount was to come from each source, subject to a floor on the adjusted remuneration rate at 85 percent of the SDR interest rate.[152] When the floor was reached (as it was in the first half of 1988), the uncompensated portion of deferred charges would be carried over to the next period. Because the average outstanding amount of balances subject to charges was smaller than the average of remunerable credit balances, the average increase required in the rate of charge (81 basis points through FY 1990) was slightly larger than the average adjustment in the remuneration rate (77 basis points).

[152]Decision No. 8348-(86/122), adopted July 25, 1986; in the Appendix to Chapter 16.

This painting, *No More Funds*, by Ernesto Bertani hung in the anteroom of Managing Director Camdessus's office.

Despite the continual accumulation of arrears, the Fund succeeded in raising reserves gradually in relation to outstanding claims, to 6¼ percent in FY 1990, to a level that was in line with historical (pre-1980s) experience. Along with the buildup in special precautionary balances to cover arrears, these measures averted a crisis in the Fund's finances. That achievement, however, had not been costless, because it had required raising the rate of charge to levels close to short-term market interest rates and thus greatly reducing the concessional element in Fund lending. After a decade of struggle and evolution, the Fund had become both a stronger financial institution and a more conventional financial intermediary.

Appendix I: An Alternative Balance Sheet Presentation

The standard presentation of financial accounts by the IMF treats each of the institution's departments and administered accounts as a distinct entity. Separate balance sheets are presented for the General Department, the SDR Department, the Trust Fund, the ESAF Trust, and other administered accounts that have been in use at various times. That practice reflects the legal and financial differences among those units. For analytical purposes, however, it is also of interest to picture the IMF as a conglomerate in which these different operating units are all overseen by a single management and Board of Directors and are all driven by similar goals as defined in the institutional charter (the Articles of Agreement).

Table 17.A1 presents a consolidated balance sheet for all major financial operations controlled by the IMF. As can be readily seen by comparing this table with Table 17.1, the bulk of the assets and liabilities are those of the General Department, but the stock of SDR allocations in 1989 (SDR 21.4 billion) was nearly as large as the total amount of credit extended through the GRA and administered accounts (24.6 billion). A substantial portion of the assets held by the General Department consists of currencies that are judged to be unusable for operations, and other nonliquid claims. Total allocated SDRs are an additional financial claim on the asset side, matched on the other side by the sum of SDRs held by the Fund and outside (by member countries and prescribed holders). ESAF loans and investments and Trust Fund loans, and their corresponding liabilities, round out the picture. Overall, this conglomerate grew somewhat more rapidly than the General Department alone during the 1980s, and at the end of the decade was nearly 25 percent larger than that one department. Whereas the Fund's own resources, provided primarily by quota subscriptions, amounted to SDR 99 billion at the end of FY 1989, the total stock of assets supplied by or through the Fund totaled SDR 122 billion.

Table 17.A1. Consolidated Balance Sheet of the IMF and ESAF Trust
(Billions of SDRs; see text for explanatory notes)

	December 31, 1978	December 31, 1989	Change
Assets			
Liquid cash assets	5.9	27.4	21.5
Quota subscriptions	39.0	90.1	51.1
Less reserve tranche positions	–8.5	–22.0	(13.5)
Less nonliquid holdings	–26.4	–43.0	(16.6)
SDA (Trust Fund) investments	0.6	0.8	0.2
ESAF Trust investments		0.7	0.7
Nonliquid cash assets	26.4	43.0	16.6
Currently unusable currencies	20.8	28.6	7.8
Undrawn credit commitments	3.2	4.3	1.1
Required working balances	2.4	10.1	7.7
Loans and credits	11.1	24.7	13.5
GRA credits	10.3	22.3	12.0
SAF loans	0.0	1.5	1.5
Trust Fund loans	0.8	0.5	(0.4)
ESAF Trust loans		0.4	0.4
SDR allocations	9.3	21.4	12.1
Receivables	0.1	1.4	1.3
Current charges and interest	0.1	0.5	0.4
Deferred charges		0.9	0.9
Gold (at SDR 35 per ounce)	4.1	3.6	(0.5)
Other assets	0.1	0.2	0.1
Total assets	57.1	121.7	64.5
Liabilities and Net Worth			
Liquid liabilities	14.9	25.5	10.6
Reserve tranche positions	8.5	22.0	13.5
Borrowings (General Department)	6.4	3.5	(2.9)
Balance of quota subscriptions	30.5	68.1	37.6
SDRs outside the Fund	8.1	20.5	12.4
Borrowings by the ESAF Trust		0.6	0.6
Dedicated resources	1.5	3.2	1.8
SDA		2.3	2.3
Trust Fund	1.5	0.5	(1.0)
ESAF Trust		0.5	0.5
Other liabilities	0.2	0.4	0.2
Reserves, etc.	2.0	3.4	1.4
Ordinary reserves	0.7	1.4	0.6
SCA	0.0	0.2	0.2
Deferred charges	0.0	0.9	0.9
SDR holdings	1.2	0.9	(0.3)
Total liabilities and net worth	57.1	121.7	64.5
Memorandum items:			
Gold at market prices	45.9	31.6	–14.4
Unused and available credit lines	5.5	19.4	13.9

