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PART A

Begins: 1/2/83

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1/9/95

CHANCELLOR'S MEETINGS AT  
THE INTERNATIONAL  
MONETARY FUND (IMF)

PART A



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TREASURY AND CIVIL SERVICE COMMITTEE

1<sup>st</sup> February 1983

Dear Michael,

I enclose a transcript of the evidence given by you to the Committee. I should be grateful if you would examine this and make in ink such alterations as are:

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- ii) restricted to the correction of matters of fact which do not materially alter the general sense of any answer.

Minor alterations to the style or grammar of any answer should not be made.

You should not alter any Question, and if you wish to explain or give any additional information, you may either submit a footnote to your evidence at the appropriate point, or submit a Memorandum.

I should be grateful further if you would return the corrected copy to reach me within ~~seven~~ <sup>seven</sup> days from the date of this letter. If special circumstances make this impossible please let me know, but if I do not hear from you to that effect, and do not receive the corrected transcript within the time indicated, the evidence will be published in its original form.

You should not make any public use of this copy of the evidence.

Yours,

Steve Barrett

S.D. Barrett  
Assistant to the Clerk to the Committee

Enc.

HOUSE OF COMMONS  
MINUTES OF EVIDENCE  
TAKEN BEFORE THE  
TREASURY AND CIVIL SERVICE COMMITTEE

MONDAY 31 JANUARY 1983

THE RT. HON. SIR GEOFFREY HOWE, QC, MP, MR J.G. LITTLE, CB,  
MR J. ODLING-SMEE and MR D.L.C. PERETZ

Evidence taken in Public

Questions 1313 - 1413

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MONDAY 31 JANUARY 1983

Members present:

Mr Edward du Cann, in the Chair

Mr Anthony Beaumont-Dark  
Dr Jeremy Bray  
Mr John Browne  
Mr Michael English

Mr Terence Higgins  
Mr Ralph Howell  
Mr Michael Meacher  
Mr Richard Wainwright

THE RT. HON. SIR GEOFFREY HOWE, QC, MP, Chancellor of the Exchequer, a Member of the House, examined; MR J.G. LITTLER, CB, Second Permanent Secretary, Overseas Finance Sector, MR J. ODLING-SMEE, Under Secretary, Finance Economic Unit, and MR D.L.G. PERETZ, Assistant Secretary, Balance of Payments Division, of H.M. Treasury, called in and examined.

Chairman

1313. Chancellor, we are very grateful to see you. As you know, you have been kind enough to follow the work of this Committee with a particular interest when exactly twelve months ago we made the decision to make a long term inquiry into international financial arrangements. Of course, bearing in mind what happened since, it might be thought that that was a prescient decision. Certain things that have happened have undoubtedly been very worrying and we are glad to have an opportunity now to talk to you about them. We thought it right not only, as you are very well aware, to talk to you, to the Governor and to Treasury officials and to receive evidence from academics and practical people, broadly speaking on a world-wide basis, but to visit the United States and talk to the Chairman of the Federal Reserve and the International Monetary Fund and so on. I am asked by the Committee to express to you our gratitude for all the help that you have been good enough to

give us in relation to that visit and to the inquiry in general. We thought today, if it is agreeable to you, we would divide our discussion into two: first to talk about the exchange rate system which is perhaps the most important longer term matter we want to inquire into; and secondly to talk about the debt crisis. There are a number of overlaps about policy, coordination, world liquidity and the like, and I think we can see how these evolve if we can divide our discussions broadly in that way. Although there are a number of matters which are highly topical at the present time, the Committee is much more concerned to consider the general issues rather than perhaps to fix on any particular matter, and I think that is probably right. Chancellor, I understand that it would be convenient to you, and I am sure it would be helpful to the Committee, if you were to make a short opening statement. Please do so, if you would like, and we will start our general discussion.

(Sir Geoffrey Howe) Can I begin by welcoming, if that is not too pompous a thing to do, the Committee's interest in this very important area, because it is clearly one of great significance not just to this country, and expressing my appreciation for what you have said about the arrangements made for your visit to North America. Perhaps I can also introduce my team. Mr Littler is the new Second Permanent Secretary in charge of Overseas Finance. He has had considerable experience in the field before and he takes the place of Sir Kenneth Couzens, to whom one should, I think, pay a tribute, although it may be unusual to do so; but he has achieved a considerable reputation and success in the international field over the seven years he has been there, which is a long time. He has now moved on to the Department of Energy. Then there is Mr Odling-Smee, who came back two months ago after two years of

secondment to the International Monetary Fund; he is Under Secretary in charge of the Finance Economic Unit of the Treasury. Mr Peretz is Assistant Secretary and Head of EF.1 Division, which is the Balance of Payments Division in the Overseas Finance Sector. May I take advantage of your other opening remark, by making what I hope will be quite a short opening statement, because the subject is sufficiently important and the issues sufficiently relevant and timely, since I shall be presiding over the IMF Interim Committee next week, for me to say something about the way in which I see the problems of the international financial system at the present time? As the Committee knows, there have been suggestions that there is a need for a new Bretton Woods, and I share the concern that prompts that suggestion, a concern for greater stability and order in international financial relationships as a basis for renewed economic progress. We all would like to achieve lower inflation, less volatile exchange rates, a more orderly system of international lending and borrowing; but it is my own judgement that a suggestion for a new Bretton Woods does not give the right kind of signal as to what is, in practice, needed. As stated it implies a need for new objectives, new methods, new international financial institutions. It pays too little attention to the reason why international financial markets and exchange rates in particular have been so volatile in recent years and too little attention as well to what practical steps can be taken to remedy that. The Bretton Woods system provided a basis for stability through the discipline it imposed, and as long as the United States dollar remained dominant and the economy on which it was based set a pattern of reasonably well maintained currency value, the system was effective; but those conditions were eroded in the 1960s, and

as too many countries sought to maintain ambitious growth rates without sufficient discipline, the world lived for a decade on increasingly insecure foundations of inflation and rising indebtedness.

\* I, of course, accept that the world will not achieve stability again until we create a satisfactory framework and disciplines which ensure more consistent policies and restore confidence in currencies, but it is no longer conceivable, certainly in the foreseeable future, that such a framework should be built upon one currency, on Bretton Woods lines. Eighteen months ago, at the annual IMF meeting in Washington, I suggested that we must in future seek stability through the cooperation of the major countries whose currencies make up the Special Drawing Rights, that is, the United States, Japan, France, Germany and the United Kingdom. We still have a long way to go, but the notion that these five countries bear a special responsibility to the rest of the world is increasingly recognised; and it is also increasingly recognised that they must exercise that responsibility by seeking parallel or convergent economic and financial policies within their own boundaries which will serve to maintain the values of their currencies, absolutely and in relation to each other. Of course that does not imply a rigid straitjacket, nor is it meant to imply that complete arrangements will be settled quickly, or made effective without difficulty, but I am sure this is the practical way forward. Our immediate priority, in the short term, is to nurture the process of recovery through a very difficult period. At last year's annual IMF meeting in Toronto I again identified several of the goals we should be seeking now. I said that the world was passing through a difficult transitional phase as economies adjusted to lower inflation. It is true of the world economy, as of our own,



that a price has to be paid for errors spread over more than a decade. It has long seemed to me that the more ready and willing we are to accept that conclusion, the less onerous it will be and the sooner we shall have the chance of ensuring sustainable growth. There are now growing signs of recovery, earlier in some countries than in others, but its pace will not and should not be too rapid. As different countries successively begin to overcome their own problems of imbalance and inflation, world recovery as a whole should gain strength. But there are important dangers against which we need to guard, and in respect of which some important practical steps need to be taken. Let me now try to summarise the broad strategy which, speaking now as Chairman of the IMF Interim Committee, I believe we shall need to follow over the months and years ahead. It is essentially pragmatic - and I make no apology for that. The dual aim, which is now pretty widely shared, is so to manage the recovery that it is sustained without rekindling inflation and so jeopardising the stability of the international financial system; and at the same time to ensure that those countries with particularly severe debt problems are restored to economic health. I will pick out four elements of the strategy for recovery that seem to me to be particularly important. First, major countries need to continue collectively to pursue prudent monetary and fiscal policies. This is the key to stability. It was underlined by the undertakings made at last year's Versailles Summit on the pursuit of convergent policies. This, rather than artificial capital controls or massive intervention, is the way to reduce exchange rate volatility. Intervention has a role to play, but essentially I think Dr Emminger was right to refer to it as a side issue, and to say that we should concentrate on promoting

better underlying conditions. This is the way to make the multi-currency reserve system work. Second, within the overall framework of prudent policies, countries need to ensure that the balance of their individual policies is right. In some countries where inflation has been brought down, where the budget deficit is under control and the external position strong, there may be scope for a rise in domestic activity to sustain the recovery. In others continued firm policies may be needed rather longer. Nowhere would it be wise to let up in the fight against inflation.

A particular responsibility rests with the United States. Their success in reducing inflation has been impressive, but the rising budget deficit, if unchecked, could risk a renewed surge in prices and interest rates just when recovery is getting under way.

Mr Martin Feldstein, Chairman of the Council of Economic Advisers, said last November - and I quote: "I do not see how we can have a healthy economic recovery unless we have deficits coming down and coming down substantially". Accordingly I welcome President Reagan's recognition, in his State of the Union address last week, of the need to restrain the growth in the Federal deficit. But the future figures are strikingly large and the task formidable; he will need the full cooperation of Congress if the deficit is to be put, as it plainly must be for the health of the world economy, on a convincingly declining path. Third, there is the need for adjustment by major debtors, the scale of whose difficulties has at times threatened to overwhelm the international financial and banking system. Here, the IMF has a crucial role. As Chairman of the Interim Committee, I intend to do my utmost to see that the Fund has the resources to play its role effectively. We made a welcome start earlier this month when the Group of Ten industrial

countries agreed to increase the General Arrangements to Borrow from Special Drawing Rights of 6.4 billion to Special Drawing Rights of 17 billion, and in addition to make credits available to the Fund for lending to non-participants if major payments imbalances threaten the stability of the international monetary system. Next week in Washington we shall be seeking to put in place a further element in the package by agreeing to a substantial increase in Fund quotas at the Interim Committee meeting which I have asked to be brought forward from April. Active adjustment policies supported by IMF finance should help substantially to restore confidence and encourage continued private banking flows which are essential to many developing countries. Adequate supervision and prudent individual risk assessments are also essential components of a stable system, and it is clearly part of our present task to build - at this stage often by working more or less informally and from case to case - on the important progress made in this area in recent years. The fourth element of the strategy for the recovery is the need to avoid protectionism. I do not believe that the way to solve payments problems and exchange rate fluctuations is through increased restrictions on trade which can only impoverish us all. I am grateful to you, Mr Chairman, for allowing me to set out briefly to the Committee how I see these major international issues that confront us. My main conclusion is that we cannot look at the system in the abstract or seek remedies for real difficulties in artificial mechanisms. There is no substitute for collective agreement among countries on sound policies, and their translation into individual practice. And there is no realistic alternative to the pragmatic approach of building on the existing international institutions and ensuring they are effective. It is a task to

which the world's financial authorities must be seen to apply themselves with all diligence and a proper sense of urgency, and that, certainly, is the approach of Her Majesty's Government.

1314. Thank you very much. It is very useful to have your views as Chairman of the Interim Committee. Could I first associate the Committee warmly with the tribute you paid to Sir Sir Kenneth Couzens and to welcome you and your colleagues here. Would you allow me on behalf of the Committee to congratulate you on your Chairmanship of the Interim Committee. I am sure that the general views that you have just been expressing are those which are very much in the minds of the Committee. Incidentally, there were, as you will appreciate, prominent among those which we had the opportunity to talk to Mr Feldstein, Dr Sprinkel, and Mr Volcker, and academics, Members of Congress and others of you in New York. But rather than go through those matters I think it would be better if I call individual members of the Committee to express a view; but again thank you for your introduction.

(Sir Geoffrey Howe) Yes, certainly.

Mr English

1315. I should like to start by saying a few words to thank the Chancellor for his assistance in regard to our visit to Washington and New York. Chancellor, Sir Terence Beckett, according to the Financial Times of 22nd January, said, "We are still 20 per cent less competitive than our main trading rivals". He was referring, I think, to the exchange rate, although in the quotation he does not actually say so. Do you agree?

(Sir Geoffrey Howe) I think it is misleading to rest oneself on a single figure of that kind, because there are a number of different components which go to make up competitiveness, and I leave on one side the obvious ones, quality, delivery and

performance, in that respect. But the concept of competitiveness as a measuring tool does bring together two quite different ideas. One is the competitiveness in terms of improvement of unit labour costs and the improvement of cost efficiency in that sense, and any improvement of that kind is pure nett gain, as it were; but it also embraces the impact of relative exchange rate positions, and it goes without saying, but it should be said even so, that an improvement in competitiveness achieved by exchange rate movements, an initial improvement in price competitiveness, of that kind carries with it of course the risk of offsetting features, namely, an increase in the cost of imported materials and made-up components and so on, and therefore is intrinsically less desirable than improved competitiveness achieved by sheer performance. If you actually look at the figure you quote of 20 per cent \_\_\_\_\_

1316. No, I just quoted from the Financial Times - I was quoting him.

(Sir Geoffrey Howe) Exactly, I am shorthanding that for the moment. That, I think, is by reference to the base date of 1975, which is the one we conventionally take. I think we ought not to be too beguiled by that particular base date. If one takes, for example, the second quarter of 1979 when there was not a notable chorus of complaint about competitiveness, then the figure is significantly less than that. It is 10 per cent in relative actual unit labour costs and actually plus one - in other words, no deterioration set in relative export prices. So I think one has to be very careful not to endorse, put in orbit and then endorse, a figure which appears to be a figure for which one wishes to see changes on only one side of the account and the exchange rate is only on one side of the account. One also has to remember the underlying figure must

be affected and must have been affected over that particular period by the accession of oil as a component of our currency and by the fact that we are, on last year's figures, running a very substantial current account surplus on balance of payments. I am very anxious to avoid, therefore, as I say, putting in orbit and endorsing the particular figure you mention.

1317. But you really basically agree with the CBI Conference rather than the CBI Council on the occasion when they last disagreed about the exchange rate?

(Sir Geoffrey Howe) In so far as one can make a judgement of that kind. The interesting thing is, when the CBI placed a paper before us in the National Economic Development Council in August - I am speaking now from memory, but I think they were saying that what we needed to achieve was an improvement in unit labour costs through lower pay settlements of 2 per cent a year, an improvement in the unit labour costs through higher productivity of 2 per cent a year, and an improvement in competitiveness through exchange rate changes of 4 per cent a year spread over three years. Now that represents their insight at that stage when the exchange rate was, I suppose, about 12 per cent higher than it is today. So it is another reason for not underwriting the statistical figure of 20 per cent with which you started your questioning.

1318. Yes, you also linked in oil, which I did not mention, and I do not know whether Sir Terence did. So you do assume, I take it, that there will be some further reduction in exchange rates as a result of falling oil prices?

(Sir Geoffrey Howe) I do not assume any such thing, no. I think the difficulty about making any such assumption is the difficulty in determining how far, if at all, any possible change

in oil prices may or may not have been discounted in advance. The possibility of a fall in the oil price is something that has been canvassed from at least twelve months back, I suppose, increasingly canvassed, and that is, must have been, one component of which the markets have been taking account. I do not think one should assume that, although I readily acknowledge that oil as a component in our economic structure is a feature which has an effect on exchange rate judgements.

1319. If oil prices fall, it presumably would have an adverse effect on the exchange rate but a beneficial effect on the economy as a whole. When oil prices went up we started on the current recession. It might be that if they went down the developed countries might gain some reverse advantage. But if that is not your view, what is your view?

(Sir Geoffrey Howe) We have moved on to a different question now.

1320. Not quite.

(Sir Geoffrey Howe) Well, we have, with respect, Mr English. You are now inviting me to give my view on the effect of oil price changes on the economy in a wider sense - and of course I will do that. On balance, plainly a lower oil price is good for our economy because it is likely to lower the rate of inflation world-wide and add to the rate of growth world-wide; but it must be said that a gradual or modest fall is more likely to be advantageous than a precipitate one, because any precipitate change is likely to have disruptive effects outside this country. It also has an effect on our exchange rate, of course, but as I have said already, the effect on the exchange rate may already have been anticipated. Perhaps that is enough for the moment. But let me add one other thing.

Also of course it does potentially affect our tax revenue, although that again may have been offset in whole or in part because the oil price is determined world-wide in dollars, and any change in the dollar/sterling exchange rate adds to the sterling revenue while no longer .....

1321. Tax is something we may want to discuss with you later in the year.

(Sir Geoffrey Howe) I mention it for the sake of completeness.

1322. You said it has been "anticipated" and you mean, presumably, not by the Bank of England. Obviously it was not anticipated by them when they lost something like one thousand million dollars in the course of two months in the last quarter of the calendar year.

(Sir Geoffrey Howe) That is a rather different concept, if I may say so. I am saying, to an extent, because no one can be certain because markets cannot be tracked even retrospectively with certainty, but to an extent changes in the oil price must have been one of the components underlying the changes in sterling exchange rates over recent months. The question of Bank of England dealing in intervention is a separate question, of course.

1323. You often explained to us that there is no published target rate for the exchange rate - and I know these details are decided at a lower level and I think part of the lower level is present amongst your officials - but one does wonder. When the pound was regarded as high, did the Bank make as much money as it lost out of the reserves in the last quarter of the last calendar year?

(Sir Geoffrey Howe) I do not have the figures with me, but certainly during the twelve months when the pound was rising very strongly there was a very substantial offsetting addition



to the reserves at least exceeding that which has taken place in the last six months. Is that right, Mr Peretz?

(Mr Peretz) Yes. Going back to the middle of 1979 there has been a nett addition to reserves. The underlying change in reserves amounts to a nett addition rather than a nett fall.

1324. In real terms?

(Mr Peretz) I mean in money terms.

1325. But why do we do this when we believe in a free market?

(Sir Geoffrey Howe) Because throughout the policy has consisted of intervention in conditions of market turbulence for the sake of smoothing, but not intervention designed to hold any particular rate. The point that has just been made - the fact that changes in the reserves on the way up and changes on the way down have netted off favourably to the addition rather than the reduction shows the consistency of that pattern. Of course it has fluctuated. There have been periods when intervention both ways has been on a larger scale than others. There have been times when there have been particularly sharp movements, actual or threatened, in the exchange markets.



1326. Is there not an inherent theoretical contradiction between trying to have a monetary target - I grant you have overshoot that and changed it twice and still overshoot it - and a free market on the exchange rate and trying to influence the exchange rate?

(Sir Geoffrey Howe) If that was in either respect what we were trying to do there would be an inherent contradiction but it is not what we are trying to do so there is not. We are not trying to influence the exchange rate in any policy sense, nor are we trying to have a free market, if by free market policy you mean a policy free of intervention. What we have had is a policy of intervention designed, as I have said before, to smooth and even-out potentially sharp changes in the exchange rate, taking account throughout of the exchange rate as one contributor of monetary policy. So that policy is not as you have described it. It is close to that described by Dr. Emminger, who has been before you, which is that the monetary policy is the primary objective but it is necessary and sensible to take account of the exchange rate as well, and to do it in the way I have described. If one looks at the other extreme of policy, the United States pretty well without exception has ruled out intervention of the kind which we have been embarking on except at very exceptional times. It is not our policy. Other countries, for example, Franco, have been much more active in an intervention policy designed to secure a particular rate. There is a difference as large as the difference between chalk and cheese between the scale of intervention over a short or long period involved in that policy and our own. The scale of intervention in a day or two days, if one is to hold a given exchange rate, can exceed the largest flow within a month, speaking roughly, at their height in our own policy. They are quite different policies and our policy has remained unchanged.

1327. When I quoted a paper written by Dr. Emminger in translation here I asked him if he still agreed with it in the light of what had happened in Britain and he said yes although when he said it he said he did not have you particularly in mind.

(Sir Geoffrey Howe) I am not sure what statement you were quoting to him nor what translation.

1328. We can soon find that.

(Sir Geoffrey Howe) We can swap quotations.

Mr. English: You are quoting Dr. Emminger, I have refrained from doing so actually.

Mr. Meacher

1329. Is it not the case, Chancellor, that the exchange rate has shifted over the last three years from 1.58, or thereabouts, up to 2.45 and then down to 1.54 or thereabouts? Would you not accept that this had very little to do with the underlying state of the economy and a great deal with other factors and represented a substantial degree of misalignment. What lessons does that tell you about the inadequacy of current policy for managing the exchange rate or not managing it as the case may be?

(Sir Geoffrey Howe) I think it is a characteristic of the volatility in exchange rate levels which has been one of the concerns of this Committee and of others. If one looks - of course there are comments to be made on these figures but I give the raw figures for what they are worth - the effective rate of sterling between November 1976 and January 1981, the peak, rose by 33.2 per cent., that is from November 1976, the bottom. The Deutsche Mark between the end of September 1975 and the end of September 1979 rose by 37.3 per cent. The dollar, 1978 fourth quarter to November 1982 rose by 36.2 per cent. and the yen, end of December 1975 to end of October 1978 rose by 61.3 per cent.. Now you will

find in here a series of downward steps in the yen effective rate since then - I will not bore you with them - which I think probably total almost as much as the 61.3 per cent. upward movement. You will remember Dr. Emminger discussing it with you, I think, that that depreciation in the effective rate of the yen was taking place notwithstanding the most vociferous protestations by those responsible for the Japanese economy it was the opposite to what they wanted. The point I am making is that these very large changes are de-stabilising, there are very good reasons for seeking to move towards a more stable pattern of international financial arrangements and a very good reason for us discussing them. Incidentally it should be noted that of the other currencies I have mentioned none of those had the additional impact of turning from being a currency of a country without oil to being a currency of a country with oil, which is an additional formidable factor to the reasons.

1330. Do you not agree that those movements in the sterling rate represent not just volatility but a substantial degree of misalignment, there being a clear difference between the two, particularly since it went up as far as it did and has now come right down?

(Sir Geoffrey Howe) What one can say is that if you want to study the alignment of a currency it consists of its alignment in relation to other currencies, all of which are changing their alignment, sometimes in the same direction, sometimes in different directions. What I am accepting is that during the period since the Bretton Woods arrangement there has been such a large movement of all the world's major currencies in both directions on such a scale that there must have been many moments when those

currencies were misaligned, although which one was misaligned in relation to what at any particular time is difficult to tell at any particular time.

1331. Is there not an argument, given what you have said, for trying to establish a target exchange rate even with a wide band somewhere around the vicinity of where it is at the present time? Might that not limit the extent of misalignment? I take account of what you have said as the first of four points in your introductory remarks, that you simply put emphasis on prudent monetary and fiscal policies in order to reduce exchange rate volatility. In the light of the experience of the last three years that is not enough and does one not need to look again at the possibility of establishing a target exchange rate, perhaps in co-operation with the other five countries.

(Sir Geoffrey Howe) You have moved to a slightly different ground which is as interesting and as important. I think the burden of our experience, the burden of the experiences of these other countries and the burden of the evidence you have had from Dr. Emminger and Dr. Eieke is that it would be very difficult to establish and maintain a target for the exchange rate and that has been the experience in this country at several different times since we became a floated currency. If we look at the experience in 1977 when it was intended to cap the rate, as you know at that time there was a substantial and sustained effort to achieve that and in the end it was not achieved. That is why the evidence you have had from both your German witnesses has been to emphasise that they do not have an exchange rate target, they have a money supply target range, as we do, and one of the conditions of which they take account in fulfilling that policy is the way in which the exchange rate is behaving. To move on to your second point, I readily

see that it would be preferable for people engaged in international trade to have more stable exchange rate alignments, just as it would be preferable to have more stable, less inflationary domestic currencies, and it is to that as an objective we ought to be applying ourselves, not, as you said just now, by seeking to uphold prudent monetary and fiscal policies but also a greater convergence to try and diminish the factors which lead to this volatility.

Dr. Emminger said if you actually sought to bring together the key currencies at this moment in order to try to hammer out between them here and now an arrangement for greater stability of exchange rates you would have little chance of achieving that, which is why my point at Versailles was to emphasise the objectives there set out and to pursue, so far as one can, the policy of having greater convergence between different policies of different countries. To fix or semi-fix exchange rates is not attainable but progress, pragmatically, towards less instability of exchange rates is desirable and, I hope, attainable over time.

1332. Can I move on to the question that Mr. English partly touched on. If the OPEC price were to slide as a result of a failure to agree on product quotas where do you anticipate it might settle?

(Sir Geoffrey Howe) I would not presume to offer a prediction of that kind.

1333. Can I help you then, inasmuch as Professor Friedman, for instance, has suggested it might settle at somewhere like 13 dollars and most people think that is a bit excessive. If it were to fall to something of the order of 20 to 25 dollars, which most people think could well happen, what would be the effects on the British economy?

(Sir Geoffrey Howe) I would rather not try, even hypothetically, to give any assessment, promise or forecast. One of the joys of being a professor as opposed to being a finance minister is that you may be free with your forecasts without having responsibility for then having an impact on the outside world; that is not true for all professors but most of them. Taking your question a little more broadly than that, as I said at the outset a fall in the oil price which was modest and gradual would be beneficial for reasons that I have given, but I think that a sharp and substantial fall, leaving aside the UK for the moment, would be likely to have such an impact on other countries it would operate significantly to the advantage of non-oil LDCs and indeed non-oil OECD countries, but on OPEC countries, particularly those that have been under significant pressure anyway, such as Mexico or Nigeria, it would have a very sharply disadvantageous effect. I think the question is whether the capacity of the economic system to respond to the greater growth potential of the countries that have been advantaged would be as fast as the necessity for the countries that have been disadvantaged to respond to the fall in their oil revenue. If there was an imbalance in that there would be I think a net minus component as far as the world economy is concerned. Britain would be standing, in that sense, relatively neutral as far as that scene was concerned, but one must say that any sharp and substantial and rapid change would be likely to have, at least, for a time, a disturbing effect on the pattern advanced by our own economic and fiscal structure. I cannot determine it or measure it because one would have to know a great deal of other unknowns.



1334. Given that the cost of producing a gallon of Saudi crude is about one dollar the possibilities of a collapse are considerable, would you not agree, particularly when there is, rather contrary to that, what you seemed to say at the beginning, so little possibility of a world economic recovery? Would you like to be more precise on the effect of interest rates and exchange rates as well as on tax revenues for the UK?

(Sir Geoffrey Howe) I would rather not offer precise answers to that because, as I say, so much depends upon what is happening in the rest of the world and what other assumptions one makes about the United Kingdom economy. I have given the qualitative point that a lower oil price would likely in itself lead to lower inflation world wide, likely in itself to improve output world wide, so long as it does not have this inbalancing effect between oil and non-oil countries, and is likely to have some effect on new pay and economic conditions both in relation to output and inflation. Quite how the mix would work out, I would have to know a great deal more, certainly it would be unwise for me to offer speculative conclusions before this Committee.

1335. Can I just, as a final question, ask you whether in this situation, with a very fluid oil price, you think there is a real risk that the recent depreciation could over-shoot?

(Sir Geoffrey Howe) I would hesitate to accept any conclusion because what we simply do not know, unless and until they happen, is how far these prospective changes may or may not have been already discounted and what other factors are planned. I do not think I can accept that proposition. I may leave it in your mouth but I would rather not accept it myself.

Mr. Wainwright

1336. We gained the impression in North America among many of the different authorities we consulted that in their view, not all of them, collective agreement amongst the countries of the major economies would be much more useful if it was more related to exchange rate management even at the expense of being less related to monetary targets. In that connection can I ask: are there technical objections to altering the monetary targets in consequence of what has happened to the exchange rate? Is it not possible to have an effective linkage between the two?

(Sir Geoffrey Howe) It is certainly possible and necessary in assessing what is desirable and what is happening so far as monetary policy is concerned to take account of exchange rate movements, and there one stands on common ground with your German witnesses. One must take account of them in determining the overall stance of monetary policy arrangements but to believe you can introduce a mechanic formula to achieve that is to deceive oneself. One remembers the Swiss experience in 1978 when, as far as I recollect, their monetary targets were for a time a sustained thing but in their case it did result in a monetary expansion which they regard as the cause of their subsequent inflation. So I think it is difficult in a world of floating rates to believe that one can sustain the need to focus on your monetary aggregates in themselves. One takes account of them, I do not think you can find the mechanistic formula.

1337. If we may stay with this question of the possibilities of effective collective agreement amongst the leading countries, your aim on this, as I think you expressed it in your opening statement, is collective agreement on sound economic policies. Would it not be very much more realistic and achievable to aim at a degree of

collective achievement of exchange rate policies rather than the very, very ambitious aim of trying to get democracies, subject to regular elections and so on and a lot of political considerations, to agree on something so vast as sound economic policies?

(Sir Geoffrey Howe) I think, if you look at the position of the United States at the present time, they certainly would stand apart from any attempt to focus on the agreements of exchange rates and if you look at the Germans, for the reasons given to you by Dr. Emminger and Dr. Rieke, they also would continue to attach a priority to monetary policy by attention to the exchange rate. Those are two solidly practical reasons for believing one would not find it easy to go down that road, on the other hand the attempt to secure a better balance of economic policies, although it sounds grandiloquent, and I see the point you are making, can be put in measurable terms and one can identify objectives in pursuit of which one could move. If I can take the scene as it has appeared over the last year or two there do appear to have been two contributory factors to the imbalance and structure of the world economy. One is the contrast between monetary and fiscal policy in the United States where I have said many times - and this is in no sense an original thought - that their fiscal policy has been too relaxed along side their monetary policy in pursuit of lower inflation and as long as that persists you are going to get high interest rates in the United States with the effect that has on exchange rates around the world. On the other hand, the same kind of position in obverse can be put forward on the Japanese economy where their monetary and fiscal policy has had the opposite effect. The authorities in both those countries - give or take - would accept both those propositions. If one was able to secure better convergence between those components then one

would move towards less volatility, more realistic, whatever that might mean, exchange rate relationships. So if it is hard to persuade democratic institutions in those countries to move in those directions I am not sure it would be any easier to do it in relation to their exchange rate policy. At the risk of scoring an own goal, which I will save in a moment if necessary, I mention the European Monetary System. I think it is a fact that that exchange rate mechanism has operated to some extent as a framework which has enabled member state governments to present their people with a necessity for policy decisions which would otherwise have been less obvious and less easy to take; they have not always been taken with complete success. So it depends which one you put first. Either way you are going to have to operate on democratic institutions to achieve the right balance of domestic policy.

Mr. Wainwright: Since you have put the ball in position very close to your goal may I ask you whether the trend of the pound in the last few weeks and indeed its present position vis-a-vis the EMS currency disposes you to look again - I do not ask any more than that - at the possibility of beginning to negotiate bringing sterling into the EMS?

Chairman

1338. Before you answer that, I see that you have a transcript in your hand. Did you see the very forthright comment that the Deputy Governor of the Bank of England made to us a week ago today on that subject?

(Sir Geoffrey Howe) My eyealights immediately on the comment made by the Chairman - I think unusually because you are very laconic in your comments, but you were moved to say: "It is a very, very important and clear answer."

1339. Yes, it was.

(Sir Geoffrey Howe) And I was going to echo almost precisely what the Deputy Governor said there. There clearly are attractions as envisaged in trying to find a framework which can contribute a greater degree of stability in respect of exchange rates, but if you judge that on its own, if you introduce other components of instability into your economic policy you are actually serving, however unwittingly, to de-stabilise the mechanism you are joining and the gain is not worth the price. Joining the exchange rate mechanism is not a policy, it is a decision to adhere to certain objectives which have certain consequential policy imperatives and those consequential policy imperatives may mean willingness to raise interest rates sharply to maintain your place in the system, as some countries have had to do, the willingness to move very sharply in relation to the public sector deficit or at very substantial cost to your reserves. In our case I think the component to which the Deputy Governor drew attention, namely the impact of petro-currency factors, about which your colleagues have been pressing me on the position of our currency, does make one still apprehensive about joining. I think Dr. Rieke said in the past, "Do us a favour by not being in it". That view is becoming less firm and I did not get the impression that even he became overwhelmingly enthusiastic. The experience I have seen of the exchange rate mechanism (having taken the chair of more than one re-alignment conference. does give one an insight into the framework of collective discipline) <sup>is such a thing</sup> can give it a price. I do not think the fact that the Deputy Governor sets out can be overlooked at this stage.

Dr. Bray

1340. People will read your opening statement very carefully to see in what respects you were adding to what you have previously said. I wonder if you could help them by pointing them in the right direction?

(Sir Geoffrey Howe) I have not emphasised it in that way because one's thought process is necessarily/unflattering and is a dramatic and developing business.

1341. There was one phrase that was new to me, perhaps you have used it before, the phrase, "the new Bretton Woods does not give the right signal."

(Sir Geoffrey Howe) Yes.

1342. You said that.

(Sir Geoffrey Howe) That is certainly a new phrase although I take credit it for it myself.

1343. You said that you felt that rather than look just for newness it gave too little attention to the cause of volatility in recent events and the directions to which remedies should be sought. You quoted some movements of exchange rates of a number of countries in reply to Mr. Meacher but you did not quote any movement of competitiveness which many people would feel to be of a greater impact on economies including, I think, yourself because it includes the vital factor of labour costs?

(Sir Geoffrey Howe) Yes.

1344. On relative unit labour cost, normalised, the IMF index between 1976-four and 1981 one, the normalised relative unit labour cost in the UK increased by 79.1 per cent.. Is there any country in the last five years which has suffered anything like a comparable shift in competitiveness?

(Sir Geoffrey Howe) You are taking 1976 four?

1345 To 1981 one, the trough to peak.

(Sir Geoffrey Howe) Taking, as you say, trough to peak I would think it is most improbable because no country - perhaps happily - is able to state a comparable experience alongside ours. The trough from which that starts is a trough fixed at a point when our economic conditions were such we had to begin putting in place a formidable IMF adjustment programme. By any standards it must be regarded as having gone further off the map than in retrospect seems to have been necessary, so one starts at a pre-IMF letter of intent low. You then move from that on through a period of adjustment set, over the next three years, by the IMF letter of intent accompanied by the excess of petro-currency status. In addition you find yourself, not for the first time in the United Kingdom, going through one of those periodic bouts of pay mania which affected us from the winter of 1978 on. ~~86~~ These powerful components are at work consecutively or in parallel. As I say I do not think any other country would have experienced such a unique combination of factors.

1346. Whatever the cause it was the most extreme incidence of volatility of competitiveness we have seen in the industrial world?

(Sir Geoffrey Howe) Yes, because it was taking place in the context of an extreme combination of circumstances.

1347. May I draw your attention to the fact that the trough was in fact no lower than the preceding trough in 1973 three, IMF Annual Report, chart 18, page 48?

(Sir Geoffrey Howe) If I can have a look. Yes, that is right, but even so the point is it is the trough and it was a trough preceding the putting in place of the IMF adjustment

programme. There is then the oil factor, the wage explosion; all three of which make their consecutive contribution.

1348. In terms of policy, again IMF report, page 3, it is said: "Among industrial countries by far the largest restrictive shift over the past two years, equivalent to more than  $3\frac{1}{2}$  per cent. of GNP, was that of the United Kingdom; no other shift exceeded 2 per cent. of GNP and some of the shifts ran in the opposite direction." In terms of policy adjustments therefore that again comes out as the most extreme of any industrial country.

(Sir Geoffrey Howe) But that again, if I may say so, starts from a condition which called for a substantial policy shift and if one looks at the comments made by such characters as the IMF Committee on such things there is no implication that it was an unjustifiable policy.



Indeed the whole burden of the analysis one is hearing from the Fund and from Monsieur Heroisier in particular has been the necessity for emphasising the need for a state of rest and one sees it very clearly in the United States.

1349. I will come back to the comment from the IMF later. Nevertheless you did say whatever the explanation about class behaviour that you think we do need to pay attention to the remedies of past volatilities. Among those remedies perhaps can be found some in the direction that you have pointed to where you said that some countries have to get the balance of their activities right but other countries, and you enumerated the various balances to which attention must be paid, may have scope for some expansion of demand. I think all the balances that you enumerated you would maintain that the UK was satisfactory upon. Are you therefore saying that there is some room along with that in other countries for expanding demand in the UK?

(Sir Geoffrey Howe) No. What I have said was: "In some countries where inflation has been brought down, where the budget deficit is under control and the external position strong, there may be scope for a rise in domestic activity to sustain the recovery." Indeed that is a rise which may in any event be taking place. If I may put it in a paraphrase, for those countries that are successfully pursuing a medium term policy for the reduction and control of their public sector deficits then in so far as that strategy is on a proper course and in so far as there is room for them to adjust in order to remain in line with that strategy, so be it, and in the autumn statement which we published in the autumn we indicated that by those standards there may be scope for fiscal adjustment of £1 million. That was the figure we discussed then. I am indicating the intellectual framework within which one is approaching it.

1350. Do we know that all the balances that you list, the three

balances, are all satisfied in the UK at the moment?

(Sir Geoffrey Howe) It depends how you define the external position. If you choose to make any judgment on the exchange rate there may be room for differences but if you choose to <sup>do so</sup> as far as the current account balance of payments is concerned, clearly that is right.

1351. So the UK may be one of those countries in which some expansion of demand would help?

(Sir Geoffrey Howe) There may be scope along the lines foreshadowed in my autumn statement which we shall have to consider when we know more about it.

Chairman

1352. Do we see the public expenditure white paper tomorrow?

(Sir Geoffrey Howe) Yes, you do.

Dr Bray

1353. Pursuing the same thought further, you later on emphasised the question of convergence. This was the phrase used at Versailles. By convergence do you mean everybody achieving zero inflation and zero current balances?

(Sir Geoffrey Howe) No, I would not begin to be as precise as that. It is of course a piece of Euro-speak I think in origin, economic convergence. By convergence, and this may sound like an Irishman's answer, I mean the opposite of massive divergence to begin with and it is clearly less easy to achieve the minor adjustment one wants if you have very widely divergent inflation rates, much more difficult to achieve it, but if you have very widely divergent fiscal and monetary policies, as I exemplified the Japanese and the United States with their push/pull effects on exchange rate relativities and interest rates and so on — what I am really

saying is one can certainly see ways in which the act could be put together better without focusing on a precise set of zeros to place alongside each other. In a theoretically ideal world zero inflation, universal zero movement of exchange rates might be right, but the probability is you cannot possibly establish, and it would not be right to establish, zero exchange rates because they will be moving to reflect differential rates in the economy, but zero exchange rates - I would not say hoorah for that.

1354. We are talking about the adjustment process, not just about the goals. As countries get their rates of inflation down and hopefully economic growth up, unemployment down and so forth, is it necessary for all countries in fact to follow the same path towards the goals and by convergence do you mean that they follow the same path or follow mutually consistent paths because just now you said exchange rates might need to adjust because of relative adjustments in the structure of different economies?

(Sir Geoffrey Howe) I am sure they would not follow the same path because they start from different places with different economic loads and opportunities of course. But it is clear that it is unnecessary divergence which gives rise to exchange rate volatility amongst other things. You are not going to eliminate the swings that take place in the balance of payments as countries from month to month and year to year change their trading position with one another, and those are bound to be reflected one way or another in their exchange rates and there are other things which the world did by and large do quite a lot to keep under control so long as the Bretton Wood system lasted.

1355. In this difficult business of financing therefore, would that practical process of adjustment of the whole lot of different national economies and positions, of different changes and so on,

be what one means by convergence in that situation, which would seem to be the kind of problem on which a certain amount of analysis might be useful as to what in fact one meant, as well as the ways of achieving it?

(Sir Geoffrey Howe) Yes, I think that is right, and that is one of the reasons why I attach importance to the developing by-products of the Versailles communique, if I may say so. There is the declaration of intent which is a step in the right direction. There is the so-called Jergenson Study of the value of intervention where I said in Toronto that at least it ought not to be machinery for justifying disagreement. It ought hopefully to be something that secures the coming together of views if possible, and the more one sees evidence of the United States being willing to contemplate convergence in other ways, then the more it is possible to see the United States accepting the role of intervention along the lines I have described. The third feature which can emerge I think from the Versailles agreement is a development of the role of the International Monetary Fund, what is called the surveillance role of policies in relation to exchange rate and other matters. It had a clear position during the Bretton Wood regime. It has not had such a clear foothold during the current circumstances and you may know that at the meeting of five financial Ministers last autumn we were assisted by the presence of the Managing Director of the Monetary Fund beginning to offer that kind of insight. I think a development along those lines may be one way of synthesising the dialogue between the five key currencies and if I may say so it is the kind of area in which I would very much welcome such advice and insight as this Committee feels able to give because it is very illustrative of the step by step way in which we have to move ourselves back to a less volatile system I think.

1356. Is it not rather disappointing that that meeting to which you refer is in fact the only practical step which seems to have been taken at all on this question of surveillance?

(Sir Geoffrey Howe) I think that I would certainly hope to see more developing from it but it must be remembered the Fund and the institutions, and indeed their officials, have been very very preoccupied in the months since Versailles with the international debt problem, but also if I may say with the moves we are now making for the enlargement of Probus (?) and so on.

I think one also has to recognise that there is a certain glacialism about the process of international treatment. If you meet every day you do not move more quickly than if you meet twice a year, but I am anxious to see some further headway along that road.

1357. Recognising the preoccupations of the IMF, is it not perhaps more natural to look on OECD as the framework within which economic co-operation might be developed because there is there the apparatus of Working Party 1 and Working Party 3 where the participants are used to talking about the interaction of their policies and they have the apparatus to do so? There is neither the tradition nor the apparatus in the IMF.

(Sir Geoffrey Howe) I would not want to give an exclusive answer to that at all. I agree with you that OECD is certainly a place where WP1 and WP3 provide that kind of dialogue. The G10 Group at the BIS is another forum in which countries co-operate together. So is the European Community another one. I think the one thing which emerged in the talks was that finance Ministers and central bank governors are less used to coming together for practical purposes than is the IMF and World Bank setting. The OECD has a ministerial conference only once a year. It does represent only its own membership and a great deal more of the work of the OECD is taking place

at official level. I think the more operational bodies in my judgment, and others may like to correct me on this, are the Fund and the Bank.

1356. Does not that bring out a weakness in the institutional balances here that on the one hand you have the decision makers ready to talk turkey in the IMF but without staff work and analyses to justify decisions and take them forward, and on the other you have the analyses in the OECD but disjointed from the decision makers?

(Sir Geoffrey Howe) Mr Odling-Smee may make a supplementary comment on this, but it is my impression that a very great deal of staff work and analyses do not take place within the Fund and at the Bank, but take place for severely practical operational reasons because the Fund is something that manages resource funds for two different purposes and has to make its judgment, and I do not want to award palms or cast aspersions but I would think that the practical insight coming from the Fund is at least as useful as that which we get from the regular reports and surveys of analyses in the OECD. The other feature is that the OECD is by definition representative of the industrial countries and it exists to serve the industrial countries. It may be the case that the five key currencies - indeed it is the case - are all members of OECD but it does not represent the developing countries or the OPEC countries and to that extent has to be seen more as representing an interest group in the world economy. One has the group of 24 and the group of 77 representing the old OECD and OPEC members so it is one of the reasons why one has not sought to advance discussion with the IMF quota and the increases we shall be discussing next week beyond a very modest point within the Group of 5 and the Group of 10 because it is not for us to decide. It is a debate we have to have with the OECD and the OPEC countries and I think there would be some risk of doing too much to consolidate a rich man's club as the OECD is seen as the

principal decision taking body but one has to take account of the old OECD and OPEC countries.

1359. That is a very encouraging view but it does seem contrary to the view you have previously mentioned of narrowing things down to the Group of 5. There are problems certainly which we <sup>would</sup> need to tackle, and I doubt whether the analytical apparatus in the IMF is adequate to service that. Going back 25 years, indeed research in the IMF did provide the basis of conditionality based on OECD and balance. There has been nothing comparable to that ever since and I think if you saw the people in the international division of the Federal Reserve Board in Washington as we did you would have seen a very different assessment of that in the IMF and the OECD.

(Sir Geoffrey Howe) I am not going to stick to that judgment because frankly I would not claim to have a sufficiently exhaustive familiarity to make a judgment. I am speaking institutionally. The reason for selecting the Group of 5 countries is because they are the countries whose currencies make up the special drawing right, who can therefore be seen in the context of the IMF to have a special responsibility within the framework of existing international financial institutions. In other words the reference we made to them at Versailles was, if I remember correctly, endorsed by the communique of the Interim Committee meeting in Toronto in September. I cannot remember but I am sure the spirit of it was not challenged by the developing countries. It is important in that sense.

1360. To sum up on the exchange rate, the general tenor of what you have been saying is that the exchange rate cannot be regarded as a separate policy instrument or objective from that of economic policy as a whole, but that economic co-operation between countries necessarily has to take account of the exchange rate within its ambit?

(Sir Geoffrey Howe) And indeed one has to take account of the exchange rate in one's judgment of monetary policy in one's own economy as well. I think that I go along with the general flavour of what Dr Rieke was saying about this. May I add one other point, and the Committee are familiar with it. I think it is worth drawing attention to it. The description by Dr Emminger in his earlier appearance about the movement of the pound sterling between 1979 and 1981. It is worth reminding the Committee that when he was asked about it again last October he did say that he did not think that very much could be done against that record change, that the reaction of the British economy was rather inflexible as concerns wage developments, and as I said in my earlier evidence, it started from the point where the pound "in its real rate went considerably down and it is mainly due to that that afterwards its upward movement was so exaggerated." In other words of course one has one's own judgment about the precise figure, but if you put it in the context of the huge movements about which I told the Committee earlier on and of the three factors to which I have drawn attention applying to the United Kingdom at that time, I think that puts it in a better perspective.

Chairman

1361. That was question 828?

(Sir Geoffrey Howe) That is right.

Dr Bray

1362. You have read the Morgan Guaranty World Financial Markets paper on the UK economy?

(Sir Geoffrey Howe) I read it in Riyadh some weeks ago. I could not claim instant familiarity with it.

1363. You will recall there that it has attributed much of the shift that you have referred to to the fact that the Government did in fact



ignore the need to pay attention to wage policy particularly in the public sector in the early days?

(Sir Geoffrey Howe) Well, if the cap fits, wear it, so to speak. Of course the one thing that I have never ceased to emphasise to this Committee, and this Committee has fortified, if I may say so, my hand formidably in presenting the case —

Chairman

1364. Totally.

(Sir Geoffrey Howe) — is the importance of achieving effective moderation and control of pay movements in the public and private sectors. I think we all start, as we go back over this ground, with the fact that this Parliament was elected with the great Professor Clegg already in situ with a large number of pay groups already referred to him in respect of which all parties came to this Parliament ready to accept his recommendations. I do not begin to deny — I do not think anybody in the House would deny — that the consequences of that had a very substantial impact on the rise in the public sector pay bill. I think Mr Higgins and you, Chairman, were the two protagonists who specifically drew attention to the cash consequences of that, which is where we came in.

1365. You may like to note that we went through this paper with Morgans fairly closely just about the moment of publication. It was set up before we had the chance to comment on it and I think we shall probably have some useful further material in due time. I am not sure that the Committee accepted everything that paper said. It has had a very great deal of publicity since.

(Sir Geoffrey Howe) I would hope not. I do not want to comment on it in detail. One does have to remember that these great independent organisations like Morgan Guaranty are less continuously preoccupied with the scene which they describe than we are. Sometimes the spectator sees more of the game; sometimes he does not.

Dr Bray

1366. Chancellor, we have seen an awful lot of the game.

(Sir Geoffrey Howe) I find myself playing in it very often.

1367. There are two elements of learning from experience as well as seeking the remedies for the future and if we do not have any experience we will not get the remedies right.

(Sir Geoffrey Howe) I would endorse that absolutely and the more common the lessons can be that are learned from this experience, and it is one of my main reasons for having welcomed from the outset the establishment of this Committee, then the greater will be our prospects of national advance.

Chairman

1368. Chancellor, just before we move on to the debt crisis may I put one thing to you which emerges from the earlier questioning. I think the impression this Committee, and I think probably already has, is that there has evolved over recent years a far greater degree of consultation in relation to these matters, the development of the economies of individual countries than ever before and a huge amount of work goes into it. It must occupy a very great deal of your time and those who advise you in the Treasury. But the discussions that take place are not the same thing as co-ordination and they are not the same thing by any means as leadership. Do you think that the lack of international co-ordination as there seems to be to many established regimes has contributed to the debts and the current recession, because many of us feel the answer to that question is yes?

(Sir Geoffrey Howe) I think one should hesitate to believe, and I do not mean to sound too sceptical now, that it is easy - not that it is easy - to put in place, have in place and mobilise a pattern of response to the events we have been through in the last

ten years, until you have to a significant extent been through it. If one traces the thing back, we had all come to live in a world in which the fixed exchange rate, Bretton Woods regime was part of our life, and one recollects, as I am sure you do, the exchange rate parity of the pound before and after Sir Stafford Cripps changed it, as readily as one recollects the price of a Mars Bar before the war. It was all part of the furniture of one's mind. All that disintegrated. I do not think that those - indeed I am sure that those - responsible for the management of the American economy visualised the impact on that system of the attempt to run the great society and the space programme, the Vietnam War, simultaneously, but it went on and there was the Smithsonian regime to replace it, and to use the awful jargon again, we are all in a new ball game and it is pretty difficult to believe that it was easy for new insight to develop very quickly. Had there been some geniuses around who could have cast some view on it quickly enough then maybe we would have began doing what we are now doing more quickly. The first OPEC oil shock was obviously the consequence of the collapse of the system, when the oil producers found themselves left out of the game, and before that one was truly through we had the second one upon us. I remember it happening on the day we were at the Tokyo Conference, so it would be nice to think that there was a stock of leadership around somewhere if only we could have mobilised it, but that is history, is it not?

1369. Yes.

(Sir Geoffrey Howe) I think the key thing now is that it is important for all of us to be addressing our minds to this and I think that is our view and I am doing the best I can.

1370. I think what you say is very fair and right and reasonable but we did recognise that we were in, to use that awful phrase again,

a new ball game when the Bretton Woods arrangements were made after the war, and perhaps we did recognise again that we were in a new ball game when this country of ours took a particular initiative and showed some leadership particularly in relation to the establishment of the SDR system. It is the view of many of us that we are in a new and very frightening and worrying ball game now and that is why we are so particularly interested in — speaking to you as Chairman of the Interim Committee why we are so delighted that the meeting has been brought forward. As you say, international events and international decisions tend to be made very slowly and I think many of us think it is very urgent that a number of decisions are made and as strong a view as possible should be taken of the scene. The reasons for that we are about to advance in the next section of our discussion.

(Sir Geoffrey Howe) May I make one point. I think that I would like to underline the point you make, about the one encouraging feature, that there is a great deal of consultation and common insight into these problems now. It is partly due to the I think increasing habit of co-operation which the European Community has in recent parishes built up amongst European Finance Ministers. It was not one of the objectives necessarily but it certainly has made an input into the world. It is almost certainly due to the impact of very disturbing flows like the problem countries we are going to discuss shortly. What one still sees pointed out is the difficulty of moving even from common intellectual insights into what needs to be done and the implementation in the countries that make up the world. If one visualises oneself as the Finance Minister of an oil producing LDC or a non oil producing LDC and one is suddenly smitten by these changes in position — take Mexico as an example; the problems of adjustment we talk about relatively glibly that are necessary to apply under IMF conditionality, are

formidable for a country of that kind, testing its institutions to the utmost, and the difficulty of adjustment in fact for countries like the United States or our own at different times have also been formidable so even if one had the ability to see what was necessary, there is at least as much a task of national leadership and international leadership for us to bear in mind because in a sense the burdens that this process of adjustment places on the LDCs are inescapable and they do have to adjust in conditions of great discomfort with huge changes being made in the pattern of poverty of their people and so on because they have not got the institutions we have in the industrial countries which cushion us against the consequences of those changes. If you like it is one reason why I do not apologise for having mentioned the role of the United States in my opening statement. It has an enormously powerful role to play. It is well placed by its history and prosperity to play it and if it is able to do so along the lines I have indicated it can give a contribution as substantial but different in quality as that made by the establishment of martial aid. It is that kind of leadership. We do not look to other countries. Instead we all have to play our part in doing it.

1371. I am sure that is entirely right. I do not think any member of the Committee, particularly after our visit to the United States - if they did not hold that view before they unanimously hold it now. What is so anxious from our point of view is that we do not just think that the world has been on the verge of<sup>a</sup> financial banking disaster. We think that is a situation which continues. That is why we are so anxious to talk about it.

(Sir Geoffrey Howe) Yes.

Mr Beaumont-Dark

1372. Chancellor, bearing in mind what you have just said, which I think we agree with, about the international debt situation, bearing in mind that some of the US banks have lent about nine times their capital to four countries and that the debt problem is not just in the undeveloped part of the world but Poland and Yugoslavia, and certainly every day we hear of one huge debt or another being rescheduled, I would be intrigued to know what you made of the Governor Elect of the Bank of England's comments that the world debt crisis was over? If ever there was one thing which struck me, that, along with Harold Wilson's, "The pound in your pocket" and Edward Heath's, "At a stroke", is one of the most bizarre statements I have heard recently.

(Sir Geoffrey Howe) I do not know the context in which the statement was made and I would not want to comment on that anyway. The only comment I would make is that the word "crisis" is one that naturally comes to the pens of commentators. I think it is a word which should not be overdone because it has always seemed to me to imply a point of time, as it were, when one can say there is the crunch and the crunch is over. I think the real point, and there was no doubt about this, is that the world is facing, as I said in my opening statement, a series of problems. That is why we are all taking the steps we are taking but it is still important to see them in perspective, and I think to put them in a crisis context suggests they come and go away quickly. They are things to which we have to address ourselves over a period of time.

1373. I suppose that is one explanation. Can I return to the point. You must think there is some kind of crisis because you used the words "Marshall Aid", that the Americans are the lynchpins in this whole thing. Yes, I agree with that. We found in America

they were making the point quite clearly that if America could not get a sustainable growth of 3 per cent. over the next few years the chance of debts being sensibly rescheduled in real money instead of just confetti was virtually nil. Surely it is not being alarmist to concentrate everybody's mind upon the fact that we have to get some growth going in this country and particularly in America if we are going to be able to feed to half the world?

(Sir Geoffrey Howe) I do not begin to quarrel with that at all. The whole burden of my opening statement was, here is a world which has been hit by major shocks now going through a difficult period of adjustment leading towards sustainable growth which, as I said in my statement, will be less fast than it has been in the more swinging patterns of the past, and certainly a world where there are very real difficulties and problems, where the problems of indebtedness certainly look like requiring continuous and constant and sustained attention.

1374. Is not the scary thing that this was the IDCs and that is one of the tragedies but some of the countries cannot be looked upon as the poor brethren really? We have Poland and Yugoslavia and we heard Denmark mentioned while we were abroad, and we have Mexico and Brazil, apart from the African problems, which I look upon as the real IDCs.

(Sir Geoffrey Howe) "Scary" is not the word I would apply to that, because it is a more broad-spread word that I would want to use. I think the fact that so many countries have got themselves into an over-extended position is certainly a cause for concern. That is why I keep on laying emphasis on the need for every country to go on re-adjusting its own economic policies to put it right, and the concern arises because they have all lived with a high and rising rate of inflation alongside generally high and rising public

sector deficits and, as I said in my statement, have been building apparent prosperity on the sand of inflation and indebtedness. To pull back from that is a formidable task. Fortunately, a number of the countries you referred to are able to do it and are doing it without adding to their international indebtedness; others in the intermediate category are a problem for the international debt market. I think broadly speaking - and I will be corrected if I am wrong - it is 300 billion South America, 200 billion LDCs and 80 billion Iron Curtain. I think that is roughly the order of magnitude between the three contributors to the indebtedness problem.

1375. The difficulty one can see is this. If you look back in history it is one of the interesting things to see what kind of growth has ever taken place. No real growth has ever taken place in a world where real interest rates have been more than 3 per cent. In this country they are a great deal more than 3 per cent. and in America they are something like 8 or 9 per cent. over the rate of inflation. How are we going to grow out of this problem, because in the end there are only two ways of growing out of this problem? One of them is by printing paper with no growth behind it and the other way is by growing out of it. How are we going to settle the scale of the difference between growth, which may mean some inflation, and squeezing the last drop of inflation out of the Western world, which may mean an even worse depression for everybody else?

(Sir Geoffrey Howe) Again before commenting on that may I make one other point. I have given you the total figures for indebtedness. If you put them in the context of growth and allow for inflation, then the increase in relation to exports and trade over the decade of the 1970s of the external debtor developing countries was about 25 per cent. In other words, although the



figures when they are suddenly called on to be delivered are daunting, they can be adjusted back to the manageable with less than might seem to be absolutely necessary, so that is how that would be dealt with. It is important to keep it in perspective. In answer to your question, the measurement of real interest rates is always a matter for arcane discussion by reference to what you determine the real interest rate should be measured against, and certainly one component is the expectation of markets of inflation as opposed to or in addition to the current perceived inflation rate. That is one of the features which may explain the anxieties which are reflected in today's high real interest rates. The other component, of course, is the uncertainty factor, so that you have interest rates giving you apparently very high real levels, and it is those two reasons, uncertainty about inflation and uncertainty about the world in which we live. I think it is, therefore, important that the success that we have had throughout the developed countries against inflation should not be jeopardised and should be fortified if we are actually to get the sustainable growth for which we are looking. If the balance of the United States dollar continues to lead those in market places in the United States to be fearful of the risk of renewed inflation and, therefore, of a renewed rise in interest rates, then indeed the prospect of recovery is at risk. If, on the other hand, that key component in the world economy can convince its market places that it has this deficit on a downward track, then I think you really do begin to see in place much more sustainable long-run expectations about low inflation in that country and much more sustainable prospects of low interest rates in that country. That is why I think one must make the choice, "Gosh, do we have to hang on with this pattern against inflation even at the cost of jeopardising world recovery? Let's

give it up and go for world recovery." One says how can we be sure we cement that success on a credible and sustainable basis in order to ensure that an incipient recovery is not nipped in the bud. That is my analysis.

1376. But is not the one problem there that low commodity prices mean less inflation for us and low commodity prices in the developing countries are often a disaster when we export 40 per cent. of what we make to those countries? How do you get out of this circle?

(Sir Geoffrey Howe) In any economy, national or worldwide, even in the case of an economy with zero inflation, you are bound to have cyclical movements in the price of commodities above and below the zero inflation level, and I have no doubt that a process of restoring world growth would remove some of the components that have been causing commodity prices to go on falling, not excluding oil, but again, provided it does not take the pattern of everyone deciding to inject demand all over the world so as to lead to a world take off in commodity prices, then it should be possible to move towards sustainable growth without building in the seeds of its own destruction. Sustainable growth means increased activity and increased revenue for the LDCs for their commodities; it means increased markets for ourselves but if it takes place, as I said, on a moderate and sustainable pattern that is the best basis for rebuilding and stability of the world economic system.

1377. One of the problems on the sovereign lending issue has been that it seems to have become the fashion so that many banks have got in on sovereign and international lending, which may well have caused some of the trouble we have, which may not have been easily manageable. Do you think that more of the sovereign lending in particular should be channelled through the central banks or the World Bank in what seems to an outsider to be rather a haphazard

system at the present time where we suddenly find that huge sums have been lent to people who then have to reschedule, which causes everybody trouble?

(Sir Geoffrey Howe) No, I would not subscribe to that, Mr Beaumont-Dark. I understand the instinct that prompted it but, as I said in my speech in Toronto (which is a very pompous thing to say, I am sorry, but I did) there really is not all that much evidence to justify the conclusion that central banking institutions and governments, either individually or in the aggregate, would be or should have been any better at making judgments, which is the essence of the market system, and what happens is that when we moved into a period of huge OPEC surpluses the cry went up, "These must be recycled," and as a matter of economic insight they had to be, and then when the recycling took place everybody said, "Look, they recycled, isn't that marvellous?" and there was another OPEC hike and a number of people who had not been on the bicycle, as it were, the first time round, less sophisticated maybe, got into the business and it so happens the market was being led by judgments which in retrospect went further than they ought to have done. Nobody was actually at that time saying, "Hoy, look, stop it, chaps." I do not think my confidence in the speed of the thought process of governmental institutions leads me to believe that we would have seen it any faster in the commodity system.

Mr Beaumont-Dark: I am very glad to hear it.

Mr Higgins

1378. Chancellor, I think you would agree that the level of world interest rates is important as far as the sovereign borrowers are concerned and it is funded to a large extent by the United States interest rates and in turn by the United States deficit. You used the platform of your opening statement effectively to

address the American Administration and the American Congress, saying we would like to see their deficit on a downward trend. I think we would all agree with that. It is certainly something much to be desired but in the light of our experience in Washington I feel bound to ask, do you think it is conceivable that the US deficit will be on a downward trend in the next three years as against more under control?

(Sir Geoffrey Howe) Having been to Washington less recently than you-- I have always been very hesitant to make forecasts even about my own economy, let alone anybody else's - I would rather not answer the question. The one thing that can be said by way of encouragement is that there is now an increasingly clear perception between the structural and the cyclical components of it, and, so far as I can judge, the decisions being proposed in relation to the social security part of their budget do seem to be addressing themselves to the kind of question that the Government Actuary in this country requires us to address ourselves to anyway; in other words, correcting the underlying structural imbalance. That seems to be an encouraging sign but we shall have to see.

1379. I think it is common ground in the light of your answer a moment or so ago that, in fact, most of the sovereign lending problem is not just a less developed country problem but it is a mixture of Fascists and Communists and in particular four countries, namely, Mexico, Brazil, Argentina and Poland. I think that would be common ground between us?

(Sir Geoffrey Howe) Yes.

1380. That being so, do you think the regulatory authorities, either in this country or the United States, have succeeded in preventing excessive lending to those four countries?

(Sir Geoffrey Howe) I am hesitant to believe again that you would have had a better system if central banks or an aggregation of central banks had been put in place to supervise that. They cannot really judge as effectively as the people who are engaged in doing it from time to time. I think that the whole experience has taught the banking system, including central banks, the importance of absolutely doing everything possible to ensure the availability of information. I think that the information already being made available to the Bank for International Settlements might now be supplemented, and I think the experience being gained by the International Monetary Fund and the BIS in relation to putting together these particular packages for these countries is also adding to people's insight, but I do not think one could conclude there had been any failure by central banks in relation to what had happened before the difficulties arose.

1381. But if we take it from that point of view, is there not some danger that while we are all anxious obviously to prevent a default or any major collapse and so on the effect of this kind of package is for the amount of lending to these particular countries to exceed that which is really justified and that a greater degree of regulation in that respect, both here and in the United States, ought, therefore, to be carried out? In short, ought we not perhaps in those four cases, leaving a very temporary upsurge in the immediate future on one side, to aim for their total indebtedness to be reduced, individually?

(Sir Geoffrey Howe) I think that is what is actually happening. It is a very interesting and important subject because what has happened has taken place in relation to each case ad-hoc, as it were. One started off with the Polish example. That was the first, where great political difficulties in any event overlay the

purely economic and banking question they had to consider there, and I suppose the Mexican was the first untainted by that. What has happened is that the international institutions and the banking system seem to me to have put together quite an effective working arrangement whereby (I am putting it very simply) the difficulties of the debtor country to meet its obligations have been met by rescheduling so as to stretch them into a more manageable pattern supplemented by additional lending, which is not as perverse as it seems. It is necessary to enable the rescheduled debt to be paid sensibly and, of course, accompanied by an adjustment programme put in place to meet the requirements of the International Monetary Fund, with varying parts being played by the Bank for International Settlements, central banks and the commercial banking system. I think that has served to put together the kind of relationships which in that case met the need you have in mind. It certainly worked as an example for subsequent cases and it has led some people to say, "Could we not, therefore, organise this more formally and design a more completely structured system of guarantees and inter-relationships," and so on. I would be reluctant to go too far down that particular road, although I can say there are further discussions still to take place because at some point one wants to avoid constructing what I heard called somewhere else an "international entitlement programme", to use the American jargon. If one creates a system too readily available it is the same reaction. One has to reschedule anyway but it should not be a matter of first resort but very much a matter of being done when it has to be done to facilitate the reconstruction process, but again I think I certainly would very much welcome the advice and the conclusions you and your colleagues may come to.

1382. Can I summarise your answer to see if I have understood it correctly. Are you saying that the individual total indebtedness of the Argentine, Mexico, Brazil and Poland is likely to decline?

(Sir Geoffrey Howe) That as as I understand it, yes, although not instantly.

1383. Over time?

(Sir Geoffrey Howe) That is where one has put in place the programmes I have described.

(Mr Littler) I think a lot of the problem here is the rate of increase and plainly a complete stoppage of the flow of funds would have precipitated all kinds of impossibilities. The continuation of them was obtained by desire and one tries to reach a point in the middle. It seems to us that the IMF can come and say, "If the world can get agreement on changes of policy and more attention is given to the level of information and flow of resources needed and we then have contact with the banking system to see whether that can be sustained, you can get some movement towards a more appropriate decision on the preferred draw-down of the rate of increase." But I do not think one should expect a total reversal. After all, these countries are fundamentally likely to be capital importers, which is their structure for long years to come, and irrespective of the likely problems overlaid on top of that. One does not have to think of going back to square one or zero balance. It is a question of getting the pace of change down to some sustainable level of capital.

1384. If they are already overborrowed should they not let it stay alongside in relation to other countries?

(Mr Littler) But as a first step, and I would have thought if you are going to try to smooth the process you would want to slow down the pace of that capital and that is the first step being

taken at the moment. We are dealing with one-year programmes in the sense that this is bound to have to be reviewed as the course of the economy develops and the IMF arrangements envisage periodic review and checking.

1385. Annually?

(Mr Littler) Or more often - six months.

1386. Could I go to the other side of that, namely, the bank's balance sheet. Would you agree, Chancellor, that if a debt is rolled over and the bank, instead of getting their money in six weeks then get it in six years and get the interest rolled over to the end of that period as well, their balance sheet ought to be adjusted to reflect the reduced present value?

(Sir Geoffrey Howe) I should have thought so. Do not, for heaven's sake, press me, as I am not an expert on bank accounting, but I should have thought it seems likely.

1387. Does the regulatory authority have an interest in bank accounting?

(Sir Geoffrey Howe) Yes.

1388. Should they not do what I have suggested?

(Sir Geoffrey Howe) I should have thought so but I am not the regulatory authority. The Bank of England is the regulatory authority in respect of that matter. I am sure you would have asked the Bank witnesses last week about that. In principle what you say is quite right.

(Mr Odling-Smee) In many cases of rescheduling there is no reduction of the original level.

1389. Is that not wrong? Would you not pay less for the second rather than the first? Would you not, any of you?

(Mr Littler) I think there are negotiations on what the rate of interest of the rescheduling should be and it can be the



case that the real worry is whether the money is going to be repaid at all if it is going to be paid according to the rescheduling. This may be a perfectly satisfactory business from the point of view of the bank.

1390. Provided the interest is paid in time?

(Mr Littler) Indeed.

(Sir Geoffrey Howe) There is in some ways a contradiction in terms. Here is a country, a company, a character - let us take a country - which has got into an unsustainable indebtedness position. How do you deal with that? You deal with that by applying yourself to the adjustment. How did it get into debt? Is it going to go on getting into debt, and you correct the policy to alter the flow so it is tracking back in the right direction and will come back in the right direction. Can it afford to pay the rescheduled debt or the interest on the rescheduled debt? Answer, no. So let us lend it some more. Does this collective operation alter the quality of the debt in the lending bank's accounts? Although by giving it more money to enable it to pay over a longer time the rescheduled debt you are improving your chances of getting your money back, you may still be justified in making a provision in the balance sheet to take account of the risk that you will never get it at all, and there is a curious set of parallel judgments being made, "This is the best I can do to give me a chance of getting it back but even so the chance of getting back the original money I put there has diminished by X per cent.," so one's instinct of what is going on, in answer to your question, is the same but it is different in different cases.

1391. If the bank originally lent in the expectation that it would be repaid, it would be appropriate if it failed to succeed in that and created the situation you described that the shareholders should pay the lot?

(Sir Geoffrey Howe) Again it would or it would not.

I am trying to think of the most recent case I have in mind.

1392. But if you had seen the examples put to us in America repeatedly that is so?

(Sir Geoffrey Howe) On the basis that the loss would certainly fall on them if there is a loss, subject to any provision you make in the balance sheet and subject to any tax provision you have to take into account.

(Mr Peretz) One point is that the bank does not know whether there is actually a loss until some time later and it may affect the judgment one year to write a particular loss down and in the next year it may decide conditions have changed and they can write it up in that year.

1393. It knows if it has actually rescheduled it and part of the interest?

(Mr Peretz) The next year it may feel happier about that particular thing.

1394. They may reschedule it back the other way?

(Mr Peretz) It is a question of the judgments the bank have to make as to whether that loan is going to be repaid or not. The act of rescheduling makes it more likely.

(Sir Geoffrey Howe) If I may take an example, the rate of repayment of our borrowing from the IMF was accelerated, so that if an example of rescheduling the other way.

Mr Higgins: That is surely a case for optimism.

Chairman

1395. Chancellor, unfortunately that is not an exact analogy with what we are talking about. We should put you in to run the Bank of Mexico or the Bank of Argentina.

(Sir Geoffrey Howe) If I could have some volunteers from the rest of your Committee!

Mr Browne

1396. Chancellor, you said that the banking situation was not exactly a crisis and we should get it into perspective. Obviously the world economy which you alluded to in your opening statement depends very critically upon the health of the international financial system and when you have the Prime Minister last Thursday replying to a question on this subject of lending money to Argentina, with her known views on Argentina, quite correctly, and sustaining these loans, which may be recycled in the form of the purchase of arms in other countries such as France, and she justified this by saying it was in the national interest and hinted that it was very important to uphold Argentina as a credible economy and maintain its liquidity in order to prevent what we all feel is a crisis; referring back to your answer to Mr Beaumont-Dark's original question, do you still not really feel that the present banking situation, which is always, we understand, a risky business, has reached enormous proportions? And when you say we ought to keep it in perspective and one hears that the top six international lending banks in the United States have lent nine times their capital to only four different countries, to us that seems to be an enormous crisis. Could I add one more thing on the background, that these same American banks have lent very heavily to the domestic oil businesses in the United States at a very high leverage at a price of \$43 a barrel and now the price has slipped down to \$20 a barrel. Surely we are in something more than just a worrying situation?

(Sir Geoffrey Howe) I am not expected to accept all the premises of your question because these may or may not be right. I

am not saying they are implausible. I still think that the word "crisis" is one which is much overused. If you visualise the kind of situation that could arise in relation to any one actual or potential debtor country that can clearly put either itself or itself and its creditors into a crisis situation, but I think that in a sense the word "crisis" applied to the present problems we are discussing implies almost a degree of immediacy between their impact and their solution. We are living through circumstances of continuous anxiety and danger and, as I said in my opening statement, against which we have to take as many steps as we possibly can to avoid the risks transforming themselves into something worse. If you think that is a crisis then I think the word "crisis" is actually misleading because it suggests an immediacy both of impact and solution.