Appendix II: IMF Quotas, 1979–89

Table 17.A2. IMF Quotas, 1979–89
(Millions of SDRs)

Member[a]	Sixth General Review 1979–80[b]	Seventh General Review 1981–83[c]	Eighth General Review 1984–89[d]
Afghanistan	45.0	67.5	86.7
Algeria	285.0	427.5	623.1
Angola (9/19/89)	. . .	. . .	145.0
Antigua and Barbuda (2/25/82)	. . .	3.6	5.0
Argentina	535.0	802.5	1,113.0
Australia	790.0	1,185.0	1,619.2
Austria	330.0	495.0	775.6
Bahamas, The	33.0	49.5	66.4
Bahrain	20.0	30.0	48.9
Bangladesh	152.0	228.0	287.5
Barbados	17.0	25.5	34.1
Belgium	890.0	1,335.0	2,080.4
Belize (3/16/82)	. . .	7.2	9.5
Benin	16.0	24.0	31.3
Bhutan (9/28/81)	. . .	1.7	2.5**
Bolivia	45.0	67.5	90.7
Botswana	9.0	13.5	22.1
Brazil	665.0	997.5	1,461.3
Burkina Faso	16.0	24.0	31.6**
Burundi	23.0	34.5	42.7
Cambodia (Democratic Kampuchea)[e]	25.0	25.0	25.0
Cameroon	45.0	67.5	92.7
Canada	1,357.0	2,035.5	2,941.0
Cape Verde	2.0	3.0	4.5
Central African Republic	16.0	24.0	30.4
Chad	16.0	24.0	30.6
Chile	217.0	325.5	440.5
China	550.0	1,800.0	2,390.9
Colombia	193.0	289.5	394.2
Comoros	2.3	3.5	4.5**
Congo	17.0	25.5	37.3
Costa Rica	41.0	61.5	84.1
Côte d'Ivoire	76.0	114.0	165.5
Cyprus	34.0	51.0	69.7
Denmark	310.0	465.0	711.0
Djibouti	3.8	5.7	8.0**
Dominica	1.9	2.9	4.0
Dominican Republic	55.0	82.5	112.1
Ecuador	70.0	105.0	150.7
Egypt	228.0	342.0	463.4
El Salvador	43.0	64.5	89.0
Equatorial Guinea	10.0	15.0	18.4
Ethiopia	36.0	54.0	70.6
Fiji	18.0	27.0	36.5
Finland	262.0	393.0	574.9