1397. I must say on our trip to the United States most of the Members of the Committee came away with the feeling that there was a pretty immediate problem.

(Sir Geoffrey Howe) That there is an immediate problem I do not doubt. That is why we are meeting next week in Washington.

1398. And the dangers we were discussing, about the dangers of a cartel being formed of defaulters, what would this do not only to the loan portfolio in absolute terms, in money numbers, but what about the cash flows of the banks and what are the costs, for example, of the present rescheduling in terms of profit and loss account? If you had a moratorium or a cartel, a unilateral group of people getting together and saying, "We will not service our debt for the next three years," that would have a tremendous effect on the profit and loss account of these banks.

(Sir Geoffrey Howe) Of course, it is possible - and I do not mean to be disrespectful - contemplating the scene to see so many things that could go wrong and you can frighten yourself into immobility. That is not what we want to happen, nor is it my job. One has to make the best judgment one can and take the steps as necessary and as expeditiously as possible, which involves dealing with individual countries, learning from that experience how we can improve the mechanism and making such changes as are deemed to be necessary in the international institutions. As I said, that is something to which we need to apply ourselves urgently and diligently, and so we are. There is no disagreement about the nature of what has to be done.

1399. I quite understand and support the view of the international institutions such as the IMF and the World Bank and so on getting people together to improve the flow of information to co-ordinate this whole system. I think the Members of this Committee would heartily support that but it does beg one question and that is what we were told in Washington by the IMF in terms of what one might call salvage lending, that those people who were already in would "ante up" for the salvage their pro-rata quota of the outstanding debt. What legal implications does this have vis-a-vis the shareholders if, in trying to lend further to these countries, they have a salvage operation and if such a salvage operation went wrong would the international institutions be liable to shareholders' suits on those domestic banks in international law?

(Sir Geoffrey Howe) I would hesitate to answer that question of law because I have learned to be prudent in that respect, but the intention certainly is no, there should be no such liability. What is actually happening is constructive

co-operation between the International Monetary Fund playing its part and the banks alongside it making their own judgment of their collective or individual interests, because they are, after all, concerned to secure the money they have already lent and secure the prospect of its being repaid and they may, therefore, be extending their facilities in order to secure that. But there is not, I think, any concept of underwriting or guaranteeing that. Nor do I think it would be prudent to organise such a system because if one were to go as far as to centralise a risk in an underwriting form, then one actually diminishes the element of judgment required from the constituent banks and their last debt is worse than their first.

1400. In light of the impending bank crisis, or let us call it a situation, this Government levied a roughly £100 million wind-fall retrospective profits tax on clearing banks. I know that British banks are actually in a far better position than most of the OECD banks, but if push came to shove and there was a problem would you take into account the fact that the Government had taken some £400 million out of the clearing bank capital before alleviating the problems in terms of the bail-out?

(Sir Geoffrey Howe) I think that is a hypothetical question founded upon a debate on which the House came to a conclusion some years ago.

Chairman

1401. In other words, you mean no, Chancellor?

(Sir Geoffrey Howe) I was trying to be more courteous than that!

Mr Browne

1402. If the taxpayer was forced to bail out; first of all, in terms of a bail-out, I would not dream of asking you what your level would be because it would be wrong to disclose that, but are you

looking to include British banks or what about British branches of foreign banks? Would they be included in a salvage basket in London or would you look to the foreign parent?

(Sir Geoffrey Howe) Again I do not know what kind of question you are considering because you are moving into new territory and a new salvage arrangement of the UK banking system which I had not been contemplating here.

(Mr Littler) It is worth recalling there were agreements between central banks going back to 1973/74 and repeated since on how they might handle the responsibility for international banking syndicates of various kinds, not totally complete arrangements, not published in detail because in a sense one does not want everybody to know totally where they are, but there is that framework for discussion and it has touched on this subject.

(Sir Geoffrey Howe) I think if you are concerned about the completeness and effectiveness of the international machinery for bank supervision, then that is a very legitimate subject for inquiry and it is important that each nation should have its own supervisory system in place and that there should be as effective as possible a system for dealing with overlapping and interlocking arrangements. That is one thing to which the Bank for International Settlements in particular applied its mind in 1974 and 1980, where we have always been considering in the European Community where informal discussions, as Mr Littler has said, have existed, where there are some further legislative changes of a modest kind that need to be made in certain countries. But this is certainly something which I think has to be regarded as important and is very seriously in mind and I think they are largely dealt with. I hesitate to say more than that. You are quite right to draw attention to it.

1403. On the subject of the use of proceeds and the problem a lot of people have in seeing British banks lending to Argentina and the money going to France in terms of jobs and weapons, etc., and bearing in mind the fact that you said you do not want an entitlement system, nonetheless do you not feel it would be wise, and if not why not, for the IMF to operate some type of quota system for LDC lending and investment, and if any bank lent outside the quota it would do so at its own risk without the central bank as lender of last resort? Such a facility would be very powerful because you could dictate the use of the proceeds. A lot of these countries have spent huge amounts of their loans on armaments and prestige projects and, as the Chairman has illustrated, there has been some feeling of a lack of leadership and co-ordination in terms of international lending and people have been jumping over each other to lend and have not looked too closely either at the credit or the use of proceeds?

(Sir Geoffrey Howe) You are talking about commercial banks?

1404. Yes?

(Sir Geoffrey Howe) The rights of Member States to take advantage of their facilities with the IMF are determined by the Articles and are related intrinsically to their quotas in any event. If one is looking beyond that for the IMF or some institution to make a kind of global value judgment on the maximum permitted indebtedness of any sovereign risk borrower, I would again hesitate to put such a situation in place, partly because I am not at all sure the judgment would be found to be more reliable than the judgment of the market place and also because if the IMF is, as it were, taking unto itself the responsibility for determining the maximum safe borrowing to be undertaken by Country A or Country B, it is coming very close to saying, "In so far as we have endorsed that judgment we will accept responsibility for everything up to



that limit." So it is coming perilously close to a nearly universal guarantee system and I am hesitant to put that in place. Once we erode to that extent the role of judgment by the commercial banking system, then we may run other risks. I am reminded of Spencer (I think it was and I used to quote this in my Consumer Affairs days) who said, "If you seek to create a system in which everybody is protected from the consequences of his own folly, you end up with a world peopled entirely by fools," and that is as true of the banking system as of consumer protection, so there must be a limit to the involvement of central authority.

1405. Could I ask one final question on the subject of liquidity. Obviously since the American freeze of Iranian assets a lot of major depositor nations are worried about the freezing of assets. Is there not a way of getting more liquidity into the IMF even on a "loans to the IMF" basis as opposed to a paid-up quota system, by encouraging big depositor nations to deposit money in the IMF in return for the security that it would, therefore, offer from the point of view of the freezing of assets by any one nation?

(Sir Geoffrey Howe) That is not, of course, something that has happened at all frequently, so I have not heard the proposition discussed in that context. The Fund does not depend wholly on quotas for its resources. The arrangements are well-known with the Saudi-Arabian Monetary Authority, as one example, and the Fund has also been given less than enthusiastic authority by the Interim Committee, by the Board, to engage in market borrowing as well, if necessary, so it does have facilities open to it but I do not think it has thought of tailoring its use of those facilities to provide the kind of insurance policy you have in mind.

Mr Howell

1406. Several of my colleagues have talked about increasing competitiveness or more growth and I wonder whether we ought to pay more attention to cutting back Government expenditure? Both we and the group of five nations, as well as other countries, have been talking about our irresponsibility in going on employing more people than we ought to be employing and overmanning in the public sector. Also should we consider ways of getting our social security budgets under control? We found when we were in Washington this was one subject which most people were very reluctant to talk about and it occurs to me this is something which we have not talked about much here today.

(Sir Geoffrey Howe) No, I agree with you. I think you will find that in virtually every communique of all the international organisations there has been a loud if not specific echo of what is known as "Howellism". Everyone endorses the need to control the growth of the public sector deficit and in that context how to keep public spending under control, and it is a thoroughly penetrating insight. If you look at the countries of Europe, all the countries that have come to the Fund are all coming there because, in fact, their budgets have run out of control. For why? Because they are spending more of public revenue than they are getting in revenue from the taxes and they have run out of the road of borrowing. So, your point is absolutely central to the problem. It is central to the problem of running a democratic system of government and it is extraordinary how widespread the democratic bank is, even in countries one hesitates to recognise as democracies from this distance but which have moments of electoral excitement which have some impact on the nature of the government. It is preceding these moments of electoral excitement that the deficits begin to expand and the debtors begin to appear.

Dr Bray

1407. Chancellor, if all goes well at the Interim Committee, which we sincerely hope, do you think the increase of the IMF quota and a fall in the expansion of the general agreement to zero will, in fact, be sufficient to unlock the flow of private bank funds?

(Sir Geoffrey Howe) That is the judgment that we make and, of course, we do not know how much the proposed increase will be yet, but it is intended to be sufficient to put the system on a reasonably even keel. It must be said, of course, that it does not come into effect forthwith. That is one of the reasons we were anxious to get the GAB brought forward as a group exercise. We have said in Paris the other day that we hope the quota increase can take effect by the end of this calendar year.

1408. It is only 10 billion a year, assuming it is spread over three years, is it not?

(Sir Geoffrey Howe) I do not yet know what it is going to be but of that order.

1409. In the third quarter of 1982, which is the last for which data are available, the total lending by developed countries' banks to developing countries actually fell. That is on the latest information. Even the roll-over is incomplete. Are there really any grounds for your optimism about unlocking the flow of private credit?

(Sir Geoffrey Howe) What one has to bear in mind is whether the Fund itself is going to have sufficient resources to play its part in arranging its own programmes.

1410. Does it not call for supporting measures to hold the problem with the promise of a further issue of SDRs in a year or so?

(Sir Geoffrey Howe) That is a separate but important question because the possibility of a further issue of SDRs is

certainly something we shall have to be considering.

1411. And you will be moving on to consider these questions at the Interim Committee?

(Sir Geoffrey Howe) At this meeting of the Interim Committee there will certainly be some discussion of that because one of the reasons it comes onto the agenda arises from any decision as to how the increased quotas shall be met and if these increased quotas are to be met, either from the hard currencies or SDRs, then the question arises: have all the Member States got access to sufficient of those things to meet their obligation. So the SDR, the question which has been more or less in suspended animation at recent meetings of the Interim Committee, will become more urgent and more relevant but I do not imagine or expect we shall be deciding it next week.

1412. Will you be opening up the question of debt re-organisation for the longer term?

(Sir Geoffrey Howe) Again not next week. Frankly, we shall have all our time cut out to secure the agreement on the size of the quota increase and the distribution of the quota increase, and to make sufficient headway on the SDR, I hope to make that a live issue at the annual meeting in September.

1413. But you agree there is an awful lot that remains on the agenda if the problems of developing countries are to be considered?

(Sir Geoffrey Howe) Indeed, yes, that is why I have been anxious to hasten the process.

Chairman: Chancellor, thank you very much. The Committee also wishes you success in your meeting early in February of the Interim Committee. The Committee is actually likely to report to the House on the subject of sovereign lending before we come to a general conclusion about

international financial arrangements, so that your invitation to advise, if it is possible, is certainly accepted. Thank you very much for being with us today.

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Changing the Public-Private Mix: A Survey  
of Some Recent Experiences in LDCs

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	<u>Contents</u>	<u>Page</u>
I.	Introduction	1
II.	Ambiguities in the Public-Private Sector Dichotomy	2
III.	The Sources of New Interest in Privatization	3
IV.	Divestiture	7
V.	Private Provision of Services	17
	1. Education	17
	2. Health	17
	3. Marketing	18
	4. Drainage and salinity control	19
	5. Agricultural extension	20
	6. Transportation	22
VI.	Government Contracting of Services	25
	1. Private road construction	30
	2. Road maintenance: an example of contracting	32
VII.	Conclusions	35
	References	38
 Tables		
	1. Public Enterprises in Chile	8
	2. United States: Number of Cities Using Private Firms to Supply Municipal Services Under Contract	28

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\*This paper was prepared while the author was a consultant in the Fiscal Affairs Department of the Fund. The views in the paper are solely those of the author and do not necessarily reflect the views of the Fund.





## I. Introduction

The private sector is the focus of new attention in industrial as well as developing countries and in centrally planned as well as market economies. Advocates of a larger scope for the private sector claim that greater reliance on nongovernmental economic agents and broader appeal to private incentives can lead to better utilization of resources, faster economic growth, and increased economic welfare. For the poorest and least developed countries in particular, many recent analyses stress the need to mobilize individual energy, skill, and savings more effectively if present trends toward economic stagnation or decline are to be reversed. <sup>1/</sup>

Although "privatization"—defined as a greater role for the private sector—in developing countries, is being widely discussed, it is not clear how much of it is taking place. What is actually being done, especially in the developing countries, to alter the public-private economic mix? The question is not an easy one to answer, and relevant data are not readily available. Nevertheless, research for this study has uncovered some informative experiences, which are described in this paper.

Section I discusses the distinction between public and private sectors. Section II surveys some of the main factors that have led to the worldwide surge of interest in an enlarged role in the economy for the private sector. Section III analyzes experiences with respect to three of the main instruments of privatization: (1) "divestiture"—selling (or closing down) state-owned enterprises; (2) allowing private sector agents to provide services either in place of or in competition with the government; and (3) government contracting of service delivery to private firms. Many other instruments are available to increase private sector involvement in the economy, such as macroeconomic policy changes—for example, allocating more foreign exchange to private sector agents, improvements in the general investment climate through changes in law and practice (incentive legislation, labor regulations, etc.), deregulation, and imposition of more and/or higher fees for the use of government services. But for lack of space and information, these are not discussed here.

Divestiture was selected for study because it is highly attractive to economic reformers concerned with increasing the efficiency of resource use in the public sector. Nevertheless, despite its appeal, divestiture is not a common phenomenon, nor is it likely to become common very soon. On the other hand, deregulation, which allows private agents to compete with state monopolies, and government contracting of the delivery or "production" of services have clear potential. These

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<sup>1/</sup> Cf. World Bank (1981) and CILSS/Club du Sahel (1980).



measures can generate substantial new resources, significantly raise the general efficiency of resource use, improve services, and bring about faster economic growth. Of course, they are not foolproof. They entail problems of their own and may involve some new or different risks. But experience indicates that because of their inherent advantages and their promise, they merit serious consideration by governments and international agencies concerned with economic development.

## II. Ambiguities in the Public-Private Sector Dichotomy

Usually, "private" and "public" sectors are referred to as though they are well-defined entities with an unambiguous frontier between them. The "privatization" process is then conceived of as a shifting of the frontier in favor of the private sector. But this is not entirely accurate. Most activities in the real world are, in fact, public-private blends. Therefore, it is more appropriate to see privatization as a process that alters the blend, with the public sector playing a different role and the private sector a larger role.

All organized activity has many dimensions: conception, determination of scale and technology, financing, management of production (of goods), or delivery (of services). Economic activities commonly described as "public" or "private" are rarely entirely one or the other. This is obvious in such a common case as that of publicly financed manufacturing enterprises that are managed by private agents. Education and health care activities are also frequently financed by tax revenues but "produced" or provided by individuals and nongovernmental organizations. <sup>1/</sup>

Not only is the notion of a strict separation of public and private activity rendered ambiguous by distinguishing between dimensions such as financing and management or production, but even within each of these elements, 100 per cent "publicness" or "privateness" is extremely rare. Thus, a "private" enterprise often enjoys fiscal privileges—subsidized credit, tax rebates on imports, tax holidays on profits, etc.—that blur the concept of private financing. This same "private" enterprise may depend on government-determined tariffs or quotas for protection of its market and its earnings, on government wage leadership to determine its wage policies, and on government price controls to determine the prices of its outputs. This is "private" management, but under such pervasive public constraints or incentives that its "privateness" is reduced.

The complexity of public-private blends is even more evident in the case of loan guarantees. As is seen below, substantial "private" financing is being made available in Argentina for the purpose of road construction but with revenue guarantees provided by the Government. The

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<sup>1/</sup> A similar distinction between "arranging" services and "producing" or "delivering" them is made in Savas (1981).



extent to which this kind of transaction is public or private depends on whether those guarantees have to be activated, which in turn depends on future traffic flows, exchange rate changes, and rates of domestic inflation, among other unknowns.

If the distinction between public and private activity is hazy in these cases, it is even more so in the area of public sector contracting to private agencies. At issue here is an extremely large set of activities. In the U.S. Government, for example, more people are employed by the Government as contractors than as direct employees--and in some sectors, vastly more. <sup>1/</sup> Contracting for public services, such as garbage collection, road maintenance, even fire protection, is widespread, as can be seen in Table 2 and Section VI.

All of this illustrates why the image of a public-private blend with altered inputs is more apt than that of a shifting distinction. When governments contract activities, they do less direct management or production but more contract preparation, specification of performance criteria, and monitoring. The public sector is not removed from the activity; only its role is altered.

### III. The Sources of New Interest in Privatization

The interest in privatization is part of a newly intense and very general preoccupation with the effectiveness and efficiency of resource use; governments everywhere are searching for ways to mobilize new resources and to use better those they now have. These new concerns are not difficult to explain.

First of all, public sectors have grown extraordinarily fast in recent years. During the 1970s, the share of government expenditures in gross domestic product (GDP) grew by 2-3 per cent a year in many countries. Whereas in 1972 only 13 central governments (of those listed in the Fund's Government Finance Statistics Yearbook) were spending one third or more of GDP, by the late 1970s the number had tripled--to 38 out of 90 countries. In the developing countries, especially the least developed that have relatively large subsistence sectors, the public sector role is even larger when only the monetized part of the economy is considered.

One form that public sector expansion took, especially in the developing countries, was the growth of parastatal organizations--public or state-owned enterprises. Numbers are hard to come by, and generalizations tenuous; the pattern of state-owned enterprise growth

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<sup>1/</sup> Cf. Ira Sharkansky (1980), p. 117. In recent years the U.S. Department of Health, Education, and Welfare had 750,000 people working under contract, and only 157,000 as direct hire employees. See Hanrahan (1977), p. 217, and Savas (1981).



is geographically uneven. But in most developing countries for which data are available, substantial growth took place. 1/

The performance of a public enterprise is difficult to measure, and great differences exist in performance between countries and sectors. Existing information can support few firm generalizations, but it is widely asserted that, in most of the developing countries, the performance of state-owned enterprises has been "disappointing." 2/ Conceived to be leaders in modernization, adopters of new technology, and generators of public savings for investment and growth, public enterprises in the developing countries have more often than not been plagued by management deficiencies, political pressures to sustain employment and low prices, and unclear—often contradictory—policy signals from government. As a result, efficiency has been low (in the sense of minimizing input use to produce given outputs). 3/

Jones and Mason 4/ give the following reasons for "inefficiency," defined not in terms of traditional allocative criteria (choice of the wrong price/quantity bundle) but in terms of a failure to minimize costs of production for quantities of output actually chosen:

(1) Public enterprises work under bureaucratic systems that usually control processes, rather than outcomes. "The time-consuming traditional rules of government (procurement procedures, for example) are difficult to reconcile with the needs of an organization that must operate in a dynamic market place."

(2) Political influence is often used to transfer income to special interest groups, but usually not openly.

(3) Public enterprise decision makers lack incentives to control costs. One of the important reasons for this is the fact that it is difficult to distinguish between good from bad managerial performance, since there are legitimate and illegitimate reasons for losing money. Jones and Mason observe that there are no necessary reasons for public

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1/ For example, the share of state-owned enterprises in gross fixed capital formation grew between the late 1960s and late 1970s from 20 per cent to 59 per cent in Algeria, 27 per cent to 36 per cent in Taiwan, 17 per cent to 30 per cent in Turkey, 11 per cent to 23 per cent in Peru, 14 per cent to 23 per cent in Brazil, 17 per cent to 24 per cent in Kenya, and 15 per cent to 24 per cent in Ivory Coast. See Peter Short (1983).

2/ This is not only applicable to developing countries as the U.K. experience suggests. See Pryke (1981, 1982).

3/ John Sheahan (1981) stresses the need to define efficiency carefully, since market failures, imperfections, and noneconomic factors are important in explaining the origin and functioning of public enterprises.

4/ Jones and Mason (1982).





enterprises to fail to minimize costs (although there are many sufficient reasons) and that the costs of public enterprises must be compared with the costs of alternatives.

Thus, instead of contributing to public saving, the state-owned enterprises have frequently turned out to be drains on the budget and burdens on consumers of their outputs. A recent survey of the role of public enterprises in developing countries provides the following typical conclusion about performance:

Most studies have evaluated performance on the basis of financial rather than social profitability. Based on this criterion, many (but not all) countries operate public enterprises that show low profitability or large and mostly continuing financial losses. The losses are mostly due to: (i) inadequate planning and poor feasibility studies resulting in ill-conceived investments; (ii) lack of skilled managers and administrators; (iii) centralized decision-making; (iv) state intervention in the day-to-day operations of the firm; (v) unclear multiple objectives; and (vi) political patronage. 1/

Discontent with inefficiency in public enterprise operations is one factor that has pushed the idea of privatization forward. While governments have mainly concentrated on improving the performance of these enterprises, in a great many cases they also have begun to look at other ways to deal with the least profitable and most troublesome enterprises.

The rapid growth of central government activities, like those of state-owned enterprises, in the past decade coupled with slower economic growth and consequent fiscal pressures, is another major factor explaining the interest in privatization. In the industrial countries, much of the growth in government spending in the 1970s came in the area of "entitlement" programs, but the spending on these programs has everywhere been difficult to contain. Higher costs could be financed until the early 1970s without too much difficulty, since GDP and tax revenues were growing rapidly. But since then, slower economic growth and strong resistance to heavier tax burdens has forced reconsideration of the scope and financing of these programs.

In most developing countries the problem has arisen in a different form. In many of these countries, a substantial share of government expenditure is being devoted to education, health, and other activities related to the meeting of basic needs; it is not uncommon to find education claiming one fourth or more of recurrent expenditure in low-income countries. Yet access remains limited. In sub-Saharan Africa, for

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1/ Choksi (1979), p. iv.



example, one third of all children of primary school age are not in school, few people have access to modern health facilities, and only 25 per cent of the people have access to clean water. At the same time, severe constraints exist on the raising of more revenue by taxation. Economic growth has slowed down--especially in the lowest-income oil importing countries--and prospects for the next decade are poor. Also, in the low-income countries, farms and mines are virtually the only sources of tax revenues. Farmers, however, are already heavily taxed through price policies and export taxes, and international price projections for most primary goods are not particularly good, at least for the next few years. This leaves little hope for revenue buoyancy in the near future and demands closer attention to the incentive effects of price and tax policies.

These are some of the immediate problems from which the present interest in privatization derives. Political-ideological elements are, of course, strongly present in some cases, but for the most part the recent burst of interest in mobilizing private resources has its origin in pragmatic concerns. These include methods for modifying institutions and approaches that have proved to be inadequate, mobilizing individual energies now unused or misused, in order to bolster sagging economic growth rates, and providing more and better public services in the face of tight resource constraints. Privatization thus has relevance in all kinds of political systems and can be a vital component in any development strategy, whatever its ideological foundations.

The broad appeal of the idea of privatization is seen in recent moves in some of the centrally planned economies. In January 1982, for example, the Hungarian Government opened the legal door to the formation of private corporate enterprises employing up to 150 people. To be sure, the new law stipulates that these enterprises must have some features of a cooperative, but it would be surprising if most of them did not take on many characteristics of private companies as known in capitalist systems. In any case, they are to be allowed to compete against state enterprises. According to a press report, the new policy "is partly an attempt to force moonlighting workers, who account for nearly one fourth of all the hours worked in Hungary, to come out in the open . . .". A Hungarian academic calls it ". . . a change that legitimizes private enterprise on a historic scale for the socialist countries..." <sup>1/</sup>

Similar changes are under way in China. In November 1981 the Chinese Government openly dropped its previous policy of assuring state jobs to everyone, reputedly because of the negative impact of this practice on incentives and hence on productivity and because too many people are coming into the labor force to make continuation of the policy viable. The Government officially told people to "get organized on a

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<sup>1/</sup> New York Times (December 3, 1981), p. D-5.



voluntary basis and find work for themselves." 1/ As in Hungary, private corporations are now legal.

Privatization, in the sense of greater scope for private activity, is clearly a potentially useful approach for governments of all ideological persuasions. Three specific aspects of this approach are discussed in this paper: selling (or closing down) state-owned enterprises; allowing the private sector to provide services either in place of or in competition with government; and government contracting of service delivery to private firms. The relevance of each of these of course, varies between countries, but the experiences surveyed below suggest that the most promising approaches for most countries are deregulation and government contracting of services. Policies that allow an expanded private role in service delivery can generate substantial new resources, significantly raise productivity of resource use in general, improve services, and bring about faster economic growth.

#### IV. Divestiture

According to Webster's dictionary, the strictest definition of "divest" is "rid"--and this is indeed the pure, hard definition of divestiture--ridding the public sector of its enterprises by selling them or shutting them down. Divestiture in this sense is not altogether without ambiguity; it can mean simply a sale of government equity in a corporation whose shares are mainly privately held, or a transfer of assets and employees from a state-owned enterprise to a government ministry. Not much is being "divested" in these transactions.

In any event, divestiture in this sense is for many people what privatization means. It is also a chosen instrument of economic reformers and stabilizers. It is rather surprising therefore to discover how few examples of divestiture can be found. This conclusion is based on a fairly systematic look at the experience of 22 countries where there are a priori reasons for expecting some divestiture to have occurred. Eleven of these countries have experienced ideological or political turnarounds in the 1970s, with a smaller role for the public sector as one of the objectives. 2/ Eleven others are what can be called "onestep-back" countries, where the desirability of retrenching the

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1/ The press report from which this comes continues as follows: "After three years of quietly promoting private enterprise, Peking suddenly burst forth with an official imprimatur and a package of inducements for the self-employed, including tax exemptions, low-interest loans, and hiring rights . . ." Washington Post (February 5, 1982), p. A-23.

2/ These countries are Chile, Peru, Portugal, Egypt, Jamaica, Pakistan, Sri Lanka, Tunisia, Guinea-Bissau, Uganda, and the United Kingdom.



public sector has been openly expressed by local political leaders. <sup>1/</sup> The distinction between the two groups of countries is obviously blurred, as indeed is the exclusion of many countries from the list. Certainly, however, it is in these countries that plentiful examples of divestiture might be expected. In fact, examples are few.

Chile is unquestionably the best case. In the three years of the Allende Government (1971-1973), over 500 enterprises were taken into the state sector-nationalized, "intervened", <sup>2/</sup> or requisitioned. <sup>3/</sup> These were turned back to the private sector or liquidated with astonishing rapidity, as Table 1 shows. The Chilean divestiture was even broader than is indicated in the table, since much pruning took place within enterprises that remained in the state sector. Thus, the National Airline of Chile (LAN) eliminated unprofitable routes and concentrated on international service; SOQUIMICH, the state chemical corporation, closed many unprofitable plants; IANSA, the state sugar company, closed three inefficient mills and in 1980 was planning to sell a fourth.

Table 1. Public Enterprises in Chile

	1970	1973	1977	Target 1980
With participation in ownership				
Enterprises	46	229	45	15
Banks	—	19	4	—
Intervened enterprises	—	259	4	—
Enterprises in liquidation	—	—	17	—
Total	46	507	70	15

Source: Foxley (1982).

<sup>1/</sup> Turkey, Bangladesh, Somalia, Guinea, Ivory Coast, Mali, Brazil, Senegal, the Philippines, Argentina, and Zaire.

<sup>2/</sup> This refers to cases where government intervened in company management or seized companies with labor or production problems.

<sup>3/</sup> Prior to 1971 there were only 46 state-owned enterprises under CORFO, the agency responsible for most state commercial enterprises. (Corporación de Fomento de la Producción de Chile (Production Development Corporation of Chile)).





On a smaller scale, efforts at divestiture are also being made in Jamaica. The Seaga Government has acted in regard to sugar mills; of eight government-owned mills, two have been closed and five were divested by leasing to domestic and foreign sugar producers. Similarly, land under government ownership is being divested: some 20,000 acres now held by the Government Agricultural Development Corporation are being assessed for potential divestiture. In the tourism sector, the Government has tried to sell the hotels it owns; four of these have been leased to private parties, and negotiations were continuing in 1981 for the leasing of four others. Some hotels that cannot be sold at reasonable prices or even leased in their present condition have been transformed; five floors of the Kingdom International continental, for example, were converted to office space and another hotel was wholly converted.

In Peru, divestiture is still in a planning stage, although the planning is well advanced. In the late 1960s, Peru had 40 state-owned enterprises. After the military coup in 1968, this number grew fast-- by creation of new enterprises, nationalizations, and appropriation of bankrupt firms. The number of state-owned enterprises peaked in the mid-1970s to about 175, then declined to about 140 in 1982. Almost 100 of these are wholly state-owned, and the state owns over 50 per cent of the equity in another 17. The state-owned enterprises generate some 20 per cent of Peru's GDP and dominate major sectors of the economy: fishing, cement, chemicals, paper, fertilizer, agricultural marketing, banking, and utilities.

The Peruvian Government that took office in July 1980 announced its intention to reduce the number of state-owned enterprises by selling its shares. Some 70 firms are likely candidates. The market value of state-owned enterprises to be sold is probably about US\$500 million, or 2-3 per cent of Peru's GDP. The Government is working out a strategy for the sale, but little actual divestiture has yet taken place. 1/

Similar moves are under consideration elsewhere in Latin America. There have been reports that the Brazilian Government intends to divest a large number of state-owned enterprises in the next few years. A list of 250 candidates for divestiture has apparently been drawn up. Here, too, however, concrete action is not yet apparent.

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1/ IBRD-IFC (1982).



The Chilean and Jamaican experiences probably represent the most intensive divestiture efforts made in recent times. In the industrial world, only the U.K. experience is comparable. 1/

In the developing world, examples of divestiture can be seen in Pakistan, Bangladesh, Somalia, Sudan, Zaire, and the Philippines; there are undoubtedly many other countries for which information is not readily available. In Pakistan, two small engineering firms were returned to the private sector, and a specialty steel mill has been shut down. A rice mill and two sugar mills have been divested, and 12 other enterprises have been identified as candidates for liquidation or sale. In Bangladesh, major steps have been made to privatize the fertilizer marketing system. In the Philippines, the Government's National Development Company sold its shares in an electrical products manufacturing firm to General Electric Philippines. Other Philippine development banks have also divested a few enterprises. 2/ The Government of Zaire abolished many agricultural parastatals in 1978: namely, the agencies for cotton (CONAFITEX), maize (ONACER), sugar (ONDS), livestock (ONOE), edible oils (ONP), coffee (ONC), cocoa (ONDC), rubber (ONCN), fishing (ONP), and wood (ONB). A replacement grain marketing agency (ONPV) was dissolved in March 1981. The Somali Government liquidated four state-owned enterprises. The bus system in Khartoum, the Sudan, has been returned to private ownership.

Although this cursory survey has undoubtedly overlooked many other examples of limited or piecemeal divestitures, in general, despite widespread expressions of intent to divest, cases of divestiture are difficult to find. It is easy to understand why this is so, why few governments consider divestiture a viable policy, and why those that find it appealing also find divestiture difficult to implement.

1. There is, first of all, the classic general contradiction: governments do not want to sell profitable enterprises, and private parties do not want to buy unprofitable ones.

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1/ The U.K. Government under Prime Minister Thatcher has reduced its share in British Petroleum from 68 per cent to 39 per cent since 1978. In February 1981, it sold half of British Aerospace and just under half of Cable and Wireless, a telecommunications product and services company. More than half of British National Oil Corporation is slated for sale and British Gas will also be sold to private interests. These transactions involved sale of shares on the stock market. The National Freight Company, a road transport conglomerate, was sold to its workers and bankers in 1981. The Government would also like to sell British Shipbuilders, British Airways, and British Leyland. (Economist (London), November 28, 1981, pp. 94-95, and Wall Street Journal, March 16, 1982, p. 32).

2/ Far Eastern Economic Review, January 29, 1982, p. 51.



2. Potential effects on employment are a major obstacle everywhere. Overstaffing is almost invariably one of the reasons behind divestiture. Workers, their representatives, and political leaders know that, directly or indirectly, divestiture will almost surely mean higher unemployment. Fear of resulting political backlash is a major deterrent to divestiture-minded political leaders.

3. The political risks of divestiture are high for other reasons. The responsible officials or political party can be accused of giving away the national patrimony, selling out to capitalists or foreigners, or both. Whatever the price at which assets change hands between government and private buyers, charges of corruption are likely. Or the charge may be of incompetence, as in the United Kingdom. <sup>1/</sup> In some cases, divestiture involves destruction of national symbols. In Turkey, for example, the leadership reacts negatively to proposals for divestiture of state economic enterprises; they see themselves as heirs to Ataturk and consider the state-owned enterprises as his legacy, which should be retained. Much the same situation exists in some Latin American countries. In Brazil, some elements of government are in favor of widespread divestiture while others regard this as weakening national defense. In Argentina also, many state-owned enterprises are related to defense and are untouchable. In post-Nkrumah Ghana, an attempt to sell a state pharmaceuticals company to the American firm, Abbott Laboratories, led to street demonstrations and university student protests against turning back the anticolonial clock. The sale never took place.

4. Sale of state-owned enterprises is relatively easy only for enterprises that came into the state sector as a result of a political-ideological transformation that has subsequently been reversed. That is, the state enterprise sector of most countries comprises three elements: (1) enterprises that were created by the government and have always been in the public sector; (2) failed enterprises that were once private or semipublic but that have since been taken over by the government to avoid liquidation; (3) enterprises taken over during a revolution or during a period of pronounced political change. It is relatively easy to divest by sale only the third group of enterprises because they were presumably once profitable and former owners can be identified. This was the case in Chile, as well as in the Pakistan divestitures.

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<sup>1/</sup> The U.K. Government's sale of a small state-owned enterprise, Amersham International, gave rise to a storm of criticism by the Labor Party and other critics. The stock exchange put a value 30 per cent higher on Amersham stock than the price asked by the Government when it divested. Speakers in Parliament charged that the Government sold a successful enterprise ". . . at a knocked-down price . . . giving unjustified profits to some private institutions and individuals at the expense of the Exchequer." (Wall Street Journal, March 1, 1982, p. 27).



5. Even in highly permissive circumstances, small but delicate problems surround the actual divestiture.

(a) In the more advanced countries, sale of state enterprises involves sale of equity. This is the case in the United Kingdom, for example. The size and sophistication of U.K. financial institutions and capital markets are such that the Government's shares can easily be absorbed by private buyers and institutions; reduction of government holdings thus presents few difficulties. But this is not the case in developing countries. An economy as advanced as Peru—with its well-developed system of financial intermediation, a sizable middle class, and a mature private sector—cannot easily absorb the 70-odd state-owned enterprises slated for divestiture. Sale of the approximately US\$500 million in assets involved could crowd out other claimants for investible resources and accentuate inequalities in income and wealth. A smooth sale requires careful planning, a gradual approach, and the strengthening of financial institutions.

(b) Agreement on a price acceptable to the buyer and seller is particularly difficult. Buyers often enter the negotiation with the expectation of a bargain. As the government has made an enormous commitment by publicly announcing its willingness to sell the enterprise in question, buyers anticipate that the necessity to sell will result in a very low asking price.<sup>1/</sup> But the officials and politicians responsible for the sale fear that they may be accused of selling at too low a price so they are inclined to push up the price.

(c) In some cases, there are thorny problems of how to handle debt obligations of the enterprise to be divested.

Not only is divestiture difficult to achieve, but its benefits often appear slight and it can involve significant costs. Benefits must, of course, be defined in terms of objectives. In governments considering divestiture of state-owned enterprises, four main objectives are usually involved, implicitly or openly: (1) reduction of fiscal and monetary pressures; (2) improvement in efficiency of resource use; (3) reduction in the burdens on public sector managers; and (4) reduction of government for ideological reasons.

The reduction of fiscal pressures can result from smaller wage bills and lowered demands for investment resources, the monetary relief from reduced credit absorption. But experience in a number of countries (Peru, Pakistan, and Somalia, for example) suggest that the usual candidates for divestiture are neither big employers of labor nor major absorbers of credit. Most employment is in essential state-owned

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<sup>1/</sup> This happened in Canada recently, in negotiations over divestiture of some units of Air Canada.





enterprises, such as railroads and utilities; in a few strategic industries, such as copper in Chile and Peru or sugar in Somalia; in nonmanufacturing enterprises, (notably marketing) which are not usually targets of divestiture. It is the same with credit absorption. The deficits of these organizations and their resultant borrowing from the banking systems are generally due to imposed subsidies which are not reimbursed by government. Deficits of the manufacturing state-owned enterprises--the prime subjects of divestiture talk--account for only a small share of outstanding credit (in Somalia, for example, less than 15 per cent in the late 1970s).

It is true that the efficiency of resource allocation and use would probably be greater if state-owned enterprises were divested. But the major culprits are not usually even considered as targets for divestiture--the railroads, for example. In small countries, the state manufacturing sector is normally tiny. In Somalia, for example, outside of sugar refining, state industry employs fewer than 5,000 people (less than 3 per cent of the paid labor force) and its economic contribution in terms of share of GDP or share of exports is only slightly higher.

The same reasoning applies to sale with the objective of reducing management problems. In the few countries where divestiture is being seriously considered and analyzed (Pakistan and Peru, for example), the enterprises listed as candidates for divestiture include few of the ones causing problems.

Thus, potential benefits seem small in most cases. There is not much fiscal relief to be had by cutting down on padded payrolls, and the manufacturing state-owned enterprises--the usual focus of divestment strategies--normally do not contribute much to credit expansion problems. A lowered burden on public sector managers might be a more significant factor and general ideological preferences can certainly be satisfied.

If the benefits are small and uncertain, the costs of divestiture and of efforts at divestiture can be substantial. There are, first, political costs to the authorities. As noted above, divestiture requires the responsible authorities to take extremely unpleasant and often politically dangerous steps--cause unemployment, destroy symbols of modernization, impose economic hardship on particular regions and groups, and admit past errors and waste. Any sale of public assets to private parties generates suspicion of corruption and charges of selling out to capitalists--often foreigners. Such a sale can easily give rise to charges of incompetence, at best. It is not surprising that local authorities tend to be unenthusiastic, to say the least, in their attitudes toward divestiture.

There are also political opportunity costs. In pushing for divestiture, economic reformers forgo political goodwill and deplete intellectual



resources that could be used with greater effect in other reform initiatives. 1/ And there can be economic opportunity costs as well.

The argument set out above is, first, that prospects are poor for closing or selling state-owned enterprises--particularly the industrial state-owned enterprises whose presence and inefficiencies excite reformers; and, second, that the gains are not likely to be great in any case. If that is true, then the question becomes: What should be done with state-owned enterprises? A good answer requires an analysis of the dangers and opportunities created by the presence of these enterprises.

The main problem is not that state-owned enterprises are over-staffed, overfinanced, and inefficient. It is not even that, in many instances, there is little economic justification for their existence. After all, all societies have remnants of economically irrational investments. An oversized fruit cannery or match factory, or an under-utilized steel mill, represent no greater waste of resources than some roads or hospitals or administrative buildings. The special danger of the industrial state-owned enterprises is that they will not remain static; there are recurring efforts to try and validate them. The cannery management seeks a satellite scheme; a milk processing plant seeks a state dairy farm; a meat processor tries to monopolize animal purchases in order to secure a supply of beef that is otherwise unattainable. If attempts to create economically unjustifiable linkages can be thwarted, the industrial state-owned enterprises in most countries are at worst inexpensive symbols, easily supportable.

This does not mean, of course, that efforts to reduce their social costs should be abandoned or that the search for ways to increase their benefits to society should be given up. The general prescriptions for greater efficiency for state-owned enterprises everywhere are unexceptionable--that is, improvement of management, greater transparency of operation, and reduced politicization in some key respects. Better management is, of course, not only--perhaps not even mainly--a matter of training better managers. Most problems of these enterprises derive not from managerial incompetence, but from the surrounding environment and from history, weak budgets and accounting systems, disorderly intrapublic sector financial relationships, scarcities of trained and motivated staff, uncongenial macroeconomic conditions (for example, limited and irregular access to foreign exchange and even to domestic raw material inputs, and working capital scarcities due often to tax policies), and the fact that many state enterprises were originally ill-conceived.

These problems of the state-owned enterprises are likely to diminish slowly, even with persistent efforts at reform and with improvements

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1/ This is, of course, true for both local reformers and foreign donors or financial institutions.



in management skills. Because divestiture offers equally limited prospects in the short term and medium term, the policy issue becomes how to capitalize on the presence of these enterprises--how to use them in a positive way for development, while curbing their tendency to expand. Even the least efficient state-owned enterprise has some potential benefit. In particular, in the least developed countries with abundant aid, they can be used to provide needed channels for external assistance and can be encouraged to take on an explicit training role for the surrounding economy. Since these ideas are somewhat novel, they are explained in greater detail below.

One way to strengthen the management of state-owned enterprises and to allow managers to deal more effectively with the problems of the environment is to bring in foreign management specialists under managing agency arrangements. This is especially applicable in the small developing countries. This solution would serve three purposes:

(a) A formal link would be created between the enterprise in question and some donor source.

(b) Foreign management would probably be more inclined to debate with government such matters as input and output pricing; the foreigners might also be able to better withstand political pressures with respect to hiring and firing.

(c) Day-to-day management would probably be improved, and more on-the-job training could take place.

The central idea here is that, for the industrial state-owned enterprises in this group of countries, what is needed is special access to a foreign source of support--which could provide money and other help--access to information, including technology, and perhaps political support--and that this special access can be created by means of a foreign management team. A case illustrating the potential of this suggestion is the Juba Sugar Project in Somalia. This large enterprise (4,000 hectares already in cane and 8,000 planned, with accompanying refinery) is managed by Booker International. The Somali authorities have brought in this expatriate management team and, with it, have widened access to official U.K. assistance. Thus, the Juba project was endowed by the British Aid Agency (ODM), with a well-equipped training workshop for the key crafts; it is probably the best source of such training in Somalia. Other training efforts are evident at Juba--middle-level management workshops, for example, very few of which seem available elsewhere in Somalia. Casual observation suggests that this kind of training is much more relevant than what is provided in the crowded classrooms of the school of administration in the capital.

Even more to the point, when a vital piece of equipment broke down recently, and there was no hope of obtaining money either from project



resources or from the Somali Government budget to replace it, Booker International called on the ODM for help, which came in the form of a small grant (£25,000) for purchase of the required equipment. The presence of Booker in Juba has opened the possibility of further U.K. assistance of this kind. Moreover, in many countries there is untapped potential for using the state-owned enterprises as training centers for the economy as a whole. For example, in the Somalia case, the training efforts at Juba could easily be expanded for this purpose, with financing by government subsidy and/or foreign assistance.

The Juba model could also be duplicated in other state-owned enterprises in Somalia and in similar developing countries. The development literature for decades has pictured industrial enterprises as sources of "externalities"--notably training and intangible modernizing effects. In fact, the industrial sectors of many developing countries have provided little training and few intangible benefits. But industrial state-owned enterprises can be made to serve these goals more effectively by moving in the direction indicated--that is, bringing in foreign management to ease access to aid and making special efforts to turn the factories into on-the-job training institutions, which will produce skilled people for the economy as a whole.

For heavily assisted developing countries, there is a significant advantage in having industrial state-owned enterprises in the public sector; if these enterprises were divested, they would be excluded from access to most official development assistance. In that group of countries, where donors are plentiful and willing to help but few channels exist for aid, this could provide a major opportunity.

Thus far, divestiture has been considered in terms of sale or liquidation, but there are other methods for achieving the same objective which are more likely to be acceptable to local decision makers. One such method is leasing. Lease arrangements can be coupled with equity participation by private parties. They can be written so as to make the lessee responsible for rehabilitation or refurbishment investments, in return for a share (conceivably up to 100 per cent) of profits.

Leasing is especially suitable in situations where profitability is achievable if amortization of capital costs and interest charges can be reduced or completely written off and if profits are especially sensitive to management inputs. It has been used in the hotel industry in a number of developing countries, such as Jamaica and Liberia, but it has broader potential.

Leasing is a versatile and potentially powerful instrument of indirect divestiture. Some of the same effects can be achieved by deregulation and encouragement of competition. This is not likely to be acceptable for commodity-producing state-owned enterprises; few governments are willing, for example, to expose their import-substitution





industrial enterprises (public or private) to foreign competition. But leasing is certainly relevant for state-owned enterprises in marketing and other services. The best way to reduce the negative effects of these enterprises in agricultural marketing, for example, is to allow other agents to compete. This opens up the general matter of service delivery--the second instrument of privatization.

## V. Private Provision of Services

Many governments discourage the private provision of services. They claim that services such as health care, water supply, education, animal vaccinations, etc., are so important that they should be provided not only without charge but also exclusively by the public sector. However, this excludes a large and potentially beneficial source of supply--that offered by private individuals and nongovernmental organizations. If governments would encourage these private suppliers, they would increase the quantity and diversity of services offered and reduce the burdens on the public sector. They might also reduce costs, since these services are now offered illegally, in many cases; wider opportunities to provide such services would reduce risk and stimulate supply.

The range of services that can be privately supplied is, of course, very wide, and the kinds of suppliers are highly varied. Some examples are given below.

### 1. Education

Private education has a long history in industrial as well as in developing countries. In the nineteenth century, "performance contracting" was common; for example, villagers paid teachers a fixed fee when the child attained measurable competency in reading and writing. This system began in the United Kingdom and spread to India, Malaysia, Canada, and West Africa. In many developing countries, church groups and other private voluntary organizations have long been major sources of education as well as health care. And in much of the world, private schools continue to exist, and vocational training is done very extensively outside formal educational systems--by apprenticeship schemes, secretarial schools, etc.

### 2. Health care

In many developing countries, modern health care services and sale of nontraditional drugs are legal monopolies of the state. In fact, however, illegal markets flourish--for pharmaceuticals provided by private purveyors who circulate even in rural areas and for medical services provided by pharmacists or publicly-employed medical doctors and nurses who also work for private patients. The World Bank report on sub-Saharan Africa has several relevant observations:



In rural areas, often the only legal source of drugs is the public sector pharmacy or dispensary. The public sector frequently offers inadequate and irregular drug supplies, however. In many cases, budget allocations for pharmaceuticals are used up in the first few months of the year. Most rural people must, therefore, either do without, or buy on the illegal market--if they can afford it. Reductions in the legal restrictions on sales of basic pharmaceuticals would increase the public's access to these drugs and reduce their cost, making a major contribution to the health care of the majority of Africans . . . .

In market-oriented countries, this approach could be developed further. For example, training paraprofessionals in health and sanitation, and encouraging them to set up on their own, would limit the public sector role to training, certification, and supervision. Rural health workers would then circulate, or establish themselves in the villages, and provide services for fees. In contrast, the public-sector strategy (village health workers serving a group of villages) involves great financial and logistic difficulties, thus far unresolved in most of Africa, or indeed elsewhere. This example serves to illustrate a general point: much of the administrative burden in the public sector arises from the need to organize, motivate, and control people; and this burden could be reduced if the private sector were allowed a greater role under government leadership. 1/

### 3. Marketing

Agricultural marketing services are also a government monopoly in many developing countries, at least on a formal legal basis. This is especially the case for export crops and inputs (fertilizers, agricultural equipment, agricultural chemicals); in many instances, food crop marketing is also a legal monopoly of government. Agricultural marketing, in the conditions normally found in developing countries is inherently unsuitable for large-scale, bureaucratic organizations because it entails many small transactions taking place over large physical areas, typically characterized by poor communications and rapidly changing circumstances. It thus demands flexible, rapid, and decentralized decision making because of the enormous obstacles to effective central supervision and control. Moreover, state trading systems require relatively heavy inputs of skill per unit of sales (accountants, administrators, supervisors, etc.) and state trading monopolies waste the skill, experience, and human energy available in the actual or potential community of private traders. Such state monopolies substitute costly, formally acquired skills for the raw capacity and energy generated by the search for profit. Also, public sector trading monopolies involve wasteful use of capital resources.

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1/ World Bank (1981), pp. 37, 88.



They are by nature capital-intensive, requiring bigger inventories, more and better warehousing facilities, and more elaborate accounting procedures than private trade.

There are many good and understandable reasons why governments around the world have ventured so extensively into agricultural marketing, and why in developing countries they have tried so frequently to impose government monopsonies and monopolies. But experience--almost without exception--has proved this practice to be a burdensome, unsuitable, and inefficient use of public sector resources. If the main rationale for the establishment a public sector presence in rural marketing is to protect peasants against exploitation by private traders--which is often said to be the case--then the best way to achieve this goal is to allow competition between public and private trading agents. Monopoly--public or private--is the breeder of inefficiency, and market power, from whatever source, permits exploitation. Allowing private traders to compete with state trading monopolies might therefore be a major source of new resources and improved efficiency in the use of current public resources. And this policy can also spur rural effort by making the economic environment more open and more rewarding. 1/

#### 4. Drainage and salinity control

Experiments with new uses of private sector resources to meet rural development needs are taking place in many countries, although they have received little attention. In Pakistan, for example, private tubewells have taken over the major task of salinity and waterlogging control in the Indus River Plain. Twenty years ago the Pakistan Government and foreign donors decided that the most efficient and equitable approach to water control in this area was to install large-volume public tubewells. Private tubewells were to be tolerated, but it was envisaged that they would ultimately disappear. 2/ But despite the expenditure of billions of rupees by the public Salinity Control and Reclamation Projects (SCARPs),

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1/ It does not diminish the force of this argument to recognize that allowing private competitors into markets monopolized or monopsonized by state agencies is neither simple nor problem-free. In fact, one of the underlying obstacles to liberalization of these markets is precisely that much of the superstructure of price and marketing policies has to be overhauled for an effective liberalization of marketing to take place. Subsidies, pan-territorial pricing, and price stabilization schemes are all made difficult by a private presence in the market. The private traders buy where costs are relatively low but they charge full costs to consumers. This profit-maximizing (cost-minimizing) behavior is often attacked as "creaming the market." What it really means is that a state agency cannot survive competition with private traders if it must pursue social policies involving noncost-minimizing behavior; it must be explicitly subsidized to cover the losses that are inevitably incurred.

2/ Mohammed (July 1967).



which built and now maintain 11,000 tubewells, the private tubewells did spread and today they pump twice as much water as the public tubewells. Moreover, the water table has risen to dangerous levels in much of the area served by the public tubewells; the best drained region is the Bari Doab, which has no SCARP at all, but has many private wells. In addition, tubewell maintenance and repair costs are absorbing a growing share of the money available for irrigation, and the Pakistan Government now faces the appalling prospect of financing the replacement costs of the aging stock of public tubewells. The solution being explored at present is to privatize the public tubewells entirely, leaving the salinity and water control job to private wells financed by individual farmers and groups of farmers. The transitional problem of how to arrange the transfer of the existing public tubewells is now under consideration.

##### 5. Agricultural extension

No public service is given a more critical role in the development process than agricultural extension. The agricultural extension agent is supposed to be the transmitter of new technology and the instrument of agricultural transformation. Yet the virtually universal reality in developing countries is that agricultural extension agencies function extremely poorly. It is especially difficult to recruit and retain trained and motivated staff for these agencies. The deficiencies of budgeting and the cumbersome financial administration, as well as the scarcity of nonsalary budgets, mean that most extension services are poorly provided with equipment, especially vehicles. They are always short of fuel and spare parts, so that services are often impossible to perform. Moreover, long distances, bad roads, and poor communication make supervision and control of agents especially difficult.

The fielding of a smoothly functioning, effective extension service represents an administrative and organizational achievement that is beyond the reach of most poor countries for some time. Is there a way to accomplish some of the objectives of extension by privatization?

Actually, Latin America has a tradition of private extension services. In Colombia, for example, the agricultural bank (Caja Agraria) required the borrowing farmers to arrange for private technical assistance as part of the loan agreement. The farmer would hire a private specialist—an agronomist or another farmer recognized as expert—with financing provided by the loan. This assistance was provided without charge to small farmers.

In Uruguay and Argentina, these arrangements took a slightly different form. In Argentina, farmers or ranchers joined together to form Regional Agricultural Experimentation Consortia (CREAs). These began in the 1950s. <sup>1/</sup> They were patterned after the French Centres d'Etudes Techniques (CETAs). They bring together a small number of farmers (8-12)

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<sup>1/</sup> Arias (1972).





for monthly or bimonthly meetings. The group hires a technician to advise them. They visit one farmer's (rancher's) fields (or herds) for several hours and spend the rest of the day discussing what they saw. Thus, new techniques including such innovations as organic farming and use of water conservation and low-input technologies, are introduced. By 1970, there were 108 CREAs in Argentina, with 1,130 farmer-members whose holdings covered 2.9 million hectares. They have a national organization, hold training courses, and publish a monthly newsletter and a journal.

The farmers and ranchers involved in these CREAs and related organizations are, to be sure, those with relatively large farms, but the model can be adapted for small farmers. A recent experiment in Chile suggests the potentials of innovation along these lines and also indicates some of the difficulties. For a long time Chile has had the reputation of having one of the best-financed and best-staffed extension operations in the developing world. It was nonetheless much criticized because of its poor services to farmers. Over 90 per cent of the Chilean Government's agricultural technicians and professionals were located in Santiago or the provincial capitals; they were rarely in the field. In the 1970s, there were three main public sector institutions responsible for providing technical assistance to agriculture: the Agriculture and Livestock Service (SAG), the Agrarian Reform Training and Research Institute (ICIRA), and the Agricultural Development Institute (INDAP). Technicians employed by the SAG and the ICIRA numbered about 450 in the late 1970s, almost all of them working in the so-called reformed sector, consisting of small landholders who benefited from earlier land reform efforts. But the help these technicians gave was mainly nontechnical--for example, preparation of credit applications and formation of cooperatives. The agencies were unable to tell farmers much about crop practices, new seeds, and alternative technologies.

This centralization of extension efforts presented some difficulties to the post-Allende Government. The reformed sector included 40 per cent of the best land in Chile, but this land now belonged to small farmers who had little capital and, often, not much technical knowledge or management experience. To deal with this challenge, the Government started a program based on the idea that technical assistance to these farmers should be provided by the private sector, with the Government subsidizing the cost. The basic approach is that individual farmers contract for a package of technical services (farm planning, planting help, advice on agricultural practices, post-harvest evaluation) from agricultural "consultants." Middle farmers (owning between 5 to 15 hectares) are eligible for a subsidy covering 70 per cent (about US\$200 total) of the cost of the package. Farmers with holdings smaller than five hectares could also benefit from subsidies if their cash flow permitted some payment. If not, they would continue to be served through the supervised credit operation of the Agricultural Development Institute (INDAP). The Government was expected to enroll 10,000 farmers in the subsidy program in the first year, and 30,000 to 40,000 after a few years.



The subsidy element in the program quickly revealed some flaws-- notably the weakness of supervision and control. It was difficult for the Government to know whether the farmer actually received the technical services for which he contracted. Both the technical assistance "consultant" and the farmer had an obvious interest in receiving the subsidy, even if service delivery was inadequate. They could, conceivably, conspire and divide the subsidy, so that they would benefit whether or not technical assistance was actually delivered.

The Government therefore modified the system in 1981. Its central features have been retained, but more controls have been introduced. For example, the new arrangement provides for closer surveillance and harsher penalties for violation of the law. It seeks better compliance with contractual obligations. Financing arrangements have been modified with this end in view. Previously, the farmer was supposed to make some cash payment out of his own pocket to his technical assistance consultant, but this was difficult to verify. The new arrangement specifies that farmers must make advance payments to consultants before the Government will make its contribution. While this experiment in subsidized private agricultural extension clearly presents serious administrative difficulties and pitfalls, it is highly innovative and illustrates the possibilities for creative use of private service delivery to meet urgent development needs.

#### 6. Transportation

Transportation, especially urban transportation, offers many opportunities for private activity. In most cities, two common carrier systems coexist. One is the modern bus and subway network, which is relatively capital-intensive, highly structured, and usually organized in the form of publicly-owned or franchised monopolies. The other is a privately-owned and organized fleet, more diverse and unstructured; it includes such vehicles as taxis, minibuses, vans, jitneys, and rickshaws. In case after case, the superiority of the private, small-scale system has been demonstrated convincingly. A few of these cases are summarized below. 1/

For many years, the citizens of Hong Kong relied for their transportation on bus companies enjoying exclusive franchises. In the early 1930s, competition from illegal taxis became severe. These taxis were used as small buses, hired by a group at an agreed rate for a specific trip or by individuals who paid by the seat. In 1960, the Government allowed these vehicles to be licensed for specific functions--transportation of workers, school children, airline staff, and hotel guests. At the same time, many minibuses continued to operate without licenses (that is, illegally); although registered as private cars, they were available for hire.

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1/ These are drawn from Roth and Wynne (1982) and Midgeley (1981).



The Government persistently discouraged the private operators and favored the franchised buses, but the level of comfort and frequency of service of the latter were so unsatisfactory that demand for the informal carriers grew sharply and the number of nonfranchised carriers approximately tripled during the 1960s. In 1969, the Government legalized the minibus as a form of common carrier--the Public Light Bus. By 1972, the Public Light Buses were handling one fourth of all public transportation, and by 1976 they handled one third. More than 4,300 Public Light Buses had been licensed, and the Government, worried about the survival of the franchised buses, then stopped licensing new Public Light Buses.

In Buenos Aires, Argentina, the colectivo (microbus) is the main mode of transportation. It arose in the 1920s as a shared taxi, operating on a fixed route chosen by the driver himself. In 1936 the Argentine Government clamped down on the colectivos and created a state enterprise to which it gave a total monopoly of city transportation, but some microbus lines survived. In 1951 the state enterprise (Transportes de Buenos Aires) took over all services, but this was a disaster both financially and in terms of quality. By 1959 it was incurring a deficit of over US\$1 million a year. In 1962 it was liquidated--one of the few recorded cases (perhaps the only one) of the divestiture of an urban transportation system. Private operators took over all transportation services except the subway.

In Calcutta, India, the use of private buses, a system in operation since the end of the 19th century, was banned in 1960 when the Calcutta State Transport Corporation (CSTC) was given a monopoly. The CSTC quickly ran into financial, managerial, and labor relations problems, including a paralyzing strike in 1966. In response to public demands expressed before the 1966 elections, and also to raise money, the West Bengal Government licensed 300 private buses. These proved profitable, although they charged the same fares as the unprofitable CSTC and their routes were inferior. By the late 1970s, Calcutta had some 1,500 full-size private buses in operation, as well as about 500 private minibuses. They now carry, without subsidy, two thirds of all bus traffic in the city. The CSTC, with the best routes and the same fares, is subsidized by the Government at US\$12 million a year. The success of Calcutta's private bus operators illustrates some general advantages of private sector service in the less developed country setting.

(a) Private buses are kept in operation, with necessary repairs being quickly done. The CSTC, which has to go through bureaucratic procedures to get spare parts, usually has half of its buses out of operation at any one time.

(b) Private bus crews, paid a percentage of revenues, make greater efforts to collect from passengers. Fare evasion is estimated to be 25 per cent on CSTC buses, whereas it is negligible on private buses.

(c) The CSTC is greatly overstaffed. In 1980, it had 50 employees per bus, one of the highest such ratios in the world.



The private bus owners in Calcutta are organized into associations that have contributed to a successful operation. These organizations, formed voluntarily and spontaneously by the private owners, set down rules to allow smooth and equitable relations between buses, such as rules about running on time. Operation, maintenance, and overall management of the vehicles remain in the hands of the individual owners.

Some cases in Africa show both the perils of refusal to rely on the informal, small-scale sector and the benefits of doing so. Abidjan, Ivory Coast, was served until 1974 by a very active informal system of common carriers, known as a'bakas. Originally, they brought goods from outlying areas to city markets, and later they evolved into illegal common carriers for the low-income areas of the city. In 1974 Abidjan's bus system, Société de Transport d'Abidjan (SOTRA), a joint venture with a majority share held by the Government, urged the Government to ban the a'bakas in the city limits because of unfair competition. The Government agreed to do so. The consequences were unfortunate—for the people of Abidjan, for the municipal and national budgets, and even for SOTRA. Before 1974, SOTRA was profitable, despite the competition of the informal carriers, and it had a well-managed fleet of 300 buses. With the banning of the a'bakas, SOTRA launched an extensive fleet expansion and capital construction program; by 1981 the fleet had 900 buses, and it is supposed to increase to 1,600 by 1985. As a result, SOTRA has been in deficit since 1975.

The story of Dakar, Senegal is similar. The two sectors in Dakar consist of a bus company, Société de Transport en Commun (SOTRAC) and private minibuses, or "Cars Rapides." SOTRAC dates from 1971, with a 15-year franchise (monopoly) on public transport in Cap Vert (the Dakar metropolitan area). 1/ In 1981 SOTRAC had 430 buses and 35 minibuses. The informal transportation sector is dominated by Cars Rapides, organized in 1961 on a cooperative basis and later into a syndicate. At present, there are 650 vehicles in operation, less than the 1974 peak of 700 vehicles, owing to government restrictions on fleet expansion. Cars Rapides handle 40 per cent of all passenger trips, whereas SOTRAC handles 20 per cent, and taxis and private cars handle the remaining 40 per cent. SOTRAC operates with a growing deficit, from US\$2.2 million in 1976-77 to US\$3.8 million in 1978-79, representing 25 per cent of total operating costs in that year.

Deficits notwithstanding, SOTRAC proposed to expand service so as to achieve effective monopoly of Dakar's public transportation. For this purpose, it would need almost 500 additional buses and greatly expanded facilities—at a probable cost of US\$61 million. 2/ This would entail

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1/ SOTRAC is owned 64 per cent by the Government, 27 per cent by Renault-Saviem, and 9 per cent by others.

2/ French public and private capital would probably finance 38 per cent of this total.





also the banning of the Cars Rapides, which in 1979 carried twice as many passengers as SOTRAC buses without government subsidy and in the face of government restrictions on fleet expansion or even replacement.

In Nairobi, Kenya, a happier road was followed. "Matatu"--the private minibus variant in that city--were legalized in 1973. About 3,600 of them operate around Nairobi; about 1,000 provide purely urban service. Modern transportation is provided by the Kenya Bus Service Ltd. (KBS), which has 320 buses under a franchise with the Nairobi City Council and is a foreign-owned private company. After 1973 it decided, on grounds of unfair competition, not to increase its fleet when the matatu were legalized. So, while the population of Nairobi grew from some 500,000 in 1970 to almost 1 million in 1980, the fleet remained about the same size. The company's buses ply the main routes, with the company covering costs. Matatu, meanwhile, are the backbone of the transportation system. In 1979 there were 1,550 privately operated matatu, carrying 66,000 passengers a day. They go where the business is--that is, in low-income areas and, in peak periods, along commuter corridors and charge about the same fares as the Kenya Bus Service.

There can be little question that in urban transportation--and, almost as surely, in other transportation--small-scale, private operators have decisive advantages over the public sector producers. One observer comments as follows on the informal, private systems: 1/

At first glance they all appear to be different, but this is primarily because of variations in hardware--from bicycle rickshaws to sleek European minibuses. The institutional structure and basic operations are quite similar: private individuals acquire the highest technology vehicle that they can afford, and respond to the mobility demands of their neighbors at a tariff that most of them can pay . . . A few billion people cannot all be wrong, and there is really no need for us to painfully invent a new urban transportation mode when there are literally thousands of jitney systems in flourishing operation.

#### VI. Government Contracting of Services

As noted earlier, sharp distinctions between public and private sectors can mislead; economic activities rarely fall into one or the other category in all their dimensions, nor are they usually in pure form in any dimension. Thus, governments may finance an enterprise and allow a private firm to run it, or private owners may finance an

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1/ Sigurd Grava, cited by Roth (1982), p. 211.



enterprise with subsidies from the banking system. It is suggested above that, for these reasons, the picture of "private" and "public" sectors, each constituting a well-defined and separate entity, is not quite accurate.

It is nonetheless useful to distinguish the public sector from the private sector in terms of how public services are supplied or provided. Thus, there is an important distinction to be made between the agent or agency that organizes, arranges, and (usually) finances the supply of a service and the agent who delivers, produces, or manages it. By reducing the public sector's role as producer or delivery agent and increasing its role as organizer, arranger, and overseer of privately produced goods and services, the potential for constructive privatization is greatly enhanced.

Public services can be delivered in many different ways, in addition to conventional provision by a government agency through its own employees. 1/

(a) Under intergovernmental agreements, one unit or level of government pays another to supply a service. U.S. counties, for example, sometimes draw up contracts with cities for the maintenance of county roads within city limits. 2/

(b) Contracting of services is extremely widespread, in all areas of activity. Much of the U.S. national defense, that pre-eminent public good, is, of course, privately handled by contractors. A private contractor even mans and operates the Arctic Early Warning System. And elsewhere, there are now private air forces as well as mercenary forces for hire.

(c) Franchising is another method, either exclusive (a grant of monopoly rights to a private firm to provide a given service) or nonexclusive (for example, taxi franchises). In some countries franchising is common in utilities (gas, water, power) and in urban transportation.

(d) Grants and vouchers are well-known devices for encouraging consumption of goods and services. A subsidy from government to producers is the classic form of grant. Vouchers are subsidies to the consumer for specific goods or services—for example, housing, food, education, and cultural activities.

(e) In free market transactions, the government is not present at all, although it may set standards for the provision of services.

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1/ Savas (1981), p. 58.

2/ Such arrangements are very common in the United States: in 1973 two thirds of American cities had arrangements with other government units for services such as water supply, sewage treatment, jails, police communication, libraries, animal control, and public health services (Savas (1981), p. 59).



(f) Voluntary services can be organized and delivered by consumers themselves; recreation facilities, fire protection, protective patrols, and street cleaning are examples.

The instrument with the greatest relevance to the private sector in developing countries is contracting. It is widely used in the industrial world. Table 2 illustrates the vast array of activities that U.S. cities contract to private firms. In Denmark, one private firm handles ambulance and fire services for most cities; Savas observes ". . . while Wall Street is cleaned by a government bureaucracy, the streets in Communist Belgrade are cleaned by a worker-owned enterprise that has a contract with the city government." 1/

Comparable contracting arrangements are rare in developing countries, although they do exist. The city of Buenos Aires, Argentina, for example, created in 1977 a public corporation, Cinturon Ecologica Area Metropolitana S.E. (CEAMSA), to improve the region's physical environment. Its main preoccupation has been trash collection. The agency contracted (after open international competition) with a single private concessionaire. The contractor was paid on the basis of waste tonnage deposited at specified fill areas rather than on the basis of cost and was given complete freedom to organize the work and the work force. The number of employees involved in trash collection is now one seventh the number previously employed, the cost to the region's government is lower, and the urban administrative burden has been greatly reduced. The success of this approach is said to have stimulated interest in other cities--for example, in Caracas, Venezuela.

Contracting also involves major problems that limit or condition its use. A 1978 U.S. study of municipal contracting for the provision of private services listed the arguments commonly raised against private contracts. 2/

(a) Higher cost. Contracting involves costs in government administration, and the contractor's profit (or fees) must be added to the government's cost of doing business. Consequently, contracting of services to a private concern can be more expensive than public delivery of services.

(b) Poorer service for citizens. Since the objective of private firms is to maximize profits, a firm may reduce its service in order to increase its profits.

(c) Chance of corruption. Because of the desire of private firms to obtain contracts and to increase profits, great pressure may exist for contractors to engage in questionable or illegal practices, such as bribery, kickbacks, and payoffs.

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1/ Savas (1981), p. 65.

2/ Fisk (1978), pp. 7-10.



Table 2. United States: Number of Cities Using Private Firms to Supply Municipal Services Under Contract <sup>1/</sup>

Service	No. of Cities Contracting with Private Firms	Service	No. of Cities Contracting with Private Firms
Refuse collection	339	Sewer lines	14
Street lighting	309	Treasury functions	14
Electricity supply	258	All fire services	13
Engineering services	253	Mosquito control	12
Legal services	187	Museums	12
Ambulance services	169	General development	10
Solid waste disposal	143	Alcoholic rehabilitation	9
Utility billing	104	Records maintenance	9
Animal control	99	Election administration	8
Planning	92	Police communications	8
Water supply	84	Building and mechanical inspection	7
Mapping	74	Fire communications	7
Water distribution system	67	Housing	7
Payroll	65	Recreational facilities	7
Street construction and maintenance	63	Personnel services	6
Hospitals	57	Urban renewal	6
Special transportation services	49	Crime laboratory	5
Cemeteries	47	Irrigation	5
Microfilm services	47	Parks	5
Nursing services	34	Traffic control	5
Assessing	31	Water pollution abatement	5
Public relations	30	All public health services	4
Bridge construction and maintenance	25	Juvenile delinquency program	4
Industrial development	24	Licensing	4
Tax collection	24	Soil conversion	4
Mental health	22	Civil defense communications	2
Sewage disposal	21	Fire prevention	2
Management service for publicly owned transit	18	Noise abatement	2
Electrical and plumbing inspection	17	Patrol Services	2
Libraries	17	Registration of voters	2
Zoning and subdivision control	16	Training of firemen	2
		Air pollution abatement	1
		Jails and detention homes	1
		Welfare	1

Source: Savas (1981), Appendix Table 3a.

<sup>1/</sup> Based on responses of 2,375 cities to a mail survey in 1973.





(d) Possibility of default. Unlike government, a contractor may go bankrupt or cease operations.

(e) Public employee displacement, drawing opposition from municipal unions. Contracting existing government services can cause strikes, slowdowns, and legal challenges by labor unions.

(f) Problems in drawing up adequate contracts. In many service areas, it is extremely difficult to formulate contracts that will ensure that a government actually receives the desired services that it agrees to pay for.

(g) Failure to guarantee adequate competition for certain contracts. For certain services, such as fire protection, few, if any, private firms exist to provide the service.

(h) Reduced flexibility of response to change. Since contracts have to be written in very specific terms, a government does not have the ability to respond quickly to major changes in service requests. Moreover, renegotiations can be costly.

(i) Lack of control over the final service. Because of the difficulty of writing and enforcing performance contracts, particularly those which focus on the quantity and quality of final products and services, a government may lose some degree of control over these products and services.

(j) Need for close monitoring. To ensure that a government receives what it pays for, detailed monitoring of the contractor's activities is required. This problem does not exist, at least not to the same degree, when a government produces the service itself and all employees are under its direct control.

The following arguments are advanced by advocates of more contracting by the government. 1/

(a) Contracting is more efficient. It exposes inefficient producers to competitive forces, permits less political management, and puts the costs and benefits of decisions directly on the decision-maker, whose own rewards are directly at stake.