Table 17.A2 ***(continued)***

Member[a]	Sixth General Review 1979–80[b]	Seventh General Review 1981–83[c]	Eighth General Review 1984–89[d]
France	1,919.0	2,878.5	4,482.8
Gabon	30.0	45.0	73.1
Gambia, The	9.0	13.5	17.1
Germany, Federal Rep. of	2,156.0	3,234.0	5,403.7
Ghana	106.0	159.0	204.5
Greece	185.0	277.5	399.9
Grenada	3.0	4.5	6.0
Guatemala	51.0	76.5	108.0
Guinea	30.0	45.0	57.9
Guinea-Bissau	3.9	5.9	7.5
Guyana	25.0	37.5	49.2
Haiti	23.0	34.5	44.1
Honduras	34.0	51.0	67.8
Hungary (5/6/82)	. . .	375.0	530.7
Iceland	29.0	43.5	59.6
India	1,145.0	1,717.5	2,207.7
Indonesia	480.0	720.0	1,009.7
Iran[f]	660.0	660.0	660.0
Iraq	141.0	234.1	504.0*
Ireland	155.0	232.5	343.4
Israel	205.0	307.5	446.6
Italy	1,240.0	1,860.0	2,909.1
Jamaica	74.0	111.0	145.5*
Japan	1,659.0	2,488.5	4,223.3
Jordan	30.0	45.0	73.9
Kenya	69.0	103.5	142.0
Kiribati (6/3/86)	. . .	. . .	2.5
Korea	160.0	255.9	462.8
Kuwait	235.0	393.3	635.3
Lao People's Dem. Rep.	16.0	24.0	29.3*
Lebanon	12.0	27.9	78.7
Lesotho	7.0	10.5	15.1
Liberia	37.0	55.5	71.3
Libyan Arab Jamahiriya	185.0	298.4	515.7*
Luxembourg	31.0	46.5	77.0
Madagascar	34.0	51.0	66.4
Malawi	19.0	28.5	37.2
Malaysia	253.0	379.5	550.6
Maldives	0.9	1.4	2.0
Mali	27.0	40.5	50.8
Malta	20.0	30.0	45.1
Mauritania	17.0	25.5	33.9
Mauritius	27.0	40.5	53.6
Mexico	535.0	802.5	1,165.5
Morocco	150.0	225.0	306.6
Mozambique (9/24/84)	. . .	. . .	61.0
Myanmar	73.0	109.5	137.0
Nepal	19.0	28.5	37.3
Netherlands	948.0	1,422.0	2,264.8
New Zealand	232.0	348.0	461.6

Table 17.A2 *(continued)*

Member[a]	Sixth General Review 1979–80[b]	Seventh General Review 1981–83[c]	Eighth General Review 1984–89[d]
Nicaragua	34.0	51.0	68.2*
Niger	16.0	24.0	33.7
Nigeria	360.0	540.0	849.5
Norway	295.0	442.5	699.0
Oman	20.0	30.0*	63.1
Pakistan	285.0	427.5	546.3
Panama	45.0	67.5	102.2
Papua New Guinea	30.0	45.0	65.9
Paraguay	23.0	34.5	48.4
Peru	164.0	246.0	330.9*
Philippines	210.0	315.0	440.4
Poland (6/12/86)[g]	. . .	. . .	680.0
Portugal	172.0	258.0	376.6
Qatar	40.0	66.2	114.9
Romania	245.0	367.5	523.4
Rwanda	23.0	34.5	43.8
St. Kitts and Nevis (8/15/84)	. . .	. . .	4.5
St. Lucia (11/15/79)	3.6	5.4	7.5
St. Vincent and the Grenadines (12/28/79)	1.7	2.6	4.0
São Tomé and Príncipe	2.0	3.0	4.0*
Saudi Arabia	600.0	1,040.1	3,202.4
Senegal	42.0	63.0	85.1
Seychelles	1.3	2.0	3.0
Sierra Leone	31.0	46.5	57.9
Singapore[h]	49.0	92.4	92.4
Solomon Islands	2.1	3.2	5.0
Somalia	23.0	34.5	44.2
South Africa	424.0	636.0	915.7
Spain	557.0	835.5	1,286.0
Sri Lanka	119.0	178.5	223.1
Sudan	88.0	132.0	169.7
Suriname	25.0	37.5	49.3
Swaziland	12.0	18.0	24.7
Sweden	450.0	675.0	1,064.3
Syrian Arab Republic	63.0	94.5	139.1*
Tanzania	55.0	82.5	107.0
Thailand	181.0	271.5	386.6
Togo	19.0	28.5	38.4
Tonga (9/13/85)	. . .	. . .	3.3
Trinidad and Tobago	82.0	123.0	170.1
Tunisia	63.0	94.5	138.2
Turkey	200.0	300.0	429.1
Uganda	50.0	75.0	99.6
United Arab Emirates[i]	120.0	202.6	202.6
United Kingdom	2,925.0	4,387.5	6,194.0
United States	8,405.0	12,607.5	17,918.3
Uruguay	84.0	126.0	163.8
Vanuatu (9/28/81)	. . .	6.9	9.0
Venezuela	660.0	990.0	1,371.5
Vietnam	90.0	135.0	176.8