(b) It allows governments to use specialized skills absent in its own work force. It allows greater flexibility in adjusting programs as demand and revenues change. It makes experimentation easier. It avoids large, lumpy capital requirements. It permits exploitation of economies of scale by even small government entities.

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1/ See, for example, Fisk (1978), pp. 92 ff, and Savas, p. 89 ff.



(c) Contracting a part of the work provides a measure for comparison, and the cost of the service is visible in the cost of the contract. It thus increases the transparency of public sector operations.

These are very general advantages. Others peculiar to developing countries and to particular sectors are mentioned elsewhere in this paper. But, better than a listing of potential advantages and disadvantages, is the cumulative experience with government contracting, mostly anecdotal, which strongly suggests that large benefits are obtainable from government contracting of services to private suppliers. Savas, for example, assembles a large array of evidence indicating substantial gains in efficiency from privatization. 1/ Other writers have found similar gains. 2/

It is undeniable that risks and disadvantages exist, some of them especially pertinent to developing countries, particularly those relating to contract specifications and monitoring and to the dangers of corruption. But these problems are hardly absent when there is public delivery of services, and contracting skills can be developed over time. Moreover, in many cases, private delivery does not require a very complex and extensive role for the government as organizer and overseer. The advantages--and the problems--of government contracting of services to private "producers" are best illustrated by surveying experiences in one key sector--transportation--where experiments with contracting are relatively numerous.

#### 1. Private road construction

Much road construction in industrial countries after World War II was financed by private capital, but indirectly through revenue bonds floated in private capital markets; repayment arrangements frequently involved tolls. Direct private financing of road construction is rare but it is not unknown. For example, in the state of Texas, the major highway between Dallas and Fort Worth was built by private companies licensed to finance and construct the road, to operate it under a toll system until the investment was paid off with a suitable rate of return, and then to turn over ownership to the public. 3/ Comparable arrangements exist in other countries--in Spain, for example. The Transport Department of the U.K. Government would like to follow the same pattern--that is, to buy roads on credit, with contractors being paid "by some form of royalty related to the amount of traffic using the road." 4/ Road tolls cannot be used in the United Kingdom because alternative toll-free roads are so numerous that collection would be a problem, and

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1/ Savas (1981).

2/ Spann (1977) and Poole, Jr. (1980).

3/ U.S. Congress (1982).

4/ Taylor (1982).



the problem is exaggerated by the large number of intersections. Contractors want a guarantee, however, of a minimum rate of return, which means protection against a traffic flow lower than projected. The U.K. Treasury wants this risk to be borne by the private financiers. This and related differences make the outlook uncertain for roads built on such installment loans.

The private financing of roads is being tried on a sizable scale in Argentina—the pioneer in this respect in the developing world. 1/ Over US\$2 billion of road construction has been or may be privately financed in that country. The unusual aspects of this approach are that it involves social overhead capital generally regarded as unsuited to private financing or management and that it entrusts responsibility for financing construction operation and maintenance to a single contractor on a long-term basis. 2/

Feasibility studies for some of these roads projected reasonably high rates of return—12 per cent for the 25 de Mayo and Perito Moreno Thruways in Buenos Aires. The studies were completed a decade ago, however; as prices and price relationships have changed and construction costs are higher than estimated, the rate of return will be lower than projected.

The 25 de Mayo project has had a range of problems that illustrate the difficulties of the new approach. To assure the contractor's access to bank loans, both the Federal Government and the Buenos Aires Municipal Government had to guarantee most of the loan funds—70 per cent to 100 per cent of various cost items (e.g., equipment, labor, and materials). The Municipality also gave a minimum average daily traffic guarantee (85,000 light vehicle equivalent units), which was to rise slowly each year. With the specified toll rate (US\$1.00 in January 1982), this would allow the contractor to estimate the minimum revenue.

Three major problems arose. First, traffic was lower than projected—65,000 vehicle units a day instead of the guaranteed 85,000; but the contractual toll rate is fixed in real terms. Thus, the municipality is obligated to make up revenue shortfalls of about \$7.3 million a year.

Second, the cost of construction exceeded the estimated cost because of the high rate of domestic inflation and major changes in real foreign exchange rates. Escalator clauses (indexation) protected the project against rises in peso cost, but the Argentine peso was revalued upward during construction. As a result, contractor payments based on dollar estimates for construction costs fell short of needs by more than \$250

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1/ This account draws heavily on Ulin (1982).

2/ The 25 de Mayo and Perito Moreno Thruway projects were the first major public investments in Argentina financed entirely by foreign private capital.



million. Argentine public banks had to provide substantial short-term bridging finance, which was later converted to longer-term foreign debt. The present problem is how these loans will be repayed. If the relative price of the peso had stayed high, the contractor's peso revenues would have permitted repayment of the larger dollar obligation, but the peso has plummeted.

The Government is now considering raising real toll rates to increase revenue. In any event, if toll revenues do not increase substantially, loan repayment by the contractor will not be possible; the municipality of Buenos Aires and the Federal Government will have to pay the substantial sums required by their guarantees. The guarantee problem does not arise so starkly in the other road projects in Argentina; the Nueve de Julio Road, for example, seems to carry no federal loan guarantee, nor are tolls clearly specified. The contractor is guaranteed a minimum income in U.S. dollars, with an escalator clause for price rises. The city will disburse this over a 20-year period. These road projects, like other proposed private investments in infrastructure in Argentina (a new container port, for example), almost certainly result in greater investment than would otherwise occur. The size of the increment, of course, depends on whether the guarantees have to be met and on how they are financed. The productivity and social profitability of the roads and other privately financed infrastructures depend mainly on the extent to which risk is borne by the private investor, which in turn is mainly a function of guarantee arrangements. It is conceivable that this novel form of capital transfer could become simply a new version of supplier credit financing for poorly selected public sector projects.

## 2. Road maintenance: an example of contracting

Road maintenance has been subject to the greatest experimentation with contracting of this kind. Problems of staff incentives and general budget crises have always had severe effects on public works and highway agencies in developing countries, and these have been aggravated recently because these agencies are heavy users of fuel. The need to cut unit costs of maintenance has led some governments to try new approaches, particularly the use of private contractors for road maintenance. <sup>1/</sup>

Advocates of maintenance contracting stress the following benefits: (1) stronger incentives to cut costs; (2) greater flexibility in scaling resources to meet changing needs; (3) removal of the public sector burden for direct management of large and dispersed equipment fleets and work forces; (4) prevention of diversion of budgeted funds from maintenance to other uses; (5) creation of a wider political constituency for maintenance; and (6) better prospects for developing durable institutional capacity.

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<sup>1/</sup> Harral (1982).





Opponents say that contracting can raise costs because it is impossible to discharge redundant public sector employees; that contract negotiation and administration will require more people and more work; that competent contractors are too few and therefore the market for contractor services is too thin to be competitive; and that governments of developing countries are unable to manage contracts.

Some country experiences illustrate the potentials and constraints of maintenance contracting. In Yugoslavia, Brazil, and Argentina, results of a shift to maintenance contracting have been very positive. Yugoslavia started such arrangements in the 1950s. Its system is highly developed, with cooperative enterprises bearing responsibility for execution of contracts custom-tailored to specific tasks and with well-defined standards, levels of service to road users, work safety rules, and financial responsibilities. In Brazil, budget pressures, expressed in restrictive hiring and pay policies, led the Highway Department to contract maintenance which, until the 1970s, had been done entirely by the Department (i.e., by force account). The Highway Department continues to plan and manage overall operations, but production has been transferred to private contractors; the Highway Department's work force is one fourth of its 1973 size. In Argentina, a 1979 law required government agencies to reduce their work force. In response, the Argentine Highway Directorate turned over 70 per cent of its routine maintenance to contractors. In 18 months, responsibility for two thirds of the 47,000 kilometers of national road network was transferred to contractors.

An experiment in Colombia was less successful. In 1977 the Ministry of Public Works arranged four contracts for maintenance, but work programs were poorly defined. Specifications were left to contractors. No penalties were set down for noncompliance. The repayment arrangements did not work well either. The contractors were supposed to collect tolls as their only source of contract revenue, but poor estimates of traffic led to toll collections below the anticipated necessary income. Contractors also felt that the Government failed to meet its contractual obligations. Also, contractors concentrated on the most profitable maintenance elements, ignoring the rest. These and other problems related mainly to poor contract specifications generated unsatisfactory performance and much dispute. All four of these Colombian contracts ended up in court. The experience made clear the need for strengthening both contract planning and the capacity for supervision in the government.

However, limited experience and small contracting capacity need not hold back experimentation and progress in these activities, as experiences in Nigeria and Kenya suggest. In Nigeria, an initial effort in 1979 to contract maintenance for some 12,000 kilometers of paved federal highway was aborted because extreme variations in bid prices indicated that better specification of work was essential. A better prepared attempt followed in 1980. Work programs and performance standards continued to generate uncertainty among contractors, but 30 contracts



for 8,000 kilometers of road were nonetheless let, half to indigenous contractors and half to multinational contractors. Three seminars were held to discuss the performance of the contractors, which was apparently good enough to encourage the Government to extend the scheme to 16,000 kilometers of trunk roads in 1982; 60 per cent of the first group of contractors will be retained.

As an indication of contracting possibilities in the least developed countries, a recent Kenya experience is also noteworthy. Despite considerable external assistance, Kenya's road maintenance operations were generally unsatisfactory for staff reasons (shortage of skilled labor, high turnover of workers, poor incentives to work, and redundant unskilled workers) and for administrative and organizational reasons (budget inadequacies, cumbersome administrative procedures, etc.). The Roads Department in Kenya has, for some years, employed small African contractors to haul material for regravelling operations. Some of these contractors developed their capacity to the point that they can do full regravelling contracts, although help from the Roads Department is still needed. By 1980-81, they were able to deliver US\$5.2 million of regravelling work, accounting for 80 per cent of the country's total. These contractors are certainly being helped by Roads Department staff and often by development agency subsidies but they show that competence of this kind can be created in a reasonable time, if it is done consciously and gradually.

The authors of the survey from which the above accounts are taken, note that it is too early for many firm conclusions and that contracting to private parties involves risks. With respect to efficiency, however, they conclude:

"With rare exception, contract maintenance has proven to be a workable undertaking in countries at diverse levels of development and with diverse forms of social and economic organization. With relative freedom from entangling "red tape" and the ability to pay higher salaries to attract, retain, and motivate staff, contractors have in some cases, for example, in Nigeria, succeeded in getting maintenance done where all other approaches have failed. Where sufficient profit incentives exist, contractors are normally attracted to maintenance opportunities, even in remote areas; while larger firms tend to prefer larger contracts including periodic maintenance, in many instances, small firms have been formed specifically to undertake routine maintenance.

. . . It must be recognized, however, that the introduction to any new system, especially quickly and on a large scale, is risky. The Colombian experience illustrates some of the problems which can be encountered in introducing contract maintenance with inadequate planning and preparation. While the overall burden of responsibilities on the road authority is normally reduced by the



introduction of contractors, the nature of the government's responsibilities changes sharply, and there is increased need for contract management skills, for improved work planning performance monitoring, and more effective cost accounting in force account maintenance operations.

. . . initial cost results from Brazil, Argentina, and Kenya (and also the United States) suggests that contractors can perform maintenance at substantially reduced costs. The administrative costs to the government in contract management, quality control, measurement, and certification is normally substantially less than in administration of force account works, although the nature of the administrative burden is different and may require enhancement of contract management staff. In every case where contract maintenance has been used on a large scale continuing over time, government has been able to effect a substantial reduction of its own establishment.

Those who are familiar with the bloated payrolls and the vast fleets of equipment lying idle, which are characteristic of all too many road maintenance directorates, not only in developing countries, will require little evidence to convince them that contractors can perform maintenance at lower costs. However, many may question whether much of the potential cost savings would revert to the public. The best safeguard of the public interest is lively, open, and honest competition; where this is assured, large cost savings are likely to be realized . . . However, it must be recognized that the twin dangers of monopolization and corruption are ever present."

Urban services and transportation services by no means exhaust the possibilities open to developing countries in terms of government contracts for delivery of services by private parties. In the least developed countries, maintenance of rural wells might readily be subcontracted-- indeed, all maintenance activity lends itself to subcontracting. What is needed at this stage is more imagination and greater experimentation in devising ways to tailor the contracting to the specific needs and constraints of particular developing countries.

## VII. Conclusions

Better, more creative utilization of the private sector can make a significant contribution to economic growth and change in the coming decades. There is widespread agreement on this conclusion from all points on the ideological spectrum. In recent years many efforts have been made to harness the private sector more effectively, most of them in response to the problems created by rapid growth of the public sector in the 1970s, including negative impacts on incentives. Some of these efforts are described in this paper.



Private skill, energy, and savings can be mobilized in many different ways, of which only a few are considered in this paper. Nothing is said about deregulation except in the context of allowing more open markets. Nothing is said about large and important areas such as user charges or encouragement of foreign private investment. Some unusually interesting experiences, like those in postal services, are passed over. New approaches to social security are also ignored. These omissions are due to time and space constraints, rather than to neglect of their importance.

Divestiture of state-owned enterprises, which is often seen as a major instrument of privatization, has in fact been the subject of few experiments. The potential for selling commodity-producing state-owned enterprises to the private sector seems poor, except in limited circumstances. The benefits are usually small, whereas the political and economic costs are high. In modern manufacturing, ownership of equity is in any event often a relatively minor factor in determining efficiency of resource use. In industrial enterprises in developing countries, the public-private blend is particularly complex, and whether an industrial enterprise is "public" or "private" is usually less significant than the policy environment, which tends to be similar for both private and public enterprises in such basic determinants of performance as access to credit, wage policies, and market sheltering.

If divestiture by sale of equity is the least promising way to alter the private-public mix, the most promising is the provision of services, either directly or by government contracting. The advantages of resort to the private sector in these ways can be summarized as follows.

1. Privatization can make the public sector more efficient by allowing greater concentration or focus. It is a sensible general strategy for all hardpressed bureaucracies; proliferation of programs and activities disperses existing manpower and other resources and increases the need for coordination. The public sector can do its central tasks better if it is not burdened by tasks that are not so central. For example, less absorption in foodgrain marketing, in distribution of fertilizer, in running tomato canneries, or in selling matches would leave governments better able to build and operate railroads and power companies, improve health care and education systems, and administer and unify their national territories.

2. The private sector can improve the efficiency of public entities by competition and by making available to consumers alternative sources of supply. Where government monopolies exist, and scale economies are not compelling, use of private alternatives can be a significant spur to better public performance. This is perhaps most clear in the marketing of agricultural inputs and outputs and in retail trade generally. But, as noted earlier, it is also relevant in other key sectors, such as transportation.





3. Private provision of services mobilizes new resources, mainly increased individual effort, greater intensity of work, and the commitment of skills useful in the marketplace. As noted above, in trade and transportation--two sectors critical to growth in low-income countries--the technology typical of the small-scale private sector is particularly appropriate; it utilizes little capital and employs few formally educated people and many unskilled or informally trained people. Privatization in these sectors, therefore, has beneficial effects not only on output but also on income distribution and employment.

4. Areas of activity in which private agents are allowed to compete--with or without a public sector presence--are likely to be characterized by better services. This is especially true of small-scale activities, such as retail trade or personal services, sale of inputs to farmers, trucking, and urban transport. These activities are, by their nature, ill-suited to typically complex procedures of large-scale organizations, especially government bureaucracies. They are also areas where personal dedication and incentives are especially critical. But even if these factors are not strongly present, competitive provision of services leads to better services because it presents alternatives to consumers and producers, because it can make monopolistic inefficiencies more transparent, and because it dilutes power over buyers or sellers.

5. A more active private sector also allows the broader development of entrepreneurial abilities. Lack of indigenous entrepreneurs is frequently identified as a basic constraint to the economic growth of many developing countries. It is, in fact, difficult to envisage more rapid long-term development in the developing countries without more encouragement of entrepreneurship. Very little has yet been done in most developing countries to encourage the emergence of entrepreneurs; on the contrary, they have been discouraged. Leaving to the private sphere some of the activities now carried out by government would enlarge the scope for training in entrepreneurship.

6. Finally, the dispersion of economic authority brought about by a larger role for the private sector could contribute to the building of more decentralized and more democratic societies, for it represents a dilution of power and an opening of opportunity, which must in the end increase society's responsiveness to human needs.

For these reasons, the privatization of services is the policy area with the greatest potential in terms of lightening the public sector burden, increasing the efficiency of resource use, and stimulating growth. It is also rather a benign political issue (or at least much less explosive than divestiture) and more amenable to reasoned policy dialogue. It is, therefore, an especially appropriate vehicle for economic reform and is deserving of much closer attention than it has received in the past.



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7/3013

PS

FROM: A R H BOTTRILL  
DATE: 29 MARCH 1983

- 1. MR BEASTALL
- 2. MR KERR

INVITATION FROM MR CLAUSEN

I attach a draft reply for the Chancellor to send to Mr Clausen accepting his invitation to lunch on 28 September, which is the Wednesday of the IMF Annual Meeting. The other guests to be invited will be Finance Ministers from Summit countries and from Saudi Arabia and Kuwait.

*ABottrill*

A BOTTRILL

ENC

Mr Bottrill — cc Mr Anson (Washington)  
Rose Yung - for diary

Mr Anson has agreed to reply on  
the Chancellor's behalf, accepting.

*[Signature]*

29/iii





DRAFT REPLY TO MR CLAUSEN

Thank you for your letter of 9 March. I shall be  
happy to accept your invitation to lunch on 28 September.

GH



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THE WORLD BANK  
Washington, D. C. 20433  
U.S.A.

A. W. CLAUSEN  
President

HM TREASURY - MCU	
RECD.	21 MAR 1983
ACTION	Mr Bothwell ←
SIGNATURE	
REF NO.	0003482

March 9, 1983

Dear Sir Geoffrey:

I am writing today to confirm my invitation to you for an informal lunch on September 28th of this year at the time of our Annual Meetings in Washington. In addition to yourself the guests will be the Ministers representing the other six Western summit countries, as well as the Finance Ministers of Saudi Arabia and Kuwait.

All the Ministers who attended last year's lunch, which was an innovation, agreed in subsequent letters to me that they felt that such a small gathering was worthwhile and should be repeated. Recent consultation with your Executive Director has made it appear that the second day of the Annual Meetings, namely September 28th, would be the most convenient to the Ministers concerned.

I look forward to seeing you on that occasion and will in due course be in touch as to the possible subjects we might discuss, and the time and precise location of the lunch, which will be at the Sheraton Washington Hotel.

Sincerely,

The Rt. Hon.  
Sir Geoffrey Howe, P.C., M.P.  
Chancellor of the Exchequer  
Treasury Chambers  
Parliament Street  
London SW1P 3AG  
England

Chancellor ✓  
this is in the  
navy  
2. Mr Bothwell. M



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IMF: MANAGING DIRECTOR'S CONTRACT

1. KAFKA (DEAN OF THE BOARD) HAS CIRCULATED TO ALL EDS A DRAFT CONTRACT FOR THE MANAGING DIRECTOR TO RUN FROM 17 JUNE 1983. HE HAS CALLED A MEETING OF DIRECTORS FOR THURSDAY, 12 MAY TO DISCUSS IT. SINCE IT CONTAINS A SALARY REVISION, APPROVAL OF THE BOARD OF GOVERNORS WILL BE REQUIRED. DIRECTORS WILL MAKE A PROPOSAL FOR APPROVAL BY GOVERNORS VIA A POSTAL VOTE.

2. THE DRAFT HAS BEEN PREPARED BY A COMMITTEE OF DIRECTORS COMPRISING, IN ADDITION TO KAFKA, DE GROOTE, ERB, FINAISH, LASKE AND ZHANG. THE TERMS REMAIN THE SAME AS THOSE OF THE EXISTING CONTRACT EXCEPT FOR SALARY AND ALLOWANCE. THE DRAFT PROPOSAL IS FOR A SALARY OF DOLLARS 120,000 PER ANNUM, AND AN ALLOWANCE OF 55,000, BOTH TO BE REVIEWED AFTER 30 MONTHS. NEITHER IS SUBJECT TO TAX. THE ALLOWANCE IS NON-ACCOUNTABLE: THE MANAGING DIRECTOR IS ADDITIONALLY REIMBURSED FOR ENTERTAINMENT EXPENSE ACTUALLY INCURRED. THESE NUMBERS REPRESENT AN INCREASE OF 20% ON PREVIOUS SALARY AND 48.6% ON PREVIOUS ALLOWANCE, WHICH HAVE BEEN FIXED SINCE DECEMBER 1980. THE INCREASE IN TOTAL REMUNERATION IS 27.7%. THE US CONSUMER PRICE INDEX ROSE 25.8% BETWEEN JANUARY 1980 AND APRIL 1983.

3. THE PROPOSAL WOULD ESTABLISH TOTAL REMUNERATION OF THE MANAGING DIRECTOR AT 216% OF THE PROSPECTIVE TOTAL REMUNERATION OF ED'S (ASSUMING A 5% INCREASE FOR THE LATTER THIS YEAR) AND AT 194% OF THE PROSPECTIVE SALARY OF HIGHEST PAID STAFF MEMBERS (ALSO ASSUMING A 5% INCREASE), IE IN BOTH CASES BETWEEN THE MULTIPLES WHICH EXISTED AT THE BEGINNING OF THE MANAGING DIRECTOR'S CONTRACT AND AT THE TIME OF HIS DECEMBER 1980 INCREASE.

pas mal du tout !

4. THE COMMITTEE JUSTIFIED THE PROPOSAL AS FOLLOWS:  
QUOTE THE INCREASE PROPOSED IS HIGHER THAN THAT IN THE COST OF LIVING SINCE DECEMBER 1980. BUT IT SHOULD BE CONSIDERED THAT THE DRAFT CONTRACT PROVIDES FOR NO RECONSIDERATION OF THE MANAGING DIRECTOR'S SALARY FOR 30 MONTHS DURING WHICH TIME A NOT INCONSIDERABLE EROSION OF ITS PURCHASING POWER MUST BE EXPECTED. FOR INSTANCE, APPLYING THE CONSUMER PRICE INCREASE FOR THE UNITED STATES (3 1/2 PER CENT) OVER THE LAST 12 MONTHS, THE EROSION WOULD BE ABOUT 9 PER CENT, WHICH WOULD BRING THE PURCHASING POWER OF THE MANAGING DIRECTOR'S TOTAL REMUNERATION TO LESS THAN IT WAS AT THE TIME OF THE DECEMBER 1980 INCREASE. IT MUST FURTHER BE CONSIDERED THAT IN FEBRUARY 1983 THE UN SECRETARY GENERAL'S TOTAL REMUNERATION INCLUDING SALARY, REPRESENTATION ALLOWANCE, POST ADJUSTMENT AND THE ESTIMATED VALUE OF FREE HOUSING WAS DOLLARS 195,576 NET. UNQUOTE

5. KAFKA INDICATES THAT THE INCREASE IS ACCEPTABLE TO THE MANAGING DIRECTOR. THE FACT THAT HE AND THE OTHER COMMITTEE MEMBERS HAVE PUT THEIR NAMES TO THE DRAFT INDICATES THAT THEY, TOO, CAN GO ALONG WITH IT, AND I PRESUME THEY HAVE CONSULTED THEIR AUTHORITIES ALTHOUGH I DO NOT KNOW THIS FOR CERTAIN.

6. I AM NOT ENTIRELY HAPPY THAT PROVISION SEEMS TO BE BEING PROPOSED FOR COMPENSATION IN RESPECT BOTH OF PAST AND PROSPECTIVE INFLATION, ALTHOUGH THE ALLOWANCE FOR FUTURE INFLATION IS FAIRLY SMALL. HOWEVER, OUR OBJECTIONS WOULD NOT CARRY MUCH WEIGHT IF THE OTHER DIRECTORS, ESPECIALLY ERB (USA) AND LASKE (GERMANY), ARE PREPARED TO GO ALONG. RELEVANT HERE IS THAT ERB TELLS ME THAT SECRETARY REGAN WILL NOT VOTE AGAINST THE PROPOSALS WHEN IT IS PUT TO A POSTAL BALLOT. I RECOMMEND THAT WE ACCEPT THE PROPOSALS WHILE NOTING THE POINT ABOUT THE BUILDING IN OF INFLATIONARY EXPECTATIONS AND ADVISING AGAINST TOO CLOSE A CONNECTION WITH THE REMUNERATION OF HEADS OF OTHER INTERNATIONAL ORGANISATIONS.  
MAY I PLEASE HAVE GUIDANCE IN TIME FOR THE DISCUSSION ON 12 MAY.

7. FCO PLEASE ADVANCE TO PS/CHANCELLOR, LITTLER (HMT), LOEHNIS (BANK OF ENGLAND) AND APPELYARD (ERD). PLEASE DISTRIBUTE TO ADVANCE ADDRESSEES ONLY.

WICKS

OUT TELEGRAM

6/5/83

Classification and Caveats

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Precedence/Deskby

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IMF: Managing Director's Contract  
Your telno 181.  
2. We accept your recommendation that the contract (with salary revision) be accepted (para 6). We share your doubts about ~~preparing~~ proposing compensation for both past and prospective inflation. It is unwise to build in too explicitly inflationary expectations. However, in view of the fact that the US and Germany will be supporting the recommendation, our <sup>opposition</sup> ~~obligation~~ would not be effective. We would, moreover, not want to appear isolated especially since the Chancellor is the Chairman of the Interim Committee.  
3. We also agree that too close a connection with the remuneration of heads of other international organisations should be avoided. In practice, the salary ought to be fixed by indirect comparison ie by reference to the staff who are ~~themselves~~ themselves linked to the comparators rather

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FROM MR SHERIDAN  
DATE 10 May 1983

PS/CHANCELLOR



Mr Littler  
Mr Lavelle

IMF MANAGING DIRECTOR'S CONTRACT

On 9 March Larasiere, Managing Director of the IMF, accepted the offer made unanimously by the Executive Board that he should be reappointed. Subsequently a 'contract committee' of six Executive Directors<sup>h</sup> (as discussed with Larasiere the precise terms of his contract. The draft contract is to be discussed by the Executive Board on 12 May. We have to indicate our view of the contract at the Board and, since the contract contains a salary revision, a postal vote of the Board of Governors will also be necessary.

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3. The salary contains an element for prospective inflation which is justified on the grounds that the contract provides for no re~~comm~~ideration for 30 months. The provision for both past and prospective inflation is somewhat unwelcome but perhaps inevitable. The allowance for future inflation is, however, small.

4. Mr Wicks (UK DEL) suggests that we should agree the increase since we would be isolated in opposing it. Our objections would not carry weight since both the U.S and Germany are represented on the 'contract committee' recommending the increase. In the light of all the circumstances, it seems reasonable to agree the contract and I attach a draft telegram indicating our consent. I would be grateful if you could indicate whether this is acceptable. We need to send the instructions out tomorrow (11 May).

P T SHERIDAN



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~~UNITED KINGDOM TREASURY AND SUPPLY DELEGATION~~

BRITISH EMBASSY  
WASHINGTON, D. C. 20008

PPS

You can assure the Chieftains that the  
IWT pride themselves on avoiding  
leaks, but will certainly be on our  
toes.  
MAY 1976

ppp

M.A. Hall Esq  
Chief Information Officer  
HM Treasury  
London, England

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PPS

May 11, 1983

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David Parrott,  
Dr Hall.

IMF: WORLD ECONOMIC OUTLOOK

The IMF will soon publish its annual World Economic Outlook (WEO) and, as you know, it includes some material which, if it were published in an election period, might require answering.

2. For example, the WEO predicts rising inflation and rising unemployment for the UK in 1983 (page 55 of Section 1, Appendix A of the draft, on which we have already commented to the Staff). If anyone had tried to make political capital out of this, we could no doubt have pointed out that this is an independent forecast by the Fund Staff, done some months ago when the exchange rate was substantially lower than at present, and which has already been disproved to some extent by events. Reasonably convincing, but nevertheless of some potential embarrassment.

3. However, we now learn that the timetable has slipped (for technical reasons) and the Fund does not now expect to publish the report until "the middle of June". When we pressed the Associate Director of the Research Department (which produces and coordinates the WEO) to be more specific, Schwartz said it was extremely unlikely publication would be before June 9; there had been technical problems with the drafting and with the numbers. Given that the BIS would probably publish its annual report around June 12/13, the Fund could either try to shoot for about June 7, which Schwartz felt was quite unrealistic, or publish around June 15 or later.

4. Earlier indications of publication on May 25 (your note for record of May 3) have obviously had to be revised. In fact, we have only today received the last part of the draft report (dealing with oil, commodity prices, trade policies, and the statistical asymmetry on the global current account) asking for factual comments by May 24. Therefore, I feel publication later in May can effectively be discounted.

/5. If it does

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5. If it does look as if the WEO will appear before the election, we will let you know. But let me say now that there would be the gravest difficulty in trying to delay its publication for political reasons.

*Louis Mountbatten*

*Nigel Wicks*

Nigel Wicks

cc: Mr. E.P. Kemp (HMT)  
Mr. R.G. Lavelle (HMT)  
Mr. R.I.G. Allen (HMT)  
Mr. R.H. Gilchrist (B of E)

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FROM: J.G.LITTLER  
DATE: 12 MAY, 1983

MR. KERR

cc PS/Chief Secretary  
PS/Financial Secretary  
PS/Economic Secretary  
Mr. Middleton  
Mr. Burns  
Mr. Unwin  
Mrs. Hedley-Miller  
Mr. Lavelle  
Mr. Bottrill  
Mr. Peretz  
Mr. M. Hall

ADDRESS BY PRESIDENT MITTERAND

As you will have seen in the Press, President Mitterand chose to honour the Ministers present in Paris for the OECD meeting by an invitation to the Elysée on the evening of Monday, 9 May, and delivered to them an Address. This could have some bearing on Williamsburg, and I therefore thought it worth circulating the full text in French, attached, with the following comment and brief summary.

2. It was an offensive occasion. We were asked to be in place by 6-10 p.m. for a Reception at 6-30. In place meant standing, in a large semi-circle in country groups of between 2 and 4 for each country, around the edge of a large and ornate Reception Room, dominated by the Lectern which we faced and batteries of television cameras and photographers behind us and opposite the place where the Americans stood.

3. The President was nearly 15 minutes late; he briefly toured the semi-circle shaking hands with one or two from each country group, then went to the Lectern and delivered the attached Address, taking almost exactly 45 minutes. Madame Flesch (Luxembourg and President of the meeting) gave a 3 minute courtesy reply, after which we adjourned for a glass of champagne.

Main Points of the Address

4. After nearly 10 minutes of elaborate compliments to OECD and reference to the current crisis and the threat of panic, the President spoke of the three ideas which inspired his thoughts this evening: growth, stabilisation and development.

5. Under growth, he called attention to the need to reduce massive budget deficits and high real interest rates; he then urged those countries which have margins of manoeuvre to stimulate their own growth; he then offered the thought that the best way of

countering unemployment was to reduce working hours and educate youth in new technologies.

6. Under the heading of **stabilisation**, he spoke at length about exchange rates, making three main points:

- we should build on the three zones of \$, yen and European currencies;
- we needed a new Bretton Woods;
- he intended to propose an urgent high-level conference in the framework of the IMF, to promote a new and more stable exchange rate system.

He spoke very briefly against protectionism, with qualifications, and urged the stabilisation of commodity markets, the urgent completion of the Common Fund, measures to regulate futures markets and technical training.

7. Under the heading of **development**, he made a long list of demands for assistance for the South, emphasising the dependence of the North on the poorer half of the world. He spoke among other things of the need to relieve debt by lower interest rates and a lower \$value, of the need to develop forms of guarantee by international institutions to enable developing countries to borrow commercially; of the need for a new issue of SDR, linked with aid; of the need to ease conditions as well as increase amounts of borrowing from the IMF; of the need to extend the Stabex Scheme for commodities; of the need to increase aid at least to the UN target and of the need for an emergency plan for Africa.

8. He then had a passage commending the Community as a model for the world, particularly praising:


- the opening of frontiers;
- the "progression of agricultural prices"; and
- stability of exchange rates.

9. Finally, he made some minatory references to the Summit, indicating that he would advance the same kinds of ideas at Williamsburg as in this Address, that there must be a response to them, and that the utility of this type of meeting would be judged by the response.

#### Reactions

10. The United States was not, I think, mentioned by name even once. But President Mitterand looked at the United States Group during a large part of his Address, and the cameras focussed on them, as well as the President, to the exclusion of others. And a great deal of the message, and the choice of particular language and references, was plainly addressed against the United States. It was evident that the US representatives (Shultz, Regan, Brock and Wallis) were angry. When we finally adjourned, they lingered behind and had a short discussion together before rejoining the rest of the company and seeking out the President - while others, equally conscious of the tension, kept away.

11. My impression was that the President overplayed it considerably. Early the following morning, Madame Flesch referred briefly and neatly to the Address with which we had been surprised and edified the night before - and made no further comment. The Press do not seem to have taken the substance of the message seriously, although they may rightly have focussed on the implied threat to future Summit meetings. But we shall plainly have the same message again from the French President at Williamsburg.

  
(J. G. LITTLER)



PRÉSIDENCE  
DE LA  
RÉPUBLIQUE

SERVICE DE PRESSE

ALLOCUTION DE MONSIEUR FRANCOIS MITTERRAND  
PRESIDENT DE LA REPUBLIQUE FRANCAISE  
EN L'HONNEUR DES MINISTRES ET SECRETAIRES D'ETAT DES  
AFFAIRES ETRANGERES ET DES FINANCES DES PAYS  
MEMBRES DE L'O.C.D.E.

Palais de l'Elysée, lundi 9 mai 1983

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Madame la Présidente,  
Mesdames et Messieurs les Ministres,  
Monsieur le Secrétaire Général,

Laissez-moi vous dire le plaisir que j'ai de vous recevoir ici. Je ressens votre présence comme un honneur pour mon pays, vous êtes réunis ici à Paris pour examiner et pour travailler dans le cadre d'une institution internationale qui nous est proche et qui nous est chère.

Je voudrais au-delà de ces paroles d'accueil, saisir cette occasion qui m'est donnée pour indiquer selon la France, mais rejoignant sans doute la pensée de la plupart d'entre vous, les voies à suivre pour que nos travaux puissent déboucher sur un mieux être dans nos relations internationales et sur la nécessaire approche du temps qui vient, afin que la crise dont nous souffrons soit dominée.

J'espère que les conditions de travail et de réflexion qui vous sont offertes à Paris correspondent à vos besoins, mais c'est déjà une longue habitude dans cette ville que de recevoir et d'échanger. Vous avez appris vous-mêmes entre vous à vous connaître à travers les décennies précédentes. Notre organisation a pris rang, forme, a commencé de dessiner des perspectives d'avenir et, on peut le dire d'une façon générale, a réussi dans sa mission.

Je suis très heureux de vous rencontrer et je souhaite m'entretenir avec vous sur des thèmes que j'aurai l'occasion, je ne serai pas le seul, d'appréhender bientôt lorsque je me trouverai au Sommet de Williamsburg à la fin de ce mois.

Depuis 36 ans, votre organisation n'a cessé de participer à l'approfondissement des échanges entre grands pays industrialisés et de jouer un rôle important dans le dialogue et la coopération entre le Nord et le Sud. D'abord plaque tournante de la reconstruction de l'Europe dévastée, elle a ensuite, le temps de la prospérité revenu, élargi sa composition et le champ de ses intérêts.

Bref, l'O.C.D.E. permet à chacun de nos pays d'exprimer librement son point de vue et, quand s'affirment des désaccords ou des difficultés, de rechercher ensemble des voies nouvelles. Les débats qui se déroulent en son sein sont la conséquence directe de l'interdépendance dans laquelle nous vivons. Chacun perçoit mieux l'impact de ses propres choix sur l'intérêt commun.

Le travail accompli par l'O.C.D.E. fait honneur à tous. Et je suis heureux d'avoir l'occasion de lui rendre cet hommage. Mais, vous le savez, et aujourd'hui comme après la dernière guerre mondiale, le monde est à reconstruire et nous avons besoin pour cela de retrouver l'esprit qui animait les fondateurs de l'organisation. Il ne suffit pas de gérer le quotidien. Sans perspectives claires, sans règles du jeu, nous ne sortirons pas de la crise.

Rappelez-vous, au début des années soixante-dix, l'affaiblissement des disciplines monétaires, la créations incontrôlée de liquidités internationales a entraîné une première vague d'inflation. Puis la généralisation des changes flottants a accru l'instabilité des parités et multiplié les tensions inflationnistes, et le second choc pétrolier a entraîné une sévère récession aggravée par les mouvements erratiques de certaines monnaies sur les marchés internationaux.

Pour y remédier, de nombreux pays se sont engagés, sans se concerter, dans des politiques dont le cumul désordonné a entraîné l'économie mondiale dans le cercle vicieux de la récession. Le chômage a augmenté de façon dramatique de 25 millions dans nos seuls pays. Le protectionnisme multiple et dissimulé a ralenti la progression du commerce mondial, ce qui a freiné, à son tour, la croissance.

Dans les principales économies, le déséquilibre des finances publiques a maintenu les taux d'intérêt réels à un niveau beaucoup trop élevé, sans précédent depuis trente ans, diminuant de la sorte la capacité d'investir, et dressant de nouvelles barrières au moment où la technologie permettait d'avancer. Tandis que s'éloignent ainsi les chances de l'avenir, le poids du passé grandit : la charge de la dette s'accroît, écrase un plus grand nombre de pays et d'individus, ralentit le mouvement des échanges.

Bref, Mesdames et Messieurs si l'on n'y prend garde, le monde entier sera à la merci d'une panique ou d'une mise en défaut.

Que faire alors ? C'est bien l'objet de vos travaux et de ma réflexion. L'expérience nous apprend que ni les forces du marché, ni le jeu des institutions n'ont jusqu'à présent réussi à dominer la crise.

Certes, depuis le mois d'août 1982, la coopération entre les institutions financières internationales, les autorités monétaires et le secteur bancaire a évité le pire. L'élargissement des quotas du F.M.I. et le renforcement des accords généraux d'emprunts ont accru les ressources disponibles afin de soutenir les pays les plus pauvres.

Mais éviter le pire n'est pas une ambition.

Si les grands pays comprennent leur devoir, nous sortirons bientôt et ensemble de la crise, mais à cette condition.

Mais cela ne se fera pas par miracle, ni en une seule conférence, ni en une seule année, ni dans le cadre d'une seule organisation. Cela résultera d'une action internationale durable autour du plan mondial que j'appelle de mes vœux.

Tâche immense, à l'échelle d'une génération. Et il nous appartient à nous qui sommes réunis ici même, d'y préparer les esprits et de lancer le mouvement.

A cette fin, j'émettrai trois propositions .

Vous savez mieux que personne que les relations d'échange ont besoin d'un moteur à deux temps: l'affirmation des différences et la coopération. Sans différence, pas d'échange utile. Sans coopération, pas de croissance durable.

Cette observation commande les trois orientations qui inspirent ma démarche ce soir : la croissance, la stabilisation, le développement.

Pour y parvenir, Mesdames et Messieurs, il conviendra d'agir avec ambition et discipline. Sans effort, que vaut une ambition. Sans projet d'avenir à quoi sert une discipline?

Eh bien, je crois qu'il faut retrouver ensemble le chemin de la croissance. Rien de grand ne se fera sans esprit d'entreprise, sans foi en l'avenir. Mais pour commencer, le premier pas de la remise en marche ne sera possible que par la croissance concertée, qui créera les conditions d'une reprise saine et continue, je veux dire sans inflation. Sachant ce que je sais des problèmes qui restent à résoudre dans un pays comme le mien, je le dis avec d'autant plus de force et de conviction.

La reprise qui s'annonce, ici et là, s'essouffera très vite, beaucoup plus vite qu'on ne le croit, si rien ne la soutient.

Ce qui nous ramène à trois données de base :

- 1°) personne ne conteste la nécessité d'une réduction massive des déficits budgétaires excessifs qui incitent à des taux d'intérêts réels exagérés et qui réduisent de ce fait les capitaux disponibles pour l'investissement. Plus les pays sont importants, plus ces déficits sont dangereux pour eux et pour les autres.
- 2°) Dans le même temps, il appartient à ceux qui disposent de marges de stimuler leur propre croissance. De beaux résultats dans le domaine de la lutte contre l'inflation doivent conduire à relancer l'activité économique.
- 3°) Enfin, la meilleure façon de lutter contre le chômage, vous le savez, est de former les jeunes aux nouvelles technologies et d'assouplir la durée du travail.

/...



Pour atteindre une croissance durable, les meilleures recettes économiques ne sauraient cependant suffire ; il faut d'abord et avant tout retrouver, j'y insiste, la confiance en soi, dans l'avenir de notre civilisation, dans nos valeurs communes et donc dans notre aptitude à créer et à travailler ensemble. C'est pourquoi, rien ne me paraît plus important que cet échange permanent entre nous comme ce soir, comme la journée d'aujourd'hui, ou la journée de demain. Tel est l'objet en tout cas de mon propos, ce soir, et de celui que je tiendrai dans quelques semaines aux Etats-Unis d'Amérique où je me trouverai avec les représentants de quelques autres pays. Et là j'aurai l'occasion de revenir sur les thèmes que j'évoque avec vous ce soir.

Il faut aussi, Mesdames et Messieurs, stabiliser les échanges. Le retour à une croissance soutenue restera irréalisable sans la reconstruction patiente d'un système stable de relations économiques internationales, dans trois domaines essentiels : la monnaie, le commerce et les matières premières. Mais je conclurai, d'une façon illogique puisque c'est pour commencer en rappelant la nécessité d'un nouveau Bretton Woods, même si l'évocation de ce nom ne doit pas nous conduire à l'invitation pure et simple.

On l'a bien vu au lendemain de la seconde guerre mondiale, tout commence par la monnaie. Retrouver les conditions d'un système monétaire stable, avec des monnaies qui soient suffisamment fixes, de valeur économiquement raisonnable, est donc une tâche urgente. Et ce n'est pas hors de notre portée, à condition de le vouloir, mais je pense que les étapes qui conduiront très progressivement à l'établissement d'un tel système monétaire international peuvent être parfaitement définies.

Je rappellerai que nous avons, en premier lieu à poursuivre l'effort entamé l'an dernier à Versailles et à mettre en oeuvre rapidement des dispositions que nous y avons prises. Une concertation effective entre les politiques économiques des pays industrialisés devrait être recherchée et renforcée : vous êtes, Mesdames et Messieurs les Ministres orfèvres en la matière. De tels échanges porteraient également sur les objectifs recherchés par la politique monétaire et sur les tendances de fond affectant les taux de change.

/...

J'indiquerai ensuite qu'il faudra s'attacher à retrouver des parités réalistes et à limiter les fluctuations erratiques à court terme autour des taux de référence. On étudiera, en outre, les moyens d'agir en commun pour mieux ajuster les taux à moyen terme, lorsque s'écartent durablement les paramètres économiques fondamentaux des principaux pays, à savoir les prix, les taux d'intérêt et la balance des paiements.

Je sais que cet effort paraîtra à certains impossible dans notre monde instable. Et pourtant, ainsi que le montrent les conclusions du groupe de travail sur les interventions dont la France avait prôné la création l'an dernier à Versailles, la concertation monétaire se révèle vite utile quand s'affirme le désordre sur les marchés, quand s'accélère la volatilité à court terme des taux de change. Ne sommes-nous pas dans une telle situation aujourd'hui même ? Les sept, pour ne parler que d'eux - ils ne sont qu'un élément dans l'ensemble - n'ont-ils pas affirmé au surplus leur volonté de mettre en oeuvre des interventions coordonnées dans les cas où leur utilité serait reconnue ? Sinon, à quoi bon multiplier les réunions internationales ?

Dans un contexte de taux de change stabilisés, les échanges commerciaux connaîtront un essor nouveau, j'en suis sûr, dont chacun tirera avantage ; les taux de croissance s'élèveront raisonnablement et la coordination de nos politiques économiques sera facilitée.

Alors, on ira plus loin et les trois principales zones monétaires, le dollar, le yen et les monnaies européennes pourront s'engager dans la voie du renforcement de leurs liens, et servir de pôles à la stabilisation des taux de change des principales monnaies du monde. Le Fonds Monétaire International verra son rôle renforcé, pour promouvoir l'usage des D.T.S. dans les réserves officielles, dans les opérations et les comptes des institutions internationales, et les transactions privées. Doté de moyens, il pourra intervenir en cas de difficulté grave et subite d'un pays donné.

Oui, je le crois vraiment et je le répète volontairement, le moment est venu de penser à un nouveau Bretton Woods. Je ne veux pas exagérer mon propos et reprendre l'expression fameuse : hors d'une telle proposition il n'y aura pas de salut. A cette époque, en partant de rien je veux dire au lendemain de la dernière guerre mondiale, on avait mis en place un système cohérent. Si tout est

aujourd'hui plus complexe, il ne faut pas pour autant renoncer à avancer, par étapes, vers un système adapté aux conditions économiques de cette fin de siècle.

En vue, Mesdames et Messieurs, de faciliter ces réformes, je souhaite que soit organisée après une soigneuse préparation la réunion d'une conférence monétaire internationale au plus haut niveau, dans le cadre du Fonds Monétaire International.

Et je crois qu'il faut organiser le commerce des biens ainsi que la coopération technologique. Après avoir parlé de la monnaie, eh bien oui, je parlerai des biens eux-mêmes. Le protectionnisme, dont chacun se méfie lorsqu'il s'agit des autres, constitue sans doute et par définition un obstacle à la croissance des échanges et à l'essor des pays pauvres. Encore en faut-il situer l'importance.

A l'heure actuelle, le protectionnisme ne représente que 10 % du manque à gagner des pays en voie de développement, tandis que 90 % sont dus à l'absence de croissance dans les pays riches, à l'insuffisance de l'aide publique, à l'instabilité du cours des matières premières et surtout à la hausse des taux d'intérêt, dont le supplément de charge soit 45 milliards de dollars\* représente près du double de l'aide versée à ces pays, soit 26 milliards.

Si j'insiste auprès de vous ce soir, ce n'est pas au risque de vous attarder, c'est pour vous dire ces choses au nom de mon pays qui ne détient pas la vérité mais qui entend contribuer à la réflexion commune. Quelle circonstance plus solennelle avais-je pour le dire à l'ensemble des pays du monde?

\*dont 29 milliards sont dus directement à la hausse des taux, le reste étant dû à l'augmentation de l'encours

Il est temps de remédier aux principales causes du mal et de démontrer que nul n'aura rien à gagner à ce protectionnisme, y compris le plus masqué, celui des normes techniques ou sanitaires. Cela se fera notamment en assurant une ouverture équitable des marchés, condition de la croissance économique, pour le Nord comme pour le Sud. Au demeurant, le GATT joue déjà son rôle pour stimuler les flux des échanges et contribuer à résoudre les difficultés résultant des différences de structures ou de rythmes d'évolution des économies. C'est bien; ce n'est pas suffisant.

Mais, seulement, vous le savez, on n'échange plus seulement des objets, on échange aussi des savoirs, c'est-à-dire des technologies. De plus en plus souvent la coopération industrielle entre les nations différentes remplace le simple commerce des produits de chaque nation.

L'intensification des échanges et de la coopération internationale en matière de recherche avancée et de technologies progressera entre les entreprises privées et entre les institutions publiques.

Le renouvellement de la coopération technologique commande en effet une autre division internationale du travail. Nous avons tous intérêt à éviter une compétition excessive, que ce soit entre les secteurs en déclin ou entre les industries nouvelles. Nous devons nous attacher à dégager progressivement quelques règles de conduite en matière de stratégies et de politiques industrielles.

Et puisque j'ai parlé tout à l'heure du Nord et du Sud et de leurs relations compliquées, incertaines, variables, comment ne pas parler de la nécessaire stabilisation à moyen terme des échanges de matières premières!

Or, plus nous y pensons, plus nous comprenons que l'on peut engager des actions rapidement, je vous en donne quelques exemples :

- n'est-il pas possible de conclure partout où c'est possible des accords de produits? Ces accords tendront à stabiliser les cours dans une fourchette réaliste, car on ne peut lutter indéfiniment contre les tendances lourdes du marché, cela nous le savons. Et comme les moyens financiers sont indispensables, j'insisterai sur la nécessité de donner vie sans autre délai au Fonds commun des produits de base dont on parle beaucoup et qu'on ne voit jamais.

- régulariser les marchés à terme. Cela me paraît aussi une priorité car ces marchés informent les opérateurs en déterminant un prix unique. Ils protègent les producteurs contre les spéculations. Lorsqu'ils n'existent pas, comme pour le riz, le désordre règne : infinité de prix, spéculations dans l'ombre, manipulations permanentes. Mais lorsqu'ils ne sont pas régularisés, au lieu d'informer, ces marchés trompent. Au lieu de protéger, ils accablent et poussent à la spéculation. Bref, une discipline plus stricte dans le jeu de la concurrence rendra à ces marchés le rôle qui leur revient.

- pour que le Sud puisse être partie prenante dans cette réorganisation des marchés, une action de formation, de formation des hommes, s'impose avec ceux qui déjà sont nos partenaires et le seront plus encore dans un monde plus ouvert. En relation avec les dispositions des accords de Lomé, dont nous mesurons chaque jour l'importance, il conviendra de mettre en oeuvre un programme de formation des ressortissants du Tiers-Monde à nos techniques de commercialisation. C'est ce que nous essayons de faire pour notre part, je sais que d'autres pays, ici représentés, ont de remarquables réussites.

- enfin, le financement des investissements en matière d'énergies non-renouvelables dans les pays en développement doit continuer d'être encouragé, en particulier dans le cadre de la Banque Mondiale ou bien sous la forme d'une institution spéciale à créer, mais la Banque Mondiale a déjà émis des projets qui peuvent servir grandement à la réponse à cette question.

Voyez-vous, j'insisterai sur ce point qui occupe nos pensées : rien n'est possible pour le Nord si la relance n'est pas assurée pour le Sud. Comment imaginer que nous pourrions sauver une moitié de la planète sans l'autre ? Comment vouloir dans le même temps libérer les échanges et cloisonner les solidarités ?

Nous savons tous que seule la reprise, la renaissance économique, règlera nos propres problèmes, par l'ouverture de nouveaux marchés et l'exploitation de nouvelles ressources. Et cependant, par un inacceptable paradoxe, nous prétendons ignorer les marchés les plus évidents, les plus avides de croissance, ceux du Tiers-Monde.

Politiquement, j'en ai la conviction, il en va de la survie de nos démocraties et de notre capacité à faire vivre un monde libre autour de nous. Aucune relance, aucun système monétaire, aucun système d'échange ne sera stabilisé si la situation économique et financière des pays du Sud n'est pas débloquée. Si ces pays n'ont pas des moyens durables sérieux de financer leurs dettes et de promouvoir leur croissance, leur équilibre politique sera de jour en jour plus menacé. C'est déjà très souvent le cas. Il nous appartient de contribuer à leur développement.

Et pour cela, aménager les financements à partir de leurs besoins. La hausse des taux d'intérêt et la récession mondiale alourdissent l'endettement des pays pauvres. Cet endettement ne menace pas qu'eux-mêmes, il est tragiquement dangereux pour le monde tout entier. Notre intérêt bien compris est d'alléger la dette du Sud. Il est essentiel pour tous les pays d'abaisser les taux d'intérêt réels qui sont la première cause d'aggravation du coût de l'endettement des pays du Sud. Au-delà, la situation, les perspectives deviendraient différentes, les pays les plus avancés ayant largement recours au marché financier privé tandis que les pays à bas revenus n'ont accès qu'à des aides publiques.

.../...

Pour les pays du Sud en cours d'industrialisation, je crois que des institutions multilatérales accordant leur garantie ou, au moins, leur soutien, à certaines ressources venues du secteur privé se révéleront de jour en jour plus nécessaires, cette garantie s'appliquant en priorité aux échéances longues de prêts supplémentaires.

Et pour les pays les plus pauvres, la part des pays développés dans l'émission d'une nouvelle allocation de DTS pourrait servir à bonifier leurs prêts conditionnels au Tiers-Monde, par l'intermédiaire des institutions financières internationales, afin d'assurer une gestion raisonnable de la dette de ces pays.

Depuis la réforme de 1975, les montants disponibles, du fait de la "facilité" du Fonds Monétaire International, ont atteint un niveau respectable, et c'est très bien ainsi. Mais l'ampleur des moyens est encore insuffisante. A cet égard, je l'ai noté, l'augmentation récente des quotas du FMI constitue un pas important. Mais il ne faudrait pas, dans le même temps, qu'une sévérité accrue des procédures limite l'emploi de cette nouvelle ressource, vitale pour de nombreux pays en développement.

J'ajoute que le rôle de la Banque Mondiale devrait être largement accru et diversifié en fonction des besoins des emprunteurs. Il serait opportun de modifier, je le crois, les ratios et d'augmenter significativement le montant du capital de la banque elle-même, en 1985, afin de lui permettre de faire face aux besoins des pays les plus pauvres.

D'une manière générale, j'insisterais sur l'importance de la stabilité dans le temps des engagements financiers, en matière d'aide et de crédits : comment monter des projets importants, je vous le demande, sur la base de financements annuels ? Comment les plus pauvres peuvent-ils établir des stratégies si l'apport extérieur est imprévisible au-delà de l'année en cours ? Un élément essentiel de la Convention de Lomé entre la Communauté Economique Européenne et soixante pays en voie de développement a été de garantir le financement sur cinq ans. La pluriannualité de l'aide est essentielle et il faut, je le crois, s'inspirer de cet exemple.

Il faut agir de façon spécifique pour les pays les plus démunis.

Il devrait être possible de desserrer les contraintes de la dette de ces pays en leur permettant d'emprunter à des conditions plus souples des sommes très supérieures au montant de leur quota. En outre, une part des allocations nouvelles de DTS pourraient être utilisée à abaisser nettement le coût de ces concours.

Un autre type de protection spéciale existe déjà pour ces pays et fonctionne dans le cadre du STABEX de la Convention de Lomé. La première priorité est de le consolider. Lors de la Conférence de Paris sur les pays les moins avancés, tenue en 1981, des engagements ont été pris pour l'extension de

cette garantie STABEX à l'ensemble de ces pays. Cette voie doit être poursuivie. Des propositions intéressantes ont été faites en ce sens dans la perspective de la CNUCED et lors de la réunion des pays non-alignés.

Un effort supplémentaire d'aide s'impose en faveur des 36 pays les moins avancés, dans le cadre des suites de la Conférence de Paris et sur la base des programmes de développement établis et révisés par les consortiums de pays donateurs. Il y a là un devoir que les pays ici rassemblés sont appelés à accomplir. Chacun de nous doit faire ce qu'il peut pour atteindre au plus vite les niveaux d'aide recommandés par les Nations Unies.

Enfin, il faut que soit lancé un "Plan d'urgence pour l'Afrique", dont le Produit national brut par tête stagne depuis dix ans et qui, compte tenu de ses dettes, menace de devenir le "continent perdu du développement". Un effort exceptionnel de solidarité des pays occidentaux est urgent. Mon pays fera des propositions détaillées à ce sujet bientôt. Nous avons trouvé bien des exemples où certains d'entre vous ont marqué de l'imagination, de l'audace. Nous avons souvent à nous inspirer de qu'ils font, mais nous apporterons nous-mêmes notre contribution.

Relancer, stabiliser, développer, voilà ce qui nous permettra d'organiser la reconstruction de l'ordre économique international; reconstruction à laquelle je ne peux que vous inviter ce soir par la parole, mais dont les actes sont nécessaires, et ils dépendent de vous.

Le tableau d'ensemble que je viens d'esquisser, à très larges touches, ne répond pas à toutes les nécessités du moment. C'est délibérément que j'ai insisté sur la relation Nord-Sud, en soulignant l'inter-relation fondamentale, économique et politique, qui existe désormais entre le sort de ces pays, et le nôtre. Je vous le dis gravement, tout passe par là.

J'ajouterai simplement, pour en finir, qu'il ne s'agit pas dans mon esprit de formules abstraites ou de visions utopiques. Ce sont en effet des principes que nous appliquons déjà, autant que possible, au sein d'une communauté restreinte mais enfin importante, la Communauté des Dix, ici représentée. La signification de mon appel auprès de vous, Mesdames et Messieurs, elle vient précisément de l'expérience quotidienne de ces dix pays. Certes, cette expérience, nous le savons bien nous qui en sommes, est souvent décevante, surtout lorsque nous considérons les difficultés plutôt que le chemin parcouru. Mais en fin de compte, par-delà ses crises, cette Europe sait qu'elle est appelée à plus d'identité, à plus de responsabilité, à plus d'unité. Elle sent que l'ouverture équitable de ses frontières, la progression de ses prix agricoles, la stabilité relative de ses taux de change lui profitent. Quand les Européens l'oublient, le reste du monde, d'une façon ou d'une autre se charge de le lui rappeler et, au fond, c'est très bien ainsi. Cette Europe se doit donc d'être plus

forte et plus unie, pour elle-même et pour l'exemple qu'elle donne au monde. Nous aurons l'occasion, certainement, d'en reparler, et particulièrement lors d'une rencontre déjà programmée pour le mois de juin à Stuttgart.

Mesdames et Messieurs, au risque d'accroître votre fatigue en cette fin de journée - mais quelle autre occasion me serait-elle donnée pour rencontrer au même moment tant de grands et vrais responsables de la politique économique dans le monde? - j'ai essayé de vous parler ce soir un langage qui est le mien, que je voudrais être celui de la vérité, mais surtout de l'espoir. La crise, nous la vivons, nous en souffrons, elle est là, profonde, multiforme. Elle nous appelle à un dépassement collectif, au rassemblement de nos énergies, dans chacune de nos nations comme à l'échelle du monde. Seulement nous le pressentons plus confusément, sans toujours en tirer les conclusions indispensables. Or, l'avenir n'est pas fermé. Il n'a jamais été fermé à travers tous les temps. Il dépend de notre ambition, de notre coopération. Une action mondiale pour la reconstruction de l'ordre économique est possible. Il y faudra du temps, oui, mais enfin, des années, oui, mais enfin, beaucoup de moyens financiers, mais enfin, si nous n'agissons pas par ces moyens, par des réformes, par des accords, par la concertation, à quoi aboutirons-nous? Et comment pourrions-nous hésiter à utiliser au mieux les immenses potentialités créées par le génie de l'homme dont nous sommes aujourd'hui porteurs?

Il est clair que le temps presse. Nous ne pouvons pas nous permettre de perdre des occasions. Je vous ai parlé des réunions européennes, et se profile un Sommet des pays industrialisés; nous pourrions vérifier à ces occasions si nous sommes sur la bonne voie ou bien si nous nous y refusons, choisissant l'anarchie et la crise plutôt que le redressement. Chacun en tirera les conséquences qu'il souhaitera, et appréciera à cette mesure l'utilité de ce type de réunion.

L'essentiel tient, par-delà nos différences, à une commune disposition d'esprit, à une volonté, à une mobilisation de nos chercheurs, de nos entreprises, de nos jeunes, de nos responsables. C'est à ce prix, vous le savez, que nous pourrions créer, ensemble, un monde plus civilisé, plus libre et plus tolérant. Et qui doute parmi vous, Mesdames et Messieurs, que c'est là l'objectif fixé par nos peuples mêmes? Si nous sommes associés, rassemblés dans cette salle, c'est parce que la preuve a été faite que le monde s'inspire des principes de liberté et de travail, de progrès et de paix, et a su en d'autres temps dominer l'évènement. Je voudrais que ma conviction soit unanimement partagée, cela est à notre mesure, à la vôtre, Madame, Mesdames et Messieurs.



Vous nous en apportez chaque jour la preuve par le sérieux et l'importance de vos travaux.

Je vous souhaite cette fois-ci de les poursuivre en recherchant toujours la conciliation nécessaire, et je répèterai ce que j'ai dit pour commencer : vous nous honorez, Mesdames et Messieurs, en étant nos hôtes pour la reconstruction de l'ordre international. Vous êtes ici à Paris et en France chez vous. Vous y êtes les bienvenus. Oeuvrons pour le bien de tous. Je crois bien que c'est votre loi. Merci



# INTERNATIONAL MONETARY FUND

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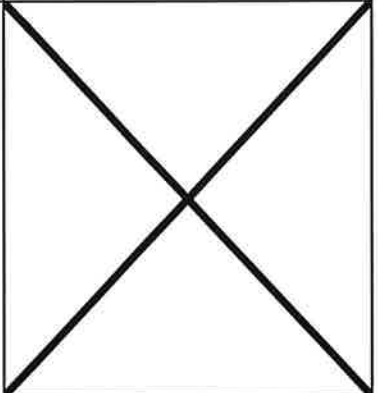
PRESS RELEASE NO. 83/33

FOR IMMEDIATE RELEASE  
May 12, 1983

Jacques de Larosière has been appointed to a second five-year term as Managing Director of the International Monetary Fund and Chairman of the Executive Board. His present term expires on June 16, 1983.

Attachment



DEPARTMENT/SERIES ..... T 639 ..... PIECE/ITEM ..... 187 ..... (one piece/item number)	Date and sign
Extract details: <i>Reference dated 12/05/1983</i>	
CLOSED UNDER FOI EXEMPTION (S.40(2))	<i>E. Barton</i> 16 102 116.
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**Instructions for completion of Dummy Card**

Use black or blue pen to complete form.

Use the card for one piece or for each extract removed from a different place within a piece.

Enter the department and series,  
eg. HO 405, J 82.

Enter the piece and item references, .  
eg. 28, 1079, 84/1, 107/3

Enter extract details if it is an extract rather than a whole piece.  
This should be an indication of what the extract is,  
eg. Folio 28, Indictment 840079, E107, Letter dated 22/11/1995.  
Do not enter details of why the extract is sensitive.

If closed under the FOI Act, enter the FOI exemption numbers applying to the closure, eg. 27(1), 40(2).

Sign and date next to the reason why the record is not available to the public ie. Closed under FOI exemption; Retained under section 3(4) of the Public Records Act 1958; Temporarily retained; Missing at transfer or Number not used.



INTERNATIONAL MONETARY FUND  
WASHINGTON, D. C. 20431

CABLE ADDRESS  
INTERFUND

May 16, 1983

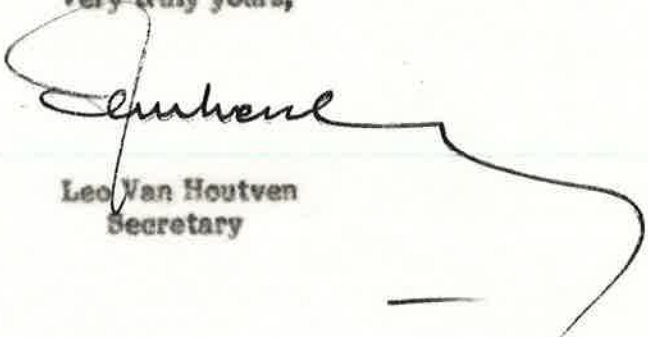
Sir:

I have been authorized and directed by the Executive Board to send to you the enclosed Report of the Executive Directors on the salary of the Managing Director proposing a Resolution for adoption by the Board of Governors without meeting, pursuant to Section 13 of the By-Laws of the Fund.

To be valid, votes on this Resolution must be cast by Governors or Alternate Governors, and must be received at the seat of the Fund on or before 6:00 p.m., Washington time, on June 13, 1983. Votes received after that date and time will not be counted.

It would be appreciated if you would transmit this communication to the Governor of the Fund representing your country with a request that he vote on the proposed Resolution. No particular form of vote is required so long as the Fund receives a clear indication as to whether the Governor approves or disapproves the proposed Resolution; such communication should be signed by the Governor or Alternate Governor or there should be a clear indication that it is sent on his behalf.

Very truly yours,



Leo Van Houtven  
Secretary

Enclosure

The Rt. Hon. Lord Richardson  
of Duntisbourne, M.B.E., T.D., P.C.  
Governor  
Bank of England  
London, EC2R 8AH, England

INTERNATIONAL MONETARY FUND  
WASHINGTON, D.C. 20421



May 14, 1963

Dear Sir:

I have been authorized and directed by the Executive Board to send to you the enclosed report of the Executive Director on the subject of the proposed amendment to the Articles of Agreement for the Fund. The Board has decided to recommend that the Fund be amended to provide for the election of the Executive Director by the Board of Governors without requiring a two-thirds vote of the Board of Governors.

To be valid, votes on this resolution must be cast by Governors or Alternate Governors, and must be received at the seat of the Fund on or before 5:00 p.m., Washington time, on May 13, 1963. Votes received after that date and time will not be counted.

It would be appreciated if you would transmit this communication to the Governor of the Fund representing your country with a request that he vote on the proposed resolution. In particular, your vote is requested so long as the Fund receives a clear indication as to whether the Governor supports or opposes the proposed resolution and whether a ballot should be filed by the Governor or Alternate Governor in this regard. It is requested that you indicate clearly on the ballot.

Very truly yours,

Paul G. Hoffman  
Director

Respectfully,

The Rt. Hon. Lord Richardson  
of Southdown, M.B., F.R.S., F.R.C.  
Governor  
Fund of England  
London, W.8A 9AT, England



Report of the Executive Board to the Board of Governors  
and Draft Resolution on the Salary of the  
Managing Director

1. Article XII, Section 2(i) of the Articles of Agreement states that the salary of the Managing Director shall be determined by the Board of Governors. Board of Governors Resolution No. 36-1, adopted January 30, 1981, provides that the annual salary of the Managing Director shall be US\$100,000, effective December 17, 1980. It is now proposed to adjust the salary of the Managing Director to US\$120,000 per annum to take account of the developments since 1980. The Executive Directors propose again to review the salary after 30 months.

2. Section 14(c) of the By-Laws provides for the reimbursement of reasonable expenses incurred by the Managing Director in the interest of the Fund. In accordance with their contracts with the Fund, the Managing Directors have been reimbursed certain specific expenses and have been receiving a nonaccountable allowance for housing and general representation. The Executive Directors have established this allowance at US\$55,000 per annum, effective June 17, 1983.

3. The other provisions of this contract remain the same as under the present contract.

4. Accordingly, the Executive Board of the Fund has approved the submission of the following Resolution to the Board of Governors of the Fund for a vote without meeting pursuant to Section 13 of the By-Laws:

RESOLVED, that effective June 17, 1983, the annual salary  
of the Managing Director of the Fund shall be one hundred twenty  
thousand United States dollars (US\$120,000).





INTERNATIONAL MONETARY FUND  
WASHINGTON, D. C. 20431

map

CHEQUE  
19 MAY 1983  
Mr Lippard  
Mr Upwin  
Mr Bavelle  
Mr Bottrill  
Mr Carey. Mr Bonney.

CABLE ADDRESS  
INTERFUND

May 16, 1983

Sir:

I have the honor to transmit herewith a copy of a communication, which has been sent today to all members of the Fund, submitting a Resolution on which Governors are requested to vote.

Very truly yours,

Leo Van Houtven  
Secretary

Enclosure

Rt. Hon. Sir Geoffrey Howe, Q.C., M.P.  
Governor of the International  
Monetary Fund for the  
United Kingdom  
H.M. Treasury  
Great George Street  
London, SW1P 3AG, England





INTERNATIONAL MONETARY FUND  
WASHINGTON, D. C. 20431

CABLE ADDRESS  
INTERFUND

May 16, 1983

Sir:

I have been authorized and directed by the Executive Board to send to you the enclosed Report of the Executive Directors on the salary of the Managing Director proposing a Resolution for adoption by the Board of Governors without meeting, pursuant to Section 13 of the By-Laws of the Fund.

To be valid, votes on this Resolution must be cast by Governors or Alternate Governors, and must be received at the seat of the Fund on or before 6:00 p.m., Washington time, on June 13, 1983. Votes received after that date and time will not be counted.

It would be appreciated if you would transmit this communication to the Governor of the Fund representing your country with a request that he vote on the proposed Resolution. No particular form of vote is required so long as the Fund receives a clear indication as to whether the Governor approves or disapproves the proposed Resolution; such communication should be signed by the Governor or Alternate Governor or there should be a clear indication that it is sent on his behalf.

Very truly yours,

Leo Van Houtven  
Secretary

Enclosure

The Rt. Hon. Lord Richardson  
of Dunstonsburne, M.B.E., T.D., P.C.  
Governor  
Bank of England  
London, EC2R 8AH, England

INTERNATIONAL MONETARY FUND  
WASHINGTON D.C. 20541



CABLE ADDRESS  
INTERNATIONAL

May 14, 1963

Sir

I have been authorized and directed by the Executive Board to send to you the enclosed report of the Executive Director on the delay of the Executive Director regarding a resolution for adoption by the Board of Governors without meeting, pursuant to Article 11 of the Articles of Agreement.

To be valid, votes on this resolution must be cast by Governors of the Executive Board, and must be received at the seat of the Fund on or before 12:00 p.m., Washington time, on May 13, 1963. Votes received after that date and time will not be counted.

It would be appreciated if you would transmit this communication to the Director of the Fund regarding your country with a request that he vote on the proposed resolution. His particular form of vote is required so long as the Fund receives a clear indication as to whether the Governor approves or disapproves the proposed resolution and no other action should be taken by the Governor or Alternate Governor or that should be a clear indication that it is not on his behalf.

Very truly yours,

Leo P. Taylor  
Secretary

Enclosure

The Rt. Hon. Lord Selkirk  
of Balmulloch, M.P., T.P., F.R.S.  
Governor  
Bank of England  
London, EC2A 3AT, England

Report of the Executive Board to the Board of Governors  
and Draft Resolution on the Salary of the  
Managing Director

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1. Article XII, Section 2(i) of the Articles of Agreement states that the salary of the Managing Director shall be determined by the Board of Governors. Board of Governors Resolution No. 36-1, adopted January 30, 1981, provides that the annual salary of the Managing Director shall be US\$100,000, effective December 17, 1980. It is now proposed to adjust the salary of the Managing Director to US\$120,000 per annum to take account of the developments since 1980. The Executive Directors propose again to review the salary after 30 months.

2. Section 14(c) of the By-Laws provides for the reimbursement of reasonable expenses incurred by the Managing Director in the interest of the Fund. In accordance with their contracts with the Fund, the Managing Directors have been reimbursed certain specific expenses and have been receiving a nonaccountable allowance for housing and general representation. The Executive Directors have established this allowance at US\$55,000 per annum, effective June 17, 1983.

3. The other provisions of this contract remain the same as under the present contract.

4. Accordingly, the Executive Board of the Fund has approved the submission of the following Resolution to the Board of Governors of the Fund for a vote without meeting pursuant to Section 13 of the By-Laws:

RESOLVED, that effective June 17, 1983, the annual salary  
of the Managing Director of the Fund shall be one hundred twenty  
thousand United States dollars (US\$120,000).