Table 17.A2 ***(concluded)***

Member[a]	Sixth General Review 1979–80[b]	Seventh General Review 1981–83[c]	Eighth General Review 1984–89[d]
Western Samoa	3.0	4.5	6.0
Yemen Arab Republic	13.0	19.5	43.3
Yemen, People's Dem. Rep. of	41.0	61.5	77.2
Yugoslavia	277.0	415.5	613.0
Zaïre	152.0	228.0	291.0
Zambia	141.0	211.5	270.3
Zimbabwe (9/29/80)	100.0	150.0	191.0*
Total	39,116.5	59,999.9	90,132.6

[a]For countries that became members after 1978, the effective date of membership is given in parentheses.

[b]Quotas under the Sixth General Review came into effect during 1978. Four member countries (Comoros, Guinea-Bissau, São Tomé and Príncipe, and Seychelles) did not participate in that review.

[c]Quotas under the Seventh General Review came into effect during December 1980, except for Oman (February 1981), which is marked with an asterisk. For exact effective dates, see *Annual Report 1981*, pp. 131–33.

[d]Quotas under the Eighth General Review in most cases came into effect during December 1983. Those marked with asterisks came into effect during the first four months of 1984; for exact effective dates, see Annual Report 1984, pp. 106–108.

[e] Democratic Kampuchea did not consent to the quota increases proposed under any of these reviews.

[f]Iran did not consent to the quota increases proposed under the Seventh and Eighth Reviews.

[g]Poland became an Original Member of the Fund in January 1946, withdrew in March 1950, and was readmitted in June 1986.

[h]Singapore did not consent to the quota increase proposed under the Eighth General Review.

[i]United Arab Emirates did not consent to the quota increase proposed under the Eighth General Review.

*See footnote *c*.

**See footnote *d*.

Appendix III: Formulas for the Eighth General Review of Quotas

Calculated Quotas

Calculated quotas for the Eighth General Review were computed from a set of five equations, as agreed upon by the Executive Board in August 1982. The general formula for all five equations may be written as

$$Q_c = (\beta_1 Y' + \beta_2 R' + \beta_3 M' + \beta_4 X' + \beta_5 V') \times (1 + \beta_6 X'/Y) \times A, \quad (1)$$

where Q_c is the calculated quota, the remaining notation is the same as in footnote 25 on p. 860, and all data were measured in SDRs for 1980:

Y' = GDP
R' = total international reserves
M' = imports of goods and services
X' = exports of goods and services ($X' - M'$ = balance on current account)
V' = variability in export receipts: $V' = \sqrt{(\sum_{t-3}^{11} (X'_t - \bar{X}'_t)^2)/3}$.

A is an adjustment factor that makes all five formulas yield the same aggregate quota.

Table 17.A3. Coefficients for Quota Formulas

Formula	$\beta_1(Y')$	$\beta_2(R')$	$\beta_3(M')$	$\beta_4(X')$	$\beta_5(V')$	$\beta_6(X'/Y)$	A
Bretton Woods	.01	.025	.05	0	.2276	1	1
III	.0065	.0205125	.078	0	.4052	1	.87554669
IV	.0045	.0389678	.07	0	.7697	1	.84548032
M4	.005	.042280464	.044	.044	.8352	0	.89703152
M7	.0045	.05281008	.039	.039	1.0432	0	.89568343

Note: As noted in the text, each country's calculated quota was computed as the higher of the quota from the reduced Bretton Woods formula and the simple mean of the two lowest values from the four derivative formulas.

The coefficients for the five formulas, with the designations used in the original presentation, are set out in Table 17.A3.

Actual Quotas

The basic formula used in the Eighth General Review for determining each country's proposed quota may be written as follows:

$$Q = aQ_c + (1 - a)(1 + p)Q_0, \quad (2)$$

where a is the "adjustment coefficient" discussed on p. 867, p is the percentage increase in total quotas, and Q_0 is the country's initial quota.

The adjustment coefficient is determined by the size of the increase (p) and the portion (s) of the total increase allocated to selective increases. To see this relationship, first note that the change in an individual quota may be decomposed into a selective and a general increase:

$$(Q - Q_0) = [s(Q_c/T) + (1 - s)(Q_0/T_0)](T - T_0), \quad (3)$$

where T and T_0 are the new and old magnitudes of total quotas, respectively.

Since $p \equiv T/T_0 - 1$, equation (3) may be rewritten as

$$(Q - Q_0)/T = [s(Q_c/T) + (1 - s)(Q_0/T_0)]p/(1 - p). \quad (4)$$

Successively rearranging terms, one eventually gets to

$$(Q/T - Q_0/T_0) = s\left(\frac{p}{1 + p}\right)(Q_c/T - Q_0/T_0). \quad (5)$$

Now define the adjustment coefficient a as the change in each country's quota share in proportion to the gap between the calculated and initial share:

$$a \equiv (Q/T - Q_0/T_0) \div (Q_c/T - Q_0/T_0). \quad (6)$$

Substituting equation (6) into equation (5) gives

$$a = sp/(1 + p). \quad (7)$$

In the Eighth General Review, the proposed quota increase was 47.5 percent ($p = 0.475$), and 60 percent of the increase was allocated to selective increases ($s = 0.6$). By equation (7), the adjustment coefficient was 19.3 percent ($a = 0.193$). (The highest possible coefficient, with $s = 1$, would have been 32.2 percent.)

Calculation of the U.S. quota illustrates the application of the formula. The initial quota share for the United States was 20.7 percent, and the calculated quota share was 16.8 percent. The adjustment coefficient implies that 19.3 percent of that gap was to be closed, making the new quota share 19.9 percent. Consequently, instead of a 47.5 percent increase (if $s = 0$), the United States got an increase of 42.1 percent. The lowest increase it could have got under this system (if $s = 1$) would have been 38.6 percent.

Appendix IV: Policies on Enlarged Access

In April 1980, the Managing Director alerted the Interim Committee to an expected tightening in the Fund's liquidity position as a result of rising demand for Fund credits.

World Economic Outlook and the Role of the Fund in Payments Adjustment and Financing Report to the Interim Committee, April 25, 1980

Mr. Chairman, the world economic picture is decidedly grim. The main difficulties include the severe worldwide problem of inflation, the marked slowdown of economic activity now under way in the industrial countries, the sudden and major worsening of the distribution of current account balances among major groups of countries, and the urgent need for both conservation and new sources of energy.

. . . the outlook for 1980 with respect to the financing of balance of payments imbalances is reasonably reassuring, although this is true only in an overall sense and does not reflect the problems in a number of individual countries that will be difficult to tackle. This relatively "easy" situation we have at present can be explained, in particular, by the existence of cushions of reserve holdings, and by the volume of bank credits which are in the pipeline, having been committed but not yet disbursed.

However, the ability to meet the financing problem in 1980 is not a reason for complacency. The expected further increase in the current account deficit of the non-oil LDCs in 1981, coupled with virtual stagnation in the volume of import growth, foreshadows a very difficult situation. Indeed, even now there are some warning signals in the financial markets: an increase in spreads, a shortening of maturities, and greater selectivity exercised by commercial banks in taking up new risks. And the signals suggest that banks might become more cautious in the recycling process as time goes by, and perhaps less active in this very essential intermediation function. Nevertheless, everyone agrees that, in the years ahead, the commercial banks will continue to play the major role in the recycling process, although perhaps with a more selective touch.

From our discussions in the Fund, I think there is a broad consensus that this institution should stand ready to assume an increasing role in recycling and to continue to promote adjustment. Both these aspects—recycling and adjustment—are closely linked. There was full agreement in our discussions in the Executive Board that the Fund should not undertake recycling on an unconditional basis. Certain elements of the Fund's role in the present situation are crucial. To begin with, in view of the size of the current deficits and of the difficulties that may arise in private intermediation, the Fund must be prepared, when necessary, to lend in larger amounts than in the past. I might summarize the views expressed on this in our discussions as a combination of flexibility and caution, with a readiness to go beyond the existing ceilings in relation to countries' quotas if and when special circumstances arise.