# NEW ZEALAND

## NEW ZEALAND HIGH COMMISSION NEWS BULLETIN

7.30 P.M. TUESDAY 17 MAY 1983

### SPEECH NOTES

1. Pt. copy to  
Mr Little —  
Mr Haville  
Mr Battell.

2. Then resubmit.

### ADDRESS TO REFORM CLUB ECONOMIC GROUP

by The Rt. Hon. R.D. Muldoon C.H.  
Prime Minister of New Zealand  
and Minister of Finance

*[Signature]*  
18/v

New Zealanders are not, by nature, self-proclaimed reformers. In fact by nature we are rather gentle folk.

Jokes told about countries can occasionally be instructive. I emphasise the word "occasionally", because on this subject, with a name as distinctively Irish as Muldoon, I have to watch my back. That said, I understand that a certain German philosopher, when asked what he would do if he thought the end of the world was nigh, replied: "I'd go to New Zealand. Everything there happens two years after the event".

I happen to think that my German friend got close to - but missed - the point. It is not that New Zealanders are forever behind the play. It's just that the rest of the world takes two years to find out what we are doing down there.



What constitutes the essence of the New Zealand "character" is something that has always fascinated me. New Zealanders, at their best, are so thoroughly understated.

Countless times I have seen All Blacks come off the field after completing some phenomenal feat of skill and physical endurance such as scoring a hat-trick of tries and say "Oh, I just happened to be on the right spot at the right time".

So New Zealanders, even when they do establish a slight edge in certain areas, do not always go around shouting about it. When we do get cast as reformers, it is others that do the casting for us - it took visitors from overseas such as Sydney and Beatrice Webb and Andre Siegfried to describe New Zealand in the early 20th century as the "social laboratory of the world".

I am sure that my predecessors did then no more than we do now: namely, implement policies that seem to be common sense - in their case allowing women the vote. Even if nobody else did. When I first became Prime Minister, I said that my long-term aim was quite modest: to leave New Zealand no worse than I found it. Now, because of a series of events, I happen to have found myself cast by others in the role of a would-be reformer.

The area for reform is quite large too - the future of the world economy no less. Allow me to tell you exactly what happened, since the truth is much less grandiose.

I have been New Zealand's Minister of Finance since 1967 - apart from one period in the early 1970s when there was a brief political aberration. After the first oil shock, it gradually became apparent to me that simply funnelling petro-dollars around the world was likely to cause problems for us somewhat down the track. At one international meeting after another, I argued that while we should welcome a recycling process, since it offset the immediate danger of a sharp contraction in the world economy, countries absorbing these petro-dollars could not build up cumulative current account deficits of that magnitude year after year without ultimately creating trouble for themselves and their creditors.



I can clearly recall expressing public doubts at various times in the 1970s when faced with hopeful forecasts of an imminent world recovery and why all these problems would thus disappear. I do not know why economics has got itself the title of the "Dismal Science". Generally, those in charge of economic policy seem to me to be perennial optimists.

Early last year I began to formulate the thesis, based primarily on my long-expressed concern about the build-up of debt, collapse of any exchange rate discipline and growth of protectionism, that we had to consider the state of world trade and payments on a rather fundamental basis. I used some carefully chosen words to describe the scale of examination I had in mind. I suggested we need another Bretton Woods conference. Overnight I had become a reformer and at the Commonwealth Finance Ministers' Meeting in London last September I received strong expressions of support for the idea.

Before I describe the substance of the proposal to you, I would like to make one or two personal observations about the interplay of ideas, politics and rhetoric. In my experience, many good ideas have been lost or buried because of the failure of the proponents to formulate them in sufficiently striking terms.

When I used the term "Bretton Woods conference" and another concept I have been advocating, namely the establishment of an "Economic Security Council", I did so in the full knowledge that they might attract or repel people, but they could not be ignored. Of course, without substance behind them, the words are meaningless and are quickly seen as such. However, the two - rhetoric and ideas - go hand in hand. Politics is the process that puts them together and leads to action.

I have often referred in New Zealand to paralysis by analysis. I believe that a prime function of a professional politician is to provide broad channels which can ensure that analysis proceeds to the next logical stage: formulating proposals for action. My call for a Bretton Woods type examination of trade and payments is designed to do just that.

I believe that we have reached a political impasse on many crucial international economic issues and we need to develop new political levers to get progress. We should not forget



that the analytical case for multilateral free trade had been established at least a century before the international community found a political mechanism in the form of the GATT - itself a compromise - of actually implementing planned multilateral reductions in industrial tariffs. Our very success since 1945 has created a global economy and thus new problems which we are not managing well. The challenge now is to find practical ways of managing those problems.

I will now put to you some of the collateral that lies behind these bold assertions. The international community is roughly divided into two camps. There are those who see the emerging economic recovery, the successful rescheduling exercises completed for the major debtor countries and the agreement to increase the resources available to the IMF, as having essentially resolved the problem. The other group, in which I count myself, of course welcomes those things although the quota increase should be larger. We also believe, however, that some of our present problems are more fundamental - that we will have to dig deeper to lay the foundations for any sustained return to world prosperity, and that there are new problems with which our existing institutions are not well equipped to deal.

Those who subscribe to that second view - the reformist view, if you like - have to be careful to distinguish their views from radical critics who want to restructure the entire international economic system under the guise of the so-called global negotiations. The advocates of global negotiations are following an illusion that domestic economic management is a matter of secondary importance. The fact is, of course, that we had to squeeze inflation and inflationary expectations out of our economies. It is, nevertheless, becoming clearer that the task of building a widespread durable recovery has an international dimension.

We have created an interdependent world economy and there is no agreement on how we should manage it. As I said to OECD ministers last week, the concept of interdependence has left out of the economics textbooks and has arrived on ministers' desks everywhere. The world "interdependence" is strongly reminiscent of the jargon of sociologists. I am just an old finance minister. Someone would do me and the international community a considerable favour if they could think of a word that might better reflect the reality of an interdependent world.





Take just one or two examples. Consider protectionism and the ritual calls we have made to resist protectionism over recent years. How can we reconcile these calls with the facts of creeping protectionism. How can we account for the reality that today almost 50 per cent of trade by all market economies is "managed" trade - that is, trade which is not, for a variety of reasons, governed by the conventional forces of the arms length free market. One possible explanation, and very popular with some journalists, is most unflattering to those ministers who attend such meetings. Now I attend these meetings and I agree to nothing that my country is not prepared to implement.

Let me tell you exactly what the problem is. It is quite simple. It is terribly difficult to extend free trade principles in today's interdependent world without tackling the underlying problems that give rise to protectionism in the first place. It can be done, of course. On the 1st of January this year the Closer Economic Relations Agreement to dismantle all remaining barriers to trade between New Zealand and Australia was put into place. We and the Australians have also quite recently set up the SPARTECA agreement which gives free access into our domestic markets for virtually all exports from the Forum island countries - the developing economies of the South Pacific.

We can do this because down there in the South Pacific we have a very clear idea of what we are trying to do, the scale is of manageable proportions, and it is all underpinned by excellent political relations. That is, incidentally, why we do not want certain other people coming in to the South Pacific causing trouble. The fact that we do have our act together is why they do not succeed even when occasionally they try. Extend the problem of getting rid of protectionism into a more complicated world, however, and the difficulties of pursuing a policy of multilateral trade liberalisation become very obvious.

In recent years we have seen massive and volatile shifts in exchange rates. These shifts are often temporary and cannot be explained by differences in underlying comparative advantage. In the case of industrial products the swings in exchange rates can make a nonsense of the generally small residual tariffs that exist. In these circumstances is it sensible simply to continue to denounce protectionism without addressing these structural problems?



Of one thing we can be sure. It is useless to call for "greater political will". Political will does not materialise from communiques that no-one reads. Political will has to be created. Allow me to let you into a fascinating secret. The overwhelming majority of political leaders that I know, and I have seen a few come and go, know the broad direction that policy needs to move in. So there is not a lot to be gained by telling them, in this case, to make a solemn Brownie oath to resist protectionism. What you have to do, and it is much more difficult, is to create a framework which allows politicians more flexibility to move in the desired direction.

*fn?*  
 In the circumstances facing us today, an agreed framework for more co-ordinated growth policies and greater coherence in macro-economic policies so as to minimise exchange rate volatility would do more to counter protectionism than a gaggle of summits. Here, I have to point to what may appear at first sight to be a contradiction in my analysis. On the one hand, I am being unkind about summit meetings. On the other hand, I am calling for a conference along the lines of Bretton Woods. There is no contradiction and the distinction is as follows. Summit meetings, ministerial meetings and so forth are held all the time - they have very little real preparation and are generally restatements of existing national positions. Their real function - and I have to say it is a valuable, if limited, one - is to keep people talking to each other and prevent any sharp descent into beggar-thy-neighbour policies.

*?*  
 There is another type of meeting. This is the meeting which might be held once every two or three decades and which tries to redefine basic ground-rules. That was what Bretton Woods was about. The law of diminishing returns must be considered to apply to such conferences in the sense that they can only be held every 2 or 3 decades. You have such a conference when your analysis leads you to believe that the world is facing fundamentally new problems which existing institutions are not handling well. The function of such a conference is to reach political agreement on modified ground rules and so create political will to tackle those problems.

At the end of the day - as happened at Bretton Woods - each government goes back to its people and says: "This is what has been agreed by the world community. Now are we in or are we out?" Most decide to be part of it, as they did in response to the formation of the GATT, the IMF and, of course, the United Nations. In some respects it is misleading to call it a conference. What I have in mind is more correctly called a



process of examination which is likely to lead, after a year or two of the most careful preparation, to an international conference. That was what happened at Bretton Woods originally - two or three years of intensive discussion and negotiation by Keynes and Harry White and others, backed by the resources of the two then dominant treasuries, which led to a statement of principles and detailed proposals for consideration by the international community as a whole.

I believe this is an idea whose time has come. I believe the recovery will be seriously constrained by structural problems of massive cumulative debt, protectionism, and absence of agreement on structural adjustment policies. The developing countries cannot be ignored in all this. We are now dependent on them as they always have been on us. Interdependence, after all, is nothing more than dependence that flows two ways. The United States learned this very fast when the near breakdown of the system in Mexico resulted in a catastrophic drop in US exports to Mexico. For the industrial countries as a group, about one third of their manufactured exports in 1980 went to developing countries. If the developing countries, faced with their massive debts and the growing caution of the major private lenders, all adjust to that situation by bludgeoning imports over the next two years or so, we shall have to wait rather longer for the sustained recovery we so desperately need.

We have, I repeat, a global economy, marked by a high degree of interdependence between economies, between issues such as trade and finance and between institutions such as the IMF and the GATT. Our system worked well until the Bretton Woods system broke down in the early 1970s with the closure of the gold window. There are aspects of the system which are still working perfectly adequately and we can build on them. Indeed a principal difference between my proposal and the global negotiations is that the latter seems to want to tear everything down and start again.

I am reminded here of the comment of Patrick Moynihan, former US Ambassador to the United Nations, who quipped that if the UN did not exist it would be impossible to create it. The institutions such as the GATT, the IMF, the BIS and the World Bank are invaluable resources. Their problem is that they are not working in a sufficiently coherent way with each other and with the other major actors involved - namely, national treasuries, and their ministers of finance, central banks, trade ministers and the international private banks which are



essentially bankrolling the whole system.

I believe that new ground rules are required for an open world economy. I go further than this and suggest the need for a body with sufficient political weight to help co-ordinate and influence sovereign governments' economic policies. I call this concept - an economic security council - and it is a natural development of the interim committee of the IMF. We are living in an interdependent world and we had better start thinking about these issues. There are other detailed issues that have to be tackled by such a conference. I shall not bore you with them.

I said at the start of my address that I find myself cast in the unaccustomed role of a reformer. All I am doing is saying what I think has happened to the international trade and payments system since I first became an under-secretary of finance almost 20 years ago. There are, of course, some advantages in being a Minister of Finance of a small country. I can put forward these ideas without causing panic in the breasts of a thousand bankers. By disposition, bankers do not favour change until they know it is unavoidable and then, like Eskimos in a bed, they all turn over at once.

Some of New Zealand's best friends are bankers and what I would like to do is give them a little more lead time. By all means let us consolidate the emerging recovery, but let us also start the long and complex task of defining how we are to get along in this interdependent world economy that we have created. If we do not, then I believe we will see continued financial crises, further slippage from the principles of free trade and ultimately political and strategic problems.

\*

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\*





*with advise*  
*of [unclear] [unclear]*

*For Pl. Chase*  
*of 31 May - to check*  
*Boonell*  
*JPL*

THE WORLD BANK  
Washington, D.C. 20433  
U.S.A.

*Let's ask*  
*- + [unclear] [unclear]*  
*WSE*

12645 Travilah Road  
Potomac, Maryland 20854  
U.S.A.  
May 17, 1983

My dear Geoffrey,

I know you have many more things on your mind at present, but whatever your future responsibilities, I think you will find the attached very interesting. It sets out to describe how agencies like the Bank (and ODA) can help developing countries to divest of their public undertakings (the U.K. is often taken as a point of reference), and it is written by Elliot Berg, author of the Bank's Sub-Saharan Africa Report and a person who I had hoped I might introduce you to one day. I am also sending a copy to Tim Raison.

All the very best for the election from us both. We will be with you in spirit and just possibly on occasions, in the flesh. *I wish I was standing!*

With love to Elspeth.

Christopher H. Walton

The Rt. Hon. Sir Geoffrey Howe, QCMP  
11, Downing Street  
London S.W. 1

6. THE CHARACTERISTICS OF THE NEW CREDITS SHOULD REFLECT THE WAY IN WHICH THE FUND FINANCED ITS MEDIUM-TERM PROGRAMMES. HE WAS NOT THINKING OF A PURELY BRIDGING OPERATION. HE DID NOT WISH TO EARMARK A LARGE PART OF THE EIGHTH QUOTA INCREASE IN ADVANCE. HIS CLEAR PREFERENCE WAS FOR MEDIUM-TERM BORROWING WITH MATURITY FROM 3 1/2 TO 7 YEARS. HE WOULD LIKE SOME ASSURANCES THAT CREDITS COULD BE ROLLED OVER AT MATURITY, BECAUSE IT WOULD BE DIFFICULT TO COUNT ON REFINANCING FROM THE ENLARGED GAB. THE FUND WOULD, OF COURSE, ASSURE THE LIQUIDITY OF CLAIMS IN THE USUAL WAY. THEY WOULD BE DENOMINATED IN SDRS AND THEIR YIELD WOULD REFLECT MARKET RATES. HE CONTEMPLATED DISBURSEMENT WITHIN 2 OR 3 YEARS AFTER COMMITMENT. THE BIS MIGHT PLAY AN IMPORTANT ROLE IN SETTING UP THE CREDITS, ON THE LINES OF THE PREVIOUS BIS ARRANGEMENT.

7. IN THE ENSURING DISCUSSION, ERB (UNITED STATES) SAID THAT THERE WAS LITTLE CHANCE OF AN EARLY AMERICAN CONTRIBUTION TO THE NEW CREDITS. AGREEMENT WOULD PROBABLY BE NEEDED FROM CONGRESS AND HE DID NOT SEE MUCH SCOPE FOR DOING ANYTHING ADDITIONAL TO THE QUOTA INCREASE IT WAS VITAL TO GET CONGRESS TO AGREE ON THIS AND HE DID NOT WANT TO PUT IT AT RISK BY RAISING THE QUESTION EITHER OF ADDITIONAL OFFICIAL CREDITS OR AN APPROACH BY THE FUND TO THE US CAPITAL MARKET. FROM THIS POINT OF VIEW, IT WOULD BE PREMATURE TO FORCE A DECISION WITHIN THE NEXT FEW WEEKS. BUT APART FROM THOSE CONSIDERATIONS, HIS AUTHORITIES WERE NOT TOO DISTURBED AT THE PROSPECT OF A COMMITMENTS GAP ON THE BORROWING SIDE. THEY WOULD NEED TO LOOK AS WELL AT THE PROSPECTS FOR FUND BORROWING IN THE NEXT TWO YEARS, INCLUDING RECOURSE TO THE GAB AND MARKET BORROWING. THERE WERE TOO MANY UNCERTAINTIES FOR THEM TO COMMIT THEMSELVES AT THE PRESENT TIME.

8. HIRAO (JAPAN) THOUGHT HIS AUTHORITIES MIGHT BE INTERESTED IN PROVIDING CREDITS IF OTHER COUNTRIES WOULD COME IN. BUT HE SAW THE EXERCISE MORE AS ONE OF PROVIDING BRIDGING FINANCE. TAYLOR PURSUED THIS LATTER POINT. HE COULD NOT SEE WHY MANAGEMENT WERE SO ADAMANT ABOUT SEPARATING THE IMMEDIATE FINANCING NEED FROM THE RESOURCES TO BE MADE AVAILABLE UNDER THE EIGHTH QUOTA INCREASE AND, MORE TENTATIVELY, THE EXPANDED GAB. THE QUOTA INCREASE WAS AFTER ALL INTENDED IN PART TO SUPPORT THE FUND'S EXISTING LENDING POLICIES. THE MD INSISTED THAT IT WOULD NOT BE WISE TO LIMIT THE EXERCISE TO A BRIDGING OPERATION FOR SIX MONTHS, ALTHOUGH HE WOULD NOT RULE OUT SUCH AN APPROACH COMPLETELY. HE HOPED THAT COUNTRIES WOULD NOT PUT TOO MANY CONDITIONS IN THE WAY OF HIS PROPOSAL. THERE WAS A NEED FOR A CLEAR MANIFESTATION OF THEIR COMMITMENT TO THE FUND. HIS PROPOSAL MEANT AFTER ALL RATHER LIMITED AMOUNTS WHEN SPREAD AS A COLLABORATIVE EFFORT AND IT MIGHT BE POSSIBLE TO SECURE A SPECIAL ARRANGEMENT WITH THE UNITED STATES.

2  
**CONFIDENTIAL**

TIMING

# CONFIDENTIAL

## TIMING

9. THE MD SAID THAT HE WOULD BE MEETING THE GERMAN AUTHORITIES ON JUNE 6 OR 7 ON HIS WAY TO UNCTAD, TO TAKE UP WITH THEM THE OFFER THEY HAD RECENTLY MADE IN THE BOARD (SEE OUR TELNO 162 AND THE MANAGING DIRECTOR'S SUMMING UP BUFF 83/97). HE WAS READY TO HAVE DISCUSSIONS WITH ANY OTHER COUNTRY AND WOULD BE HAPPY TO HAVE TALKS WITH JAPAN, THE UNITED KINGDOM, AND OTHERS. IT WOULD BE MOST USEFUL TO HAVE PRELIMINARY REACTIONS IN THE FIRST DAYS OF JUNE. HABERMEIER MIGHT TAKE THE OPPORTUNITY OF THE BIS ANNUAL MEETING BEGINNING JUNE 11 TO OFFER A FULLER PRESENTATION OF THE MD'S PROPOSALS IN BASLE, PERHAPS ON JUNE 10, AT WHICH NATIONAL REPRESENTATIVES COULD ASK QUESTIONS AND GIVE FULLER RESPONSES. THE MD WOULD LIKE TO THINK IN TERMS OF COMPLETING THINGS AT THE BASLE MEETING IN JULY, WHICH HE IS DUE TO ATTEND.

10. HABERMEIER WOULD CIRCULATE A MEMORANDUM WITH SOME ILLUSTRATIVE FIGURES IN THE NEXT FEW DAYS. THE MD HOPED THAT DIRECTORS WOULD CONVEY THESE FIRST THOUGHTS TO THEIR AUTHORITIES AS SOON AS POSSIBLE.

11. I SHOULD BE GRATEFUL FOR GUIDANCE BY 31 MAY ON HOW TO RESPOND TO THE MD'S REQUEST FOR PRELIMINARY REACTION'S.

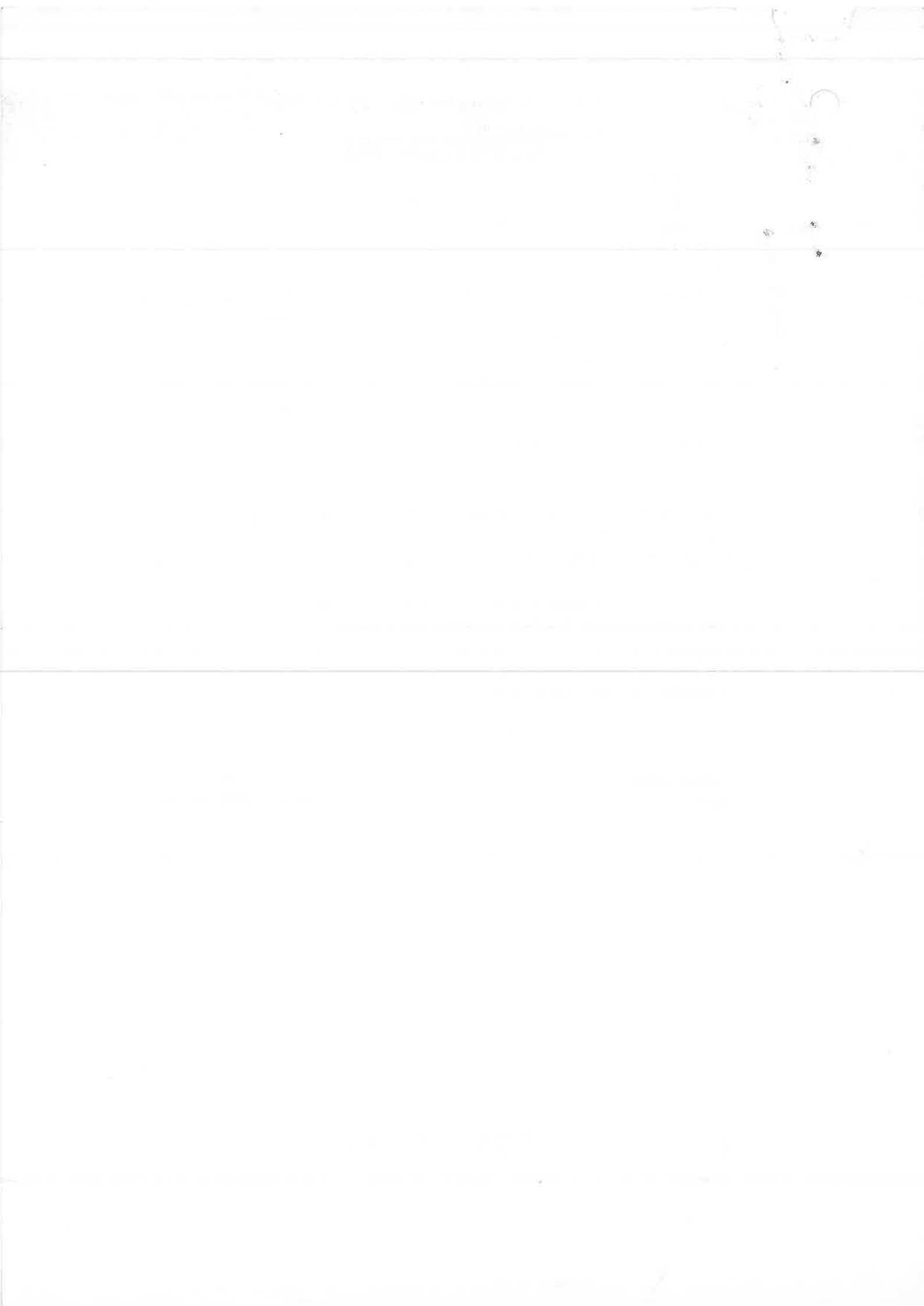
12. FCO PLEASE ADVANCE TO LAVELLE (TREASURY), GILCHRIST (BANK OF ENGLAND) AND APPEYARD (ERD).

WICKS

ADVANCED AS REQUESTED

MONETARY  
ERD

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ADVANCE ADDRESSEES



CONFIDENTIAL

10310 - 1

RR UKDEL IMF/IBRD WASHINGTON  
GRS 47  
CONFIDENTIAL  
FM FCO 201100Z MAY 83  
TO ROUTINE UKDEL IMF/IBRD WASHINGTON  
TELEGRAM NUMBER 157 OF 20 MAY

IMF: M.D.'S CONTRACT  
ON BEHALF OF THE CHANCELLOR OF THE EXCHEQUER PLEASE CAST THE  
VOTES OF THE UNITED KINGDOM IN FAVOUR OF THE RESOLUTION ATTACHED  
TO VAN HOUTVEN'S LETTER OF 16 MAY.

PYM

NNNN  
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ERD

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CONFIDENTIAL



TELEPHONE  
01-601 4444

EXCHEQUER

23 MAY 1983 23/5

BANK OF ENGLAND

LONDON EC2R 8AH

20 May 1983

(pwf)

Mr Middleton

Mr Bottrell

Mr Litter

Mr Unwin

Mr Lavelle

J O Kerr Esq  
Principal Private Secretary to  
the Chancellor of the Exchequer  
HM Treasury  
Parliament Street  
London  
SW1P 3AG

Dear John

I enclose for your action a copy of a letter of 16 May from Mr Van Houtven, Secretary of the IMF, regarding a Draft Resolution on the Salary of the Managing Director. Please note that a vote on the proposed Resolution must be received at the seat of the Fund on or before 6.00 pm Washington time on 13 June 1983.

Yours sincerely  
Andrew Lavelle

A J V Giles  
Assistant Private Secretary  
to the Governor







INTERNATIONAL MONETARY FUND  
WASHINGTON, D. C. 20431

CABLE ADDRESS  
INTERFUND

May 16, 1983

rec'd 19 May 1983 10 30am

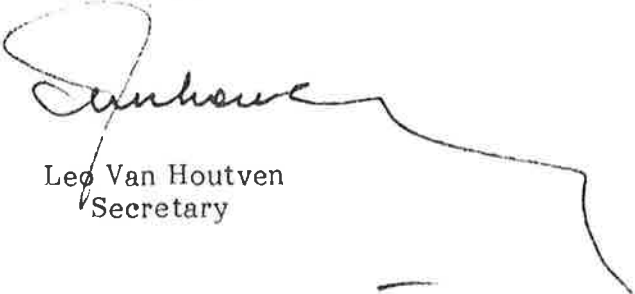
Sir:

I have been authorized and directed by the Executive Board to send to you the enclosed Report of the Executive Directors on the salary of the Managing Director proposing a Resolution for adoption by the Board of Governors without meeting, pursuant to Section 13 of the By-Laws of the Fund.

To be valid, votes on this Resolution must be cast by Governors or Alternate Governors, and must be received at the seat of the Fund on or before 6:00 p.m., Washington time, on June 13, 1983. Votes received after that date and time will not be counted.

It would be appreciated if you would transmit this communication to the Governor of the Fund representing your country with a request that he vote on the proposed Resolution. No particular form of vote is required so long as the Fund receives a clear indication as to whether the Governor approves or disapproves the proposed Resolution; such communication should be signed by the Governor or Alternate Governor or there should be a clear indication that it is sent on his behalf.

Very truly yours,



Leo Van Houtven  
Secretary

Enclosure

The Rt. Hon. Lord Richardson  
of Duntisbourne, M.B.E., T.D., P.C.  
Governor  
Bank of England  
London, EC2R 8AH, England



Report of the Executive Board to the Board of Governors  
and Draft Resolution on the Salary of the  
Managing Director

1. Article XII, Section 2(i) of the Articles of Agreement states that the salary of the Managing Director shall be determined by the Board of Governors. Board of Governors Resolution No. 36-1, adopted January 30, 1981, provides that the annual salary of the Managing Director shall be US\$100,000, effective December 17, 1980. It is now proposed to adjust the salary of the Managing Director to US\$120,000 per annum to take account of the developments since 1980. The Executive Directors propose again to review the salary after 30 months.

2. Section 14(c) of the By-Laws provides for the reimbursement of reasonable expenses incurred by the Managing Director in the interest of the Fund. In accordance with their contracts with the Fund, the Managing Directors have been reimbursed certain specific expenses and have been receiving a nonaccountable allowance for housing and general representation. The Executive Directors have established this allowance at US\$55,000 per annum, effective June 17, 1983.

3. The other provisions of this contract remain the same as under the present contract.

4. Accordingly, the Executive Board of the Fund has approved the submission of the following Resolution to the Board of Governors of the Fund for a vote without meeting pursuant to Section 13 of the By-Laws:

RESOLVED, that effective June 17, 1983, the annual salary  
of the Managing Director of the Fund shall be one hundred twenty  
thousand United States dollars (US\$120,000).





FROM: J O KERR

DATE: 23 May 1983

MR BEASTALL

... Please see the attached internal IMF paper, which was sent to the Chancellor by a friend at IBRD. (The author is, presumably, the same Berg who wrote the admirable 1981 IBRD Sub-Saharan Africa Report.) The Chancellor would be most grateful if, within the next week or so, someone could let him have a very short appraisal of this latest offering. A couple of pages would more than suffice!

A handwritten signature in cursive script, appearing to read "J O Kerr".

J O KERR



R. KERR

*(pwt)*

FROM: J.G.LITTLER  
DATE: 31 MAY, 1983

cc Mr.Middleton  
Mr.Unwin  
Mr.Lavelle

SEPTEMBER IMF/IBRD MEETINGS: TIMETABLE

At the lunch for Summit Finance Ministers yesterday, at which I represented the Chancellor, Delors (France) raised the question of a meeting of G.10 Ministers which he would normally chair in Washington in the margins of the IMF/IBRD Annual Meetings in September. He said that on this occasion he foresaw a heavy agenda for discussion, and was intending to propose a meeting lasting a whole day. There were generally supportive comments, and suggestions that there would be advantage in holding such a meeting before the main public speeches.

2. I chipped in with a reminder that we would also need a meeting, probably of a whole day, for the IMF Interim Committee, which could have some difficult pieces of business at that time.


3. Mention was made of a possible G.5 meeting for another round of surveillance, which could however be held during an evening.

4. It was agreed that Delors would take this up again after the Election here, and concert with the Chancellor on how best to time the G.10 and Interim Committee. Incidentally, Delors will probably also be suggesting a G.5 meeting (not on surveillance, but on debt and IMF issues) in Paris towards the end of July. We already have a meeting of Deputies provisionally planned for earlier in July.

5. I will discuss this further with Mr.Lavelle, and will in any case be seeing Camdessus in Brussels on 9 June. My present thought is that we ought to try to fit in both G.10 and Interim Committee before the public IMF meetings begin, and could probably slot in the G.5 one evening later in the IMF week.

*v. touchy.  
Discussed  
with Lavelle.*

*JGL  
vi*

  
(J. G. LITTLER)







INTERNATIONAL MONETARY FUND  
WASHINGTON, D. C. 20431

CC-MW LITLER. ✓  
Mr UNWIN.  
Mr Lavelle.

Am

CABLE ADDRESS  
INTERFUND

June 2, 1983

Sir:

I have the honor to transmit herewith a copy of a communication which has been sent today to all members of the Fund, submitting Resolutions on which Governors are requested to vote.

Very truly yours,

A handwritten signature in black ink, appearing to read "Leo Van Houtven".

Leo Van Houtven  
Secretary

Enclosure

Rt. Hon. Sir Geoffrey Howe, Q.C., M.P.  
Governor of the International  
Monetary Fund for the  
United Kingdom  
H.M. Treasury  
Great George Street  
London, SW1P 3AG, England





INTERNATIONAL MONETARY FUND  
WASHINGTON, D. C. 20431

CABLE ADDRESS  
INTERFUND

June 2, 1983

Sir:

The standing Joint Committee on the Remuneration of Executive Directors and their Alternates has adopted a Report and recommendations to be submitted to the Board of Governors. At the request of the Joint Committee, I am transmitting its Report and recommendations herewith. The Joint Committee neither discussed with, nor disclosed to, Executive Directors its Report and recommendations prior to their transmittal to the Governors.

The Board of Governors has been requested to vote without meeting, pursuant to Section 13 of the By-Laws of the Fund, on the Resolutions attached to the Report. The Executive Board has decided, pursuant to Section 13 (d) of the By-Laws, that no Governor shall vote on the Resolutions until June 9, 1983.

To be valid, votes on the Resolutions must be cast by Governors or Alternate Governors, and must be received at the seat of the Fund on or after Thursday, June 9, 1983, but not later than Wednesday, July 6, 1983. Votes received before June 9, 1983 or after 6:00 p.m., Washington time, on July 6, 1983 will not be counted.

It would be appreciated if you would transmit the Report to the Governor of the Fund representing your country with the request that he vote on the Resolutions attached to the Report. No particular form of vote is required so long as the Fund receives a clear indication as to whether the Governor approves or disapproves the proposed Resolutions; such communication should be signed by the Governor or Alternate Governor or there should be a clear indication that it is sent on his behalf.

Very truly yours,

Leo Van Houtven  
Secretary

Enclosure

The Rt. Hon. Lord Richardson  
of Duntisbourne, M.B.E., T.D., P.C.  
Governor  
Bank of England  
London, EC2R 8AH, England



May 21, 1983

Report to the Boards of Governors of the Bank and Fund  
by the Joint Committee on the Remuneration of  
Executive Directors and their Alternates

1. Pursuant to Section 13(e) of the By-Laws of the Bank and Section 14(e) of the By-Laws of the Fund, the undersigned were appointed to the 1983 standing Joint Committee on the Remuneration of Executive Directors and their Alternates.
2. The Joint Committee met in Washington, D.C. on March 25, 1983 and in Madrid on May 21, 1983. The Committee decided to retain the same firm of consultants, Hewitt Associates, as had assisted previous Committees since 1977; the consultants' terms of reference are attached as Annex I. The Committee was provided with background material by the Bank and the Fund and it also had the benefit of discussions with a number of Executive Directors and Alternates.
3. The Committee has noted that, under the By-Laws of the Fund and the Bank, it is not obligated to submit recommendations to the Boards of Governors because regular elections of Executive Directors are not scheduled to take place in 1983. However, as the three previous Committees have pointed out, the volatile international economic conditions of recent years continue to cause rapid changes in relative levels of compensation. In such circumstances, the Committee considers that it is necessary to examine the situation every year although it may not be necessary to carry out wide-ranging and very detailed studies on each occasion.
4. The Committee has reviewed the concepts and methods developed by previous Committees for determining Executive Directors' remuneration. In particular, it reaffirms that the principal basis should continue to be comparison with economic and financial ministers in selected embassies in Washington, D.C., while also taking note of the organizational structures and movements in staff salaries in the Fund and the Bank as well as of cost-of-living trends. It also endorses strongly the policy guideline for conducting the embassy survey defined by the 1982 Committee. In particular, comparisons should be made only with the economic and financial minister positions which have been found to have functions, and responsibilities most closely comparable to Executive Directors', namely, those in the Washington, D.C. embassies of Australia, Canada, France, Germany, Japan, the Netherlands, Norway, and the United Kingdom, together with that of U.S. economic minister in a location assumed to have a cost of living equivalent to Washington D.C. Although on average the responsibilities of the nine positions are not as complex or as extensive as those of Executive Directors, they are sufficiently similar to provide a reliable and consistent basis of comparison.