Secondly, the structural problems faced by many countries may require that adjustment take place over a longer period than has been typical in the framework of our programs in the past. In view of the difficulty of predetermining a set of precise corrective measures of a structural nature for a long period in the future, it may well be necessary for our programs to cover periods of one or two years, but accompanied by indications on how the adjustment and the policies are to be completed over the medium term. Our putting forward increased resources for balance of payments financing would of course facilitate adjustment and stretch it over a realistic period. It would also help the Fund to convince borrowing countries to engage in sound adjustment policies at a sufficiently early stage. Moreover, our lending must reflect in practice the sort of flexibility, with an awareness of the circumstances of members, that is called for in the Executive Board's current guidelines on conditionality.

. . . On the question of mustering additional resources for the Fund to use, I think we all recognize that present liquidity in the Fund is adequate for the moment, taking account of the Fund's regular resources and the fact that a large part of the supplementary financing facility resources have not yet been committed. In the longer run, Fund liquidity needs should be satisfied primarily through increases in quotas, which have, relative to international trade, been dramatically reduced since the early days of the Fund. Meanwhile, let me emphasize the importance of early consent to the Seventh Quota Review. In addition, the Fund should be ready to organize borrowing operations on appropriate terms as soon as needed.

The Interim Committee responded positively to the Managing Director's appeal.

. . . 3. In view of the outlook for the world economy and, in particular, the prospect of large and widespread payments imbalances, the Committee agreed that the Fund should stand ready to play a growing role in the adjustment and financing of these imbalances. In this connection the Committee endorsed the views set forth in the Managing Director's statement on the subject and agreed with him that any such financing by the Fund should be made available in conjunction with adjustment policies appropriate to the needs and problems of members in the present economic situation.

The Committee recognized that, in view of the availability of funds under the supplementary financing facility and the expected increase in quotas under the Seventh General Review, the Fund is, under present circumstances, in a relatively liquid position. Nevertheless, in the light of the size and the distribution of payments imbalances, the necessity to phase adjustment over a reasonable period of time, and the time needed for the completion of any borrowing arrangements, the Committee encouraged the Managing Director to start discussions with potential lenders on the terms and conditions under which the Fund could borrow funds to increase its resources, if and when the need arises.

The following year, the Executive Board adopted a policy on enlarged access, allowing for a substantial widening in lending limits on a temporary basis.

Policy on Enlarged Access to the Fund's Resources
Executive Board Decision—March 11, 1981

1. From the date on which the Fund determines that all available supplementary financing has been committed and additional borrowing arrangements have been concluded,

the Fund will be prepared to provide balance of payments assistance to members facing serious payments imbalances that are large in relation to their quotas in accordance with this decision (hereinafter referred to as "Enlarged Access"). Access to the Fund's resources under this decision will be provided under a stand-by or an extended arrangement, and purchases under the arrangement will be financed by resources that the Fund obtains for this purpose by replenishment under Article VII, Section l(i) (hereinafter referred to as "borrowed resources"), in conjunction with the use of the other resources of the Fund (hereinafter referred to as "ordinary resources").

2. Access to the Fund's resources under other policies of the Fund will remain available in accordance with the terms of those policies.

3. A member contemplating use of the Fund's resources under this decision shall consult the Managing Director before making a request for such use. A request will be met only if the Fund is satisfied: (i) that the member needs financing from the Fund that exceeds the amount available to it in the four credit tranches or under the Extended Fund Facility and its problem requires a relatively long period of adjustment and a maximum period for repurchase longer than the three to five years under the credit tranche policies; and (ii) on the basis of a detailed statement of the economic and financial policies the member will follow and the measures it will apply during the period of the stand-by or extended arrangement, that the member's program will be adequate for the solution of its problem and is compatible with the Fund's policies on the use of its resources beyond the first credit tranche or under the Extended Fund Facility.

4. The Fund may approve a stand-by or extended arrangement that provides for Enlarged Access at any time until the Eighth General Review of Quotas becomes effective, provided that the Fund may extend this period.

5. A stand-by or extended arrangement approved under this decision will be in accordance with the Fund's policies, including the policies on conditionality, phasing and performance criteria.

6. The period of a stand-by arrangement approved under this decision will normally exceed one year, and may extend up to three years in exceptional cases. The period of an extended arrangement will be normally three years.

7. The amounts that will be made available under stand-by or extended arrangements approved under this decision will be determined according to guidelines adopted by the Fund from time to time.

8. The amounts available under a stand-by or extended arrangement approved under this decision will be apportioned between ordinary and borrowed resources as follows:

(a) Under a stand-by arrangement purchases will be made with ordinary and borrowed resources in the ratio of 2 to 1 in the first credit tranche, and 1 to 1.2 in the next three credit tranches. Thereafter, purchases will be made with borrowed resources only. In the event that a member has already an outstanding use of all or part of its credit tranches because of previous purchases in the credit tranches or under the extended Fund facility, purchases will be made first with borrowed resources until that use of borrowed resources, together with any outstanding use of supplementary financing and exceptional use of the Fund's resources under Decision No. 5732-(78/65), adopted April 24, 1978, as amended on December 27, 1978, equals the amount of borrowed resources that would have been used if the previous purchases had been made under this decision.

(b) Under an extended arrangement purchases will be made with ordinary and borrowed resources in the ratio of 1 to 1 until the outstanding use of the upper credit tranches and the extended Fund facility equals 140 percent of quota. Thereafter, purchases

will be made with borrowed resources only. In the event that a member already has an outstanding use of all or part of its upper credit tranches or the extended Fund facility, purchases will be made with borrowed resources until that use of borrowed resources, together with any outstanding use of supplementary financing and exceptional use of the Fund's resources under Decision No. 5732-(78/65), adopted April 24, 1978, as amended on December 27, 1978, equals the amount of borrowed resources that would have been used if the outstanding use of the upper credit tranches and the extended Fund facility had been made under this decision.

(c) The apportionment in accordance with (a) and (b) above will be made on the basis of the outstanding use by the member of the Fund's resources at the time the arrangement for the member is approved.

(d) From time to time the Fund will review the proportions of ordinary and borrowed resources specified in (a) and (b) above and may modify them, and the modified proportions shall apply uniformly to both arrangements approved after the modification and amounts that may be purchased under existing arrangements after the modification.

9. (a) A stand-by or extended arrangement approved under this decision may provide, in part, for supplementary financing in accordance with Decision No. 5508-(77/127), adopted August 29, 1977, if

(i) the arrangement replaces an arrangement approved under that decision, or

(ii) an amount of supplementary financing becomes available because of the cancellation of an arrangement or because it is reasonably certain that an arrangement will not be fully utilized, in which case the arrangement approved under this decision may provide for the utilization of a part or all of the available amount.

(b) When an arrangement under this decision provides for supplementary financing, the supplementary financing will be used before borrowed resources.

10. (a) Repurchases in respect of outstanding purchases under this decision will be made in accordance with the provisions of the Articles of Agreement and decisions of the Fund, including those relating to repurchase as the member's balance of payments and reserve position improves, provided that repurchases in respect of outstanding purchases financed by borrowed resources shall be completed seven years after the purchase, and that the repurchases shall be made in equal semiannual installments during the period beginning three and one half years and ending seven years after the purchase.

(b) If a purchase is financed by ordinary and borrowed resources, a repurchase attributed to the purchase made with borrowed resources in advance of this schedule of installments must be accompanied by a repurchase in respect of the purchase made with ordinary resources at the same time if any part of the latter purchase is still outstanding. The amounts of the two repurchases will be in the same proportions in which ordinary and borrowed resources were used in the purchases, provided, however, that the repurchase in respect of the purchase financed with ordinary resources will not exceed the amount of the purchase still outstanding.

11. In order to carry out the purposes of this decision, the Fund will be prepared to grant a waiver of the limitation in Article V, Section 3(*b*)(iii) that is necessary to permit purchases under this decision or to permit purchases under other policies that would raise the Fund's holdings of a member's currency above the limits referred to in that provision because of purchases outstanding under this decision.

12. The Fund will apply its credit tranche policies as if the Fund's holdings of a member's currency did not include holdings resulting from purchases under this decision that have been made with borrowed resources. Purchases under this decision with borrowed resources and holdings resulting from these purchases will be excluded under Article XXX(*c*).

13. The Fund will state which purchases by a member are made under this decision and the amounts of ordinary and borrowed resources used in each purchase.

14. The Fund will determine the charges that it will levy on holdings of a member's currency resulting from purchases outstanding under this decision to the extent that they are made with borrowed resources.

15. The Fund will review this decision not later than June 30, 1983, and annually thereafter as long as the decision remains in effect.

Decision No. 6783-(81/40), adopted March 11, 1981

In 1982, as the Fund's liabilities to finance the enlarged access policy were rising, the Executive Board adopted guidelines that limited the aggregate amounts that the Fund could borrow.

Guidelines for Borrowing by the Fund

Quota subscriptions are and should remain the basic source of the Fund's financing. However, borrowing by the Fund provides an important temporary supplement to its resources. In present circumstances, it facilitates the provision of balance of payments assistance to its members under the Fund's policies of supplementary financing and enlarged access.

The confidence of present and potential creditors in the Fund will depend not only on the prudence and soundness of its financial policies but also on the effective performance of its various responsibilities, including, in particular, its success in promoting adjustment.

Against this background the Executive Board approves the following guidelines on borrowing by the Fund.

1. Fund borrowing shall remain subject to a process of continuous monitoring by the Executive Board in the light of the above considerations. For this purpose, the Executive Board will regularly review the Fund's liquidity and financial position, taking into account all relevant factors of a quantitative and qualitative nature.

2. Subject to paragraph 4 below, the Fund will not allow the total of outstanding borrowing plus unused credit lines to exceed the range of 50–60 per cent of the total of Fund quotas. If the total of outstanding borrowing plus unused credit lines reaches the level of 50 per cent of quotas, the Executive Board shall assess the various technical factors that determine, at that time, the availability of balances of unused lines of credit. While this assessment is being made, the total of outstanding borrowing plus unused credit lines may rise, if necessary, beyond 50 per cent, but shall not exceed 60 per cent of total quotas.

3. Recognizing that the credit lines of all participants in the General Arrangements to Borrow (GAB) cannot be used at the same time and that the GAB can be activated only to finance purchases by a GAB participant, the total of outstanding borrowing plus unused credit lines under paragraph 2 above shall include, in respect of the GAB, either outstanding borrowing by the Fund under the GAB or one half of the total of credit lines under the GAB, whichever is the greater.

4. In the case of major developments, the Executive Board shall promptly review, and may adjust, the guidelines. In any event, the guidelines shall be reviewed when the Board of Governors has completed the Eighth General Review of Quotas, and may be adjusted as a result of that review of the guidelines.

5. The percentage limits specified in paragraph 2 above, or any other limits that may be adopted as a result of a review pursuant to paragraph 4 above, are not to be understood, at any time, as targets for borrowing by the Fund.

Decision No. 7040-(82/7), adopted January 13, 1982

These guidelines were amended in December 1983 to take account of new developments, including the expansion and revision of the GAB.

Guidelines for Borrowing by the Fund—Revised

. . . 1. Fund borrowing shall remain subject to a process of continuous monitoring by the Executive Board in the light of the above considerations. For this purpose, the Executive Board will regularly review the Fund's liquidity and financial position, taking into account all relevant factors of a quantitative and qualitative nature.

2. Subject to paragraph 4 below, the Fund will not allow the total of outstanding borrowing plus unused credit lines to exceed the range of 50–60 percent of the total of Fund quotas. If the total of outstanding borrowing plus unused credit lines reaches the level of 50 percent of quotas, the Executive Board shall assess the various technical factors that determine, at that time, the availability of balances of unused lines of credit. While this assessment is being made, the total of outstanding borrowing plus unused credit lines may rise, if necessary, beyond 50 percent, but shall not exceed 60 percent of total quotas.

3. The total of outstanding borrowing plus unused credit lines under paragraph 2 above shall include, in respect of the GAB and borrowing arrangements associated with the GAB, either outstanding borrowing by the Fund under these arrangements, or two thirds of the total of credit lines under these arrangements, whichever is the greater.

4. In the case of major developments, the Executive Board shall promptly review, and may adjust, the guidelines. In any event, the guidelines shall be reviewed when the Board of Governors has completed the Ninth General Review of Quotas, or when there is a significant change in the GAB or associated arrangements, and may be adjusted as a result of such reviews.

5. The percentage limits specified in paragraph 2 above, or any other limits that may be adopted as a result of a review pursuant to paragraph 4 above, are not to be understood, at any time, as targets for borrowing by the Fund.

Decision No. 7589-(83/181), adopted December 23, 1983

Those guidelines remained in effect until November 1991, when they were replaced by a general policy that guidelines could be adopted again in the future as needed; see Annual Report 1992, *p. 121.*

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