5. An important principle enunciated by previous Committees has been that the remuneration of Executive Directors should be established so that it is not likely to be exceeded by the salaries of more than a moderate number of staff, provided that this does not create an automatic linkage between the two. The present Committee endorses this principle. Because Executive Directors decide on the salary structure for the staff, any form of linkage could be regarded as contravening one of the main purposes underlying the establishment of the Joint Committee, namely, that Executive Directors should not be involved in determining directly or indirectly their own remuneration. At the same time, if more than a moderate number of staff have higher pay than that of Executive Directors, the status and authority of the Directors could be perceived to be undermined and the capacity of the two organizations to attract persons of the caliber necessary for their crucial policymaking function could be seriously weakened.
6. The Committee has given much thought to the arguments that have been presented to it, and to previous Committees, for making pensionable the supplemental allowance paid to Executive Directors and Alternates since 1974. The allowance was instituted "to reflect the unique housing and representation costs and other unusual expenses associated with the temporary nature" of their assignments and their location in Washington, D.C. Moreover, most Executive Directors and Alternates serve for relatively short periods and for them the impact of making the allowance pensionable would be small; it is only after longer than average service that pension entitlements (or withdrawal benefits) would increase significantly. The Committee believes that, at the present time, the reasons for having a supplemental allowance remain valid.
7. With regard to benefits, the Committee has considered whether the termination grant and the home leave allowance available to staff should be extended to Executive Directors and Alternates. The Committee has concluded that the termination grant should not be extended to them for the reasons given by previous Committees, namely, that it would not be consistent with the character of Executive Directors' and Alternates' appointments. The home leave allowance, on the other hand, is intended to help staff members and their families to meet expenses which the families of Executive Directors and Alternates are equally likely to incur. Accordingly, the Committee proposes that, when spouses and children of Executive Directors and Alternates become eligible for, and take, home leave, they should also become eligible to receive the lump-sum allowance on the same basis and subject to the same conditions as the spouses and children of staff. However, because Executive Directors and Alternates themselves are not eligible for home leave, the allowance would only be payable for their families.
8. With regard to the relationship between the remuneration of Executive Directors and that of Alternates, the Committee has

considered whether the gap between the two should be narrowed in view of the heavy responsibilities borne by Alternates in many constituencies. The Committee concludes that the relationship established in 1980, whereby Alternates' salary plus supplemental allowance amounts to approximately 83% of that of Executive Directors, continues to be appropriate at the present time. The total net direct remuneration of Executive Directors and Alternates, which includes spouse and dependency allowances, is currently \$81,040 and \$68,035 respectively. <sup>1/</sup>

9. In formulating its recommendations the Committee has taken into account all of the considerations outlined in the preceding paragraphs, together with:

- (a) The results of the consultants' survey of the remuneration of the eight economic and financial minister positions in Washington, D.C. embassies, together with one U.S. economic minister position which, as indicated in paragraph 4 above, the Committee considers to be the most appropriate basis for determining Executive Directors' remuneration. The average annual total net direct remuneration of the nine positions as of March 1, 1983 amounted to \$83,290. The average for the group was 6.7% higher than at the time of the 1982 survey.
- (b) The evolution in the real incomes of Executive Directors as indicated in Annex II. In the twelve months to March 1983, the consumer price index (CPI-U) for Washington, D.C. went up by 3.7%. As of that date, the real incomes of Executive Directors were well below the levels of earlier years.

1/ The total net direct remuneration of Executive Directors and Alternates is comprised as follows:

	<u>Executive Directors</u>	<u>Alternates</u>
Salary	\$ 69,200	\$ 57,900
Supplemental Allowance	8,000	6,400
	<u>\$ 77,200</u>	<u>\$ 64,300</u>
Plus (assuming the average incumbent is married with two dependent children)		
Spouse Allowance	3,000	2,895
Dependency Allowance	840	840
	<u>\$ 81,040</u>	<u>\$ 68,035</u>

- (c) As a result of the increases in salaries for the staff of the Bank and the Fund effective May 1, 1983, the numbers of staff with higher remuneration than Executive Directors and Alternates have risen substantially. As pointed out in paragraph 5 above, the Committee believes that it is important that Executive Directors' pay should be established so that it is not likely to be exceeded by the salaries of more than a moderate number of staff.

Recommendations

10. The Committee recommends:

- (a) an increase effective July 1, 1983, in the salaries of Executive Directors of \$4,400 to \$73,600 per annum, and an increase in the non-pensionable supplemental allowance of \$500 to \$8,500 per annum;
- (b) an increase effective July 1, 1983, in the salaries of Alternates of \$3,700 to \$61,600 per annum, and an increase in the non-pensionable supplemental allowance of \$400 to \$6,800 per annum;
- (c) that, effective July 1, 1983, Executive Directors and Alternates should receive home leave allowances for their spouses and dependent children in the same amount as it is paid in respect of the families of the staff.

11.

As a result of the recommended increases:

- (a) the relationship between the total net remuneration of Executive Directors and that of the average of the nine comparator positions would change from 1.038 to 1.032; <sup>1/</sup>
- (b) the real incomes of Executive Directors would improve as indicated in Annex II;
- (c) the numbers of staff with salaries above the remuneration of Executive Directors would rise only slightly as shown in Annex III.--

12.

Draft resolutions covering the above recommendations are attached as Annex IV, and we recommend that they be adopted by the Boards of Governors of the Bank and the Fund, respectively.

<sup>1/</sup> The net remuneration of Executive Directors comprises salary, supplemental allowance and spouse and dependency allowances. Because of the way in which they are computed, the spouse and dependency allowances for both Executive Directors and their Alternates would be at the maximum level, namely, \$3,000 and \$840, assuming that they are married with two dependent children.




13. The Joint Committee has directed the Secretary of the Bank and the Secretary of the Fund to transmit this report to the Boards of Governors of the Bank and the Fund, respectively, for a vote without meeting in accordance with Sections 12 and 13(e) of the By-Laws of the Bank and Sections 13 and 14(e) of the By-Laws of the Fund.



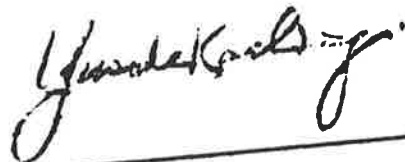
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H.E. Miguel Boyer



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Jorge Cauas Lama



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Yusuke Kashiwagi



Terms of Reference for Consultants to the Joint Committee on  
the Remuneration of Executive Directors and Their Alternates

The 1982 Joint Committee on the Remuneration of Executive Directors and their Alternates recommended that comparisons should be made with those positions that are most similar to those of Executive Directors. They noted that past surveys had found that the functions and responsibilities of Economic and Financial Ministers in the Washington, D.C. embassies of Australia, Canada, France, Germany, Japan, The Netherlands, Norway, and the United Kingdom, are comparable to those of Executive Directors. The 1982 Joint Committee also recommended that, in addition, the basis of comparison should be expanded to include the position of U.S. Economic Minister in a location assumed to have a cost of living comparable to that of Washington, D.C., thus expanding the group to a total of nine comparator positions.

The 1983 Joint Committee, concurring with those recommendations, requests the consultants to survey the remuneration and benefits of the above mentioned positions. The consultants should examine whether there is any reason to change the coverage of the survey recommended by the 1982 Joint Committee.

The consultants should report to the Joint Committee not later than the second half of April 1983.

Index of Real Income of Executive Directors and Alternates

ANNEX II

1946-1983

Effective Date	Net Salaries		Salary Index		Washington Consumer Price Index	Index of Real Income	
	Executive Directors	Alternates	Executive Directors	Alternates		Executive Directors	Alternates
June 1946	\$17,000	\$11,500	100.0	100.0			
Jan. 1951		14,000 <u>1/</u>		121.7	100.0	100.0	100.0
Nov. 1957	20,000	15,500	117.6	134.8	129.1		94.3
Nov. 1959		17,000		147.8	145.9	80.6	92.4
Sep. 1962	25,000	20,000	147.1	173.9	148.6		
Nov. 1965	28,000 <u>2/</u>	22,000 <u>2/</u>	164.7	191.3	154.1	95.5	112.9
Nov. 1968	31,000	25,000	182.4	217.4	162.3	101.5	117.9
Aug. 1969	35,000	27,000	205.9	234.8	183.6	99.4	118.4
Nov. 1972	37,000	29,000	217.6	252.2	192.3	107.1	122.1
July 1974	42,000 <u>2/</u>	33,000 <u>2/</u>	247.1	287.0	222.1	98.0	113.6
July 1975	43,500 <u>2/</u>	34,200 <u>2/</u>	255.9	297.4	252.7	97.8	113.6
July 1976	45,700 <u>2/</u>	35,900 <u>2/</u>	268.8	312.2	270.4 <u>3/</u>	94.6	110.0
July 1977	45,700 <u>2/</u>	35,900 <u>2/</u>	268.8	312.2	286.0 <u>3/</u>	94.0	109.2
July 1978	50,700 <u>2/</u>	39,900 <u>2/</u>	298.2	347.0	304.6 <u>3/</u>	88.2	102.3
July 1979	54,500 <u>2/</u>	42,900 <u>2/</u>	320.6	373.0	326.0 <u>3/</u>	91.5	106.4
July 1980	63,000 <u>2/</u>	52,500 <u>2/</u>	370.6	456.5	364.0 <u>4/</u>	88.1	102.5
July 1981	71,200 <u>2/</u>	59,300 <u>2/</u>	418.8	515.7	408.9 <u>4/</u>	90.6	111.6
July 1982	77,200 <u>2/</u>	64,300 <u>2/</u>	454.1	559.1	449.1 <u>4/</u>	93.3	114.8
July 1983 <u>5/</u>	77,200 <u>2/</u>	64,300 <u>2/</u>	454.1	559.1	477.4 <u>4/</u>	95.1	117.1
July 1983 <u>6/</u>	82,100 <u>2/</u>	68,400 <u>2/</u>	482.8	594.8	495.1 <u>4/</u>	91.7	112.9
					495.1 <u>4/</u>	97.5	120.1

- 1/ Fund Alternate. Bank Alternates remained at \$11,500 until October 1, 1956, when they too were raised to \$14,000.
- 2/ Includes supplemental allowance.
- 3/ Based on the Index for February in each year.
- 4/ Based on the Index for March in each year.
- 5/ Prior to any adjustment in remuneration that may be granted effective July 1, 1983.
- 6/ If the recommendations of the Joint Committee for adjustments in remuneration, effective July 1, 1983, were to be approved, the real income figures would change as indicated.

Number of Staff With Salaries Above the Remuneration of Executive Directors and Alternates <sup>1/</sup>

	Above Executive Directors			Above Alternates		
	Fund 2/ Number	Percentage of total profes- sional staff	Bank 3/ Number	Percentage of total profes- sional staff	Fund 2/ Number	Bank 3/ Percentage of total profes- sional staff
1969	0	-	0	-	29	2.7
1970	0	-	2	0.2	45	3.8
1971	2	0.3	1	0.1	68	5.7
1972	2	0.3	0	-	56	3.5
1973	2	0.3	7	0.4	87	5.5
1974	2	0.3	0	-	66	5.0
1975	13	1.6	7	0.3	98	10.0
1976	13	1.6	9	0.4	113	10.3
1977	17	2.1	20	0.9	180	20.6
1978	13	1.6	15	0.6	145	13.5
1979	43	5.3	45	1.7	181	19.3
1980	74	8.9	148	5.3	223	22.5
1981	38	4.4	51	1.8	121	11.3
1982	39	4.2	46	1.5	125	11.1
1983	76	8.0	121	4.1	192	20.9
1983 <sup>4/</sup> 42		4.4	55	1.9	144	11.3

<sup>1/</sup> Based on net salaries for staff and net remuneration, including supplemental allowance, for Executive Directors and Alternates.

<sup>2/</sup> Situation at end of each calendar year except for 1983, where figures as of May 1 have been used.

<sup>3/</sup> Situation at end of each calendar year except for 1983, where the figures represent the best estimate as of May 1.

<sup>4/</sup> Situation as at July 1, 1983, if recommendations for adjusting Executive Directors' and Alternates' remuneration, to be approved.



INTERNATIONAL MONETARY FUND

DRAFT RESOLUTION

Direct Remuneration of Executive  
Directors and their Alternates

RESOLVED:

THAT, effective July 1, 1983, the annual rates of remuneration of Executive Directors of the Fund and their Alternates pursuant to Section 14(e) of the By-Laws shall be as follows:

- (i) As salary, \$73,600 per year for Executive Directors and \$61,600 per year for their Alternates;
- (ii) As supplemental allowance (for expenses, including housing and entertainment expenses, except those specified in Section 14(f) of the By-Laws), \$8,500 per year for Executive Directors and \$6,800 per year for their Alternates.





INTERNATIONAL MONETARY FUND

DRAFT RESOLUTION

Home Leave Allowance for Executive  
Directors and their Alternates

RESOLVED:

THAT, effective with respect to home leave travel of the families of Executive Directors and Alternates commencing after July 1, 1983, a home leave allowance shall be paid to Executive Directors and their Alternates in the same amounts as it is paid in respect of the families of the staff.



Mrs Diggle

FROM: PAULA DIGGLE

DATE: 6 June 1983

MR KERR

ARGENTINA: IMF LOAN

I attach a few quick points the Chancellor might like to draw on in debating with Mr Healey tomorrow night. I am afraid our information about South Africa is sketchy without reference to the old files. If you want any more, perhaps I can provide that tomorrow.

PAULA DIGGLE



## 1. STABILITY OF INTERNATIONAL MONETARY SYSTEM

The IMF is intended to help stabilise world trade and financial transactions. The point made by Mr Healey himself in a letter to a bank manager published at the weekend.

## 2. ARMS PURCHASES

The IMF loan to Argentina was made subject to tight budgetary ceilings. We cannot deny that Argentina could, in effect re-order her budget to finance arms purchases if room can be found within her limited resources to do so. But it would be extraordinarily foolish. Argentina will be hard pressed to meet the IMF conditions without arms purchases. And if she fails to meet the conditions, there will be no further IMF finance available.

(If pressed) Finance for arms purchases typically medium-term (7-8 years). IMF finance shorter - repayments start after 3 years.

## 3. CONDITIONALITY

Mr Healey suggested on News at Ten over the weekend that the Chairman of the Interim Committee of the IMF could impose conditions on loans. The Chairman of the Interim Committee has no such role. These are decisions of the Board. And the only conditions which can be imposed on the standby arrangement are economic ones. The Board did prescribe a tough dose of economic medicine (see 2).

## 4. RIGHT OF VETO

As the Daily Telegraph reported on Saturday, Britain alone cannot stop the IMF Board agreeing any loan. A 50 per cent majority is required and we have 8 per cent of the voting power.

Moreover, the IMF rules do not allow political restrictions to be placed on Fund facilities. Proposals are judged on their technical merit. This is quite right. It would be dangerous if the Fund became a political animal.

## 5. BRITISH BANKS' INVOLVEMENT IN LOANS

British banks are responsible for their own commercial decisions. Understand that the syndicated loans agreed are linked with the tough



IMF package. (see 2).

6. SOUTH AFRICA

The Labour Government supported the IMF standby arrangements for South Africa in 1976.





TELEPHONE  
01-601 4444

DATE	- 7 JUN 1983
ACTION	Mr Bottrill
FILES	Mr Litterer
TO	Mr Groun
	Mr Lavelle
	Mr Carey Mr Bonney



BANK OF ENGLAND

LONDON EC2R 8AH

7 June 1983

<sup>10</sup>/<sub>7/6</sub>

Mrs Diggle  
We spoke.  
AB  
7/6.

J O Kerr Esq  
Principal Private Secretary to  
the Chancellor of the Exchequer  
HM Treasury  
Parliament Street  
London  
SW1P 3AG

Dear John,

I enclose for action a copy of a letter of 2 June from Mr Van Houtven, Secretary of the IMF, regarding draft Resolutions relating to the Remuneration of Executive Directors and their Alternates. Please note that votes on the proposed Resolutions must be received at the seat of the Fund on or after Thursday 9 June 1983 but not later than 6.00 pm Washington time on Wednesday 6 July 1983.

Yours sincerely,

Stephen Collins

S P Collins  
Assistant Private Secretary  
to the Governor

Ben:

- 1) bad example
- 2) inappropriate to give real £ to overpaid public servants. 8.6.





INTERNATIONAL MONETARY FUND  
WASHINGTON, D. C. 20431

CABLE ADDRESS  
INTERFUND

June 2, 1983

Sir:

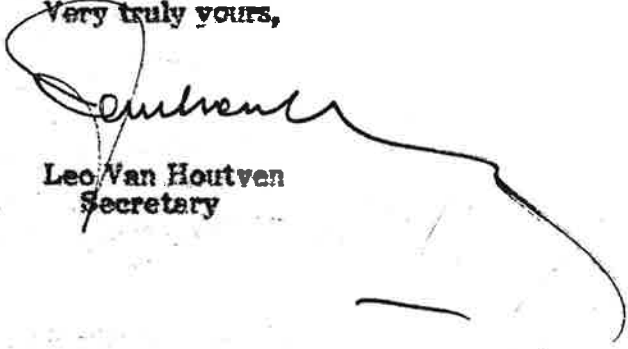
The standing Joint Committee on the Remuneration of Executive Directors and their Alternates has adopted a Report and recommendations to be submitted to the Board of Governors. At the request of the Joint Committee, I am transmitting its Report and recommendations herewith. The Joint Committee neither discussed with, nor disclosed to, Executive Directors its Report and recommendations prior to their transmittal to the Governors.

The Board of Governors has been requested to vote without meeting, pursuant to Section 13 of the By-Laws of the Fund, on the Resolutions attached to the Report. The Executive Board has decided, pursuant to Section 13 (d) of the By-Laws, that no Governor shall vote on the Resolutions until June 9, 1983.

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Very truly yours,

  
Leo Van Houtven  
Secretary

Enclosure

The Rt. Hon. Lord Richardson  
of Duntisbourne, M.B.E., T.D., P.C.  
Governor  
Bank of England  
London, EC2R 6AH, England



May 21, 1983

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8. With regard to the relationship between the remuneration of Executive Directors and that of Alternates, the Committee has

considered whether the gap between the two should be narrowed in view of the heavy responsibilities borne by Alternates in many constituencies. The Committee concludes that the relationship established in 1980, whereby Alternates' salary plus supplemental allowance amounts to approximately 83% of that of Executive Directors, continues to be appropriate at the present time. The total net direct remuneration of Executive Directors and Alternates, which includes spouse and dependency allowances, is currently \$81,040 and \$68,035 respectively. <sup>1/</sup>

9. In formulating its recommendations the Committee has taken into account all of the considerations outlined in the preceding paragraphs, together with:

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	<hr/>	<hr/>
Plus (assuming the average incumbent is married with two dependent children)	\$ 77,200	\$ 64,300
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Dependency Allowance	840	840
	<hr/>	<hr/>
Total Direct Remuneration	\$ 81,040	\$ 68,035

- (c) As a result of the increases in salaries for the staff of the Bank and the Fund effective May 1, 1983, the numbers of staff with higher remuneration than Executive Directors and Alternates have risen substantially. As pointed out in paragraph 5 above, the Committee believes that it is important that Executive Directors' pay should be established so that it is not likely to be exceeded by the salaries of more than a moderate number of staff.

### Recommendations

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- (b) an increase effective July 1, 1983, in the salaries of Alternates of \$3,700 to \$61,600 per annum, and an increase in the non-pensionable supplemental allowance of \$400 to \$6,800 per annum;
- (c) that, effective July 1, 1983, Executive Directors and Alternates should receive home leave allowances for their spouses and dependent children in the same amount as it is paid in respect of the families of the staff.

11. As a result of the recommended increases:

- (a) the relationship between the total net remuneration of Executive Directors and that of the average of the nine comparator positions would change from 1.038 to 1.032; 1/
- (b) the real incomes of Executive Directors would improve as indicated in Annex II;
- (c) the numbers of staff with salaries above the remuneration of Executive Directors would rise only slightly as shown in Annex III.-

12. Draft resolutions covering the above recommendations are attached as Annex IV. and we recommend that they be adopted by the Boards of Governors of the Bank and the Fund, respectively.

1/ The net remuneration of Executive Directors comprises salary, supplemental allowance and spouse and dependency allowances. Because of the way in which they are computed, the spouse and dependency allowances for both Executive Directors and their Alternates would be at the maximum level, namely, \$3,000 and \$840, assuming that they are married with two dependent children.



13. The Joint Committee has directed the Secretary of the Bank and the Secretary of the Fund to transmit this report to the Boards of Governors of the Bank and the Fund, respectively, for a vote without meeting in accordance with Sections 12 and 13(e) of the By-Laws of the Bank and Sections 13 and 14(e) of the By-Laws of the Fund.



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H.E. Miguel Boyer



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Jorge Cauas Lama



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Yusuke Kashiwagi



ANNEX I

Terms of Reference for Consultants to the Joint Committee on  
the Remuneration of Executive Directors and Their Alternates

The 1982 Joint Committee on the Remuneration of Executive Directors and their Alternates recommended that comparisons should be made with those positions that are most similar to those of Executive Directors. They noted that past surveys had found that the functions and responsibilities of Economic and Financial Ministers in the Washington, D.C. embassies of Australia, Canada, France, Germany, Japan, The Netherlands, Norway, and the United Kingdom, are comparable to those of Executive Directors. The 1982 Joint Committee also recommended that, in addition, the basis of comparison should be expanded to include the position of U.S. Economic Minister in a location assumed to have a cost of living comparable to that of Washington, D.C., thus expanding the group to a total of nine comparator positions.

The 1983 Joint Committee, concurring with those recommendations, requests the consultants to survey the remuneration and benefits of the above mentioned positions. The consultants should examine whether there is any reason to change the coverage of the survey recommended by the 1982 Joint Committee.

The consultants should report to the Joint Committee not later than the second half of April 1983.

## Index of Real Income of Executive Directors and Alternates

1946-1983

Effective Date	Net Salaries		Salary Index		Washington Consumer Price Index	Index of Real Income	
	Executive Directors	Alternates	Executive Directors	Alternates		Executive Directors	Alternates
June 1946	\$17,000	\$11,500	100.0	100.0	100.0	100.0	100.0
Jan. 1951		14,000 <u>1/</u>		121.7	129.1		94.3
Nov. 1957	20,000	15,500	117.6	134.8	145.9	80.6	92.4
Nov. 1959		17,000		147.8	148.6		
Sep. 1962	25,000	20,000	147.1	173.9	154.1	95.5	112.9
Nov. 1965	28,000 <u>2/</u>	22,000 <u>2/</u>	164.7	191.3	162.3	101.5	117.9
Nov. 1968	31,000	25,000	182.4	217.4	183.6	99.4	118.4
Aug. 1969	35,000	27,000	205.9	234.8	192.3	107.1	122.1
Nov. 1972	37,000	29,000	217.6	252.2	222.1	98.0	113.6
July 1974	42,000 <u>2/</u>	33,000 <u>2/</u>	247.1	287.0	252.7	97.8	113.6
July 1975	43,500 <u>2/</u>	34,200 <u>2/</u>	255.9	297.4	270.4 <u>3/</u>	94.6	110.0
July 1976	45,700 <u>2/</u>	35,900 <u>2/</u>	268.8	312.2	286.0 <u>3/</u>	94.0	109.2
July 1977	45,700 <u>2/</u>	35,900 <u>2/</u>	268.8	312.2	304.6 <u>3/</u>	88.2	102.3
July 1978	50,700 <u>2/</u>	39,900 <u>2/</u>	298.2	347.0	326.0 <u>3/</u>	91.5	106.4
July 1979	54,500 <u>2/</u>	42,900 <u>2/</u>	320.6	373.0	364.0 <u>4/</u>	88.1	102.5
July 1980	63,000 <u>2/</u>	52,500 <u>2/</u>	370.6	456.5	408.9 <u>4/</u>	90.6	111.6
July 1981	71,200 <u>2/</u>	59,300 <u>2/</u>	418.8	515.7	449.1 <u>4/</u>	93.3	114.8
July 1982	77,200 <u>2/</u>	64,300 <u>2/</u>	454.1	559.1	477.4 <u>4/</u>	95.1	117.1
July 1983 <u>5/</u>	77,200 <u>2/</u>	64,300 <u>2/</u>	454.1	559.1	495.1 <u>4/</u>	91.7	112.9
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July 1983 <u>6/</u>	82,100 <u>2/</u>	68,400 <u>2/</u>	482.8	594.8	495.1 <u>4/</u>	97.5	120.1

1/ Fund Alternate. Bank Alternates remained at \$11,500 until October 1, 1956, when they too were raised to \$14,000.

2/ Includes supplemental allowance.

3/ Based on the Index for February in each year.

4/ Based on the Index for March in each year.

5/ Prior to any adjustment in remuneration that may be granted effective July 1, 1983.

6/ If the recommendations of the Joint Committee for adjustments in remuneration, effective July 1, 1983, were to be approved, the real income figures would change as indicated.

Number of Staff With Salaries Above the Remuneration of  
Executive Directors and Alternates 1/

	Above Executive Directors				Above Alternates			
	Fund <u>2/</u>		Bank <u>3/</u>		Fund <u>2/</u>		Bank <u>3/</u>	
	Number	Percentage of total professional staff	Number	Percentage of total professional staff	Number	Percentage of total professional staff	Number	Percentage of total professional staff
1969	0	-	0	-	29	5.2	27	2.7
1970	0	-	2	0.2	45	7.3	47	3.8
1971	2	0.3	1	0.1	68	10.4	83	5.7
1972	2	0.3	0	-	56	7.8	61	3.5
1973	2	0.3	7	0.4	87	11.7	97	5.5
1974	2	0.3	0	-	66	8.8	94	5.0
1975	13	1.6	7	0.3	98	12.3	200	10.0
1976	13	1.6	9	0.4	113	13.9	227	10.3
1977	17	2.1	20	0.9	180	22.1	481	20.6
1978	13	1.6	15	0.6	145	17.6	328	13.5
1979	43	5.3	45	1.7	181	22.3	497	19.3
1980	74	8.9	148	5.3	223	26.8	626	22.5
1981	38	4.4	51	1.8	121	13.9	327	11.3
1982	39	4.2	46	1.5	125	13.4	330	11.1
1983	76	8.0	121	4.1	192	20.1	620	20.9
1983 <u>4/</u>	42	4.4	55	1.9	144	15.1	335	11.3

1/ Based on net salaries for staff and net remuneration, including supplemental allowance, for Executive Directors and Alternates.

2/ Situation at end of each calendar year except for 1983, where figures as of May 1 have been used.

3/ Situation at end of each calendar year except for 1983, where the figures represent the best estimate as of May 1.

4/ Situation as at July 1, 1983, if recommendations for adjusting Executive Directors' and Alternates' remuneration, effective July 1, 1983, were to be approved.



INTERNATIONAL MONETARY FUND

DRAFT RESOLUTION

Direct Remuneration of Executive  
Directors and their Alternates

RESOLVED:

THAT, effective July 1, 1983, the annual rates of remuneration of Executive Directors of the Fund and their Alternates pursuant to Section 14(e) of the By-Laws shall be as follows:

- (i) As salary, \$73,600 per year for Executive Directors and \$61,600 per year for their Alternates;
- (ii) As supplemental allowance (for expenses, including housing and entertainment expenses, except those specified in Section 14(f) of the By-Laws), \$8,500 per year for Executive Directors and \$6,800 per year for their Alternates.





INTERNATIONAL MONETARY FUND

DRAFT RESOLUTION

Home Leave Allowance for Executive  
Directors and their Alternates

RESOLVED:

THAT, effective with respect to home leave travel of the families of Executive Directors and Alternates commencing after July 1, 1983, a home leave allowance shall be paid to Executive Directors and their Alternates in the same amounts as it is paid in respect of the families of the staff.



FROM: J S BEASTALL  
DATE: 8 June 1983

PS/CHANCELLOR OF THE EXCHEQUER

cc Mr Littler  
Mr Unwin  
Mr Carey or  
Mr Sedgwick

PRIVATISATION IN THE LDCs

The Chancellor asked for a brief appraisal of this internal IMF paper, which was sent to him by a friend at the IBRD.

2. I attach a note prepared by the ODA economists.

*T a v.m.*

*V. intently*

*Quantity for next  
Working by [unclear]?*

*J S*

(J S BEASTALL)



CHANGING THE PUBLIC - PRIVATE MIX: A SURVEY OF SOME RECENT EXPERIENCES IN LDCs (IMF STAFF PAPER)

1. This paper reflects the growing concern in recent years with the role of the public sector in developing countries. For a mixture of ideological and pragmatic reasons most developing countries have expanded the size and scope of the public sector over the last quarter of a century in an attempt to develop and modernise their economies. Thus they have not only continued to provide economic and social infrastructure (eg utilities, railways, roads and health services) but have intervened directly in two other important areas, namely agriculture and manufacturing. In agriculture, some state farming apart, they have attempted to provide extension services and marketing for both inputs and outputs, often on a monopoly basis. In manufacturing (and mining) they have in some cases nationalised existing plants, which were often foreign owned, and used state owned enterprises (SOEs) to develop new industries. Furthermore, through legislation and regulation they have an important influence upon the performance of the private sector itself (eg taxation and price control).

2. Concern arises from the general level of efficiency of SOEs, and of other government departments providing services, and their financial burden on the central government budget. A combination of relatively high costs and low administered prices often results in operating losses and a continuing need for the government budget to finance new investment. There are, however, wider considerations such as the development of local entrepreneurial activity, particularly small scale enterprises which are generally more labour intensive and use less scarce capital. The paper itself lists the potential benefits of an expanded role for the private sector in terms of increased efficiency of enterprises and services provided under private ownership or management; increased efficiency of state enterprises subject to competition from the private sector; mobilising individual effort, skills, and finance; and encouraging a broader development of entrepreneurial abilities and more widespread economic development; leaving the state to concentrate its efforts on more central tasks.

3. The paper however is primarily concerned with the methods by which the private sector can be given a larger role:

(i) Divestiture

The paper provides a good analysis of why the sale of SOEs to the private sector has been limited to a few countries where there has been a change of ideology (eg Chile, Jamaica, and Pakistan). It points out that the main candidates for divestiture are



manufacturing enterprises which are not the main problem areas in terms of over-manning and financial burden. The undeveloped financial markets and lack of local entrepreneurs also reduces the scope for the sale of large-scale enterprises, and are often the reasons given for establishing them in the first place. Thus while the perceived benefits may not be large the perceived costs and risks in political terms may be high. Accepting that major divestiture of manufacturing enterprises is unlikely the paper argues for damage limitation (improving management and incentives, and reducing political interference) and using them more for skill training for the economy generally. It suggests that one solution is in introducing foreign management, possibly on a leasing basis. Although ODA's involvement in the Jubà Sugar Mill, Somalia, is cited as a model in this regard, the ODA has in general been reluctant to get involved in state manufacturing enterprises partly for the problems referred to above and partly because many are inherently uneconomic, depending upon high tariff protection to sustain them.

(ii) Private Provision of Services

The paper provides an array of examples of private services in education, health, marketing, irrigation, and transportation, and suggests, as did the Berg Report on Sub-Sahara Africa, that the possibilities for greater private participation in these areas should be pursued. The one of particular concern to ODA is agricultural marketing: in many countries state monopolies have been created which are grossly inefficient and which impede rather than promote agricultural development and are a financial drain on both government and farmer. Bus transportation is another obvious area where greater private sector involvement could help improve services and reduce costs. In other areas such as education, health and rural water supplies one can expect most developing countries to resist the idea of private services, but there is scope for more community participation and designing more cost-effective delivery systems, so that wider access to facilities can be made available within the severe financial limitation of central governments.





(iii) Contracting Services

The paper argues for the state concentrating more on organising and regulating services and the private sector being allowed to produce, manage, and deliver services. Although a number of areas are cited perhaps the most important for many poor countries is road maintenance. Road maintenance is poor in many countries because of inadequate financial provision combined with large over-staffed Public Works Departments. The paper refers to the successful experiment in Kenya where with government support small private contractors have developed their capability from being gravel hauliers to take on road maintenance contracts.

4. The 1983 World Development Report of the World Bank will have as its theme the management problems and role of the public sector. ODA's experience has led it to review its approach to assisting a range of sectors in developing countries, particularly in Africa. Institutional weakness, poor resource management and the imbalance between capital and recurrent expenditure are major concerns, suggesting that more emphasis needs to be given to technical co-operation and to the maintenance and better utilisation of existing assets rather than simply the acquisition of new capital assets. Not only do the private sector initiatives need supporting, but public sector activities which impinge upon the private activities need strengthening.





FROM: J O KERR

DATE: 9 June 1983

POWP

(will today's letter to Walton)

MR BEASTALL

cc Mr Littler  
Mr Unwin  
Mr Carey (OR)  
Mr Sedgwick

IMF INTERNAL PAPER ON PRIVATISATION IN THE LDCs

The Chancellor was most grateful for the ODA analysis of the Berg paper which you submitted yesterday and he found very interesting. He suggests that some of the issues touched on by Berg, and discussed by the ODA economists, might appropriately be briefly addressed in the UK speech at the September IMF/IBRD annual meetings.

J O KERR



THE SECRETARY OF THE TREASURY  
WASHINGTON, D. C. 20220

June 13, 1983

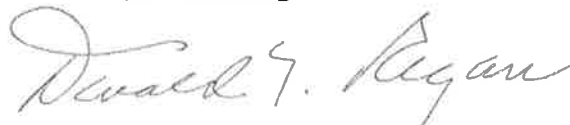
*Afa*  
*(MP)*

Dear Chancellor:

Congratulations on your recent appointment to the important post of Chancellor of the Exchequer. Clearly, this significant promotion is a sign of the trust and confidence that you have earned in your previous positions.

I wish you every success as you take on your challenging new duties. I look forward with pleasure to working closely with you and to seeing you in late July.

Sincerely,



Donald T. Regan

The Rt. Hon. Nigel Lawson  
Chancellor of the Exchequer  
H.M. Treasury  
Parliament Street  
London SW1P 3AG  
United Kingdom





INTERNATIONAL MONETARY FUND  
WASHINGTON, D.C. 20431

EX-CHEQUE

20 JUN 1983 ✓

Mr Litterer  
Mr Lowin  
Mr Lavelle  
Mr Lorey

CABLE ADDRESS  
INTERFUND

June 14, 1983

D

Sir:

This is to advise you that the Governors for Burma, Fiji, Indonesia, Lao People's Democratic Republic, Malaysia, Nepal, Singapore, Thailand, and Viet Nam have elected, effective July 1, 1983, Mr. J.E. Ismael to be Executive Director for the remainder of the term of office of Mr. A. Haman Habib whose resignation is effective close of business June 30, 1983.

Very truly yours,

Leo Van Houtven  
Secretary

The Rt. Hon. Lord Richardson  
of Duntisbourne, M.B.E., T.D., P.C.  
Governor  
Bank of England  
London, EC2R 8AH, England



INTERNATIONAL MONETARY FUND  
WASHINGTON, D.C. 20431

INTERNATIONAL  
CABLE ADDRESS

Mr. [Name]  
[Address]  
[City]

June 14, 1983



Sir

This is to advise you that the Government for [Country], [City], [Country],  
and [Country] have decided, effective July 1, 1983, to [Action].  
Executive Director for the remainder of the term of office of  
Mr. A. Hassan [Name] whose resignation is effective also at business

June 30, 1983.

Very truly yours,

Leo Van Houten  
Secretary

The Rt. Hon. Lord Richardson  
of Eastbourne, M.P., F.R.S., F.C.  
Governor  
Bank of England  
London, EC2R 9AH, England





INTERNATIONAL MONETARY FUND  
WASHINGTON, D. C. 20431

(Pmf)

EXCHEQUER	
RBC	27 JUN 1983
<del>ACTION</del>	Mr Whitler
COPIES	Mr Clavin
50	Mr Lavello
	Mr Carey

CABLE ADDRESS  
INTERFUND

June 15, 1983

Sir

This is to inform you that, in accordance with the vote carried out under the provisions of Section 13 of the By-Laws, the Resolution submitted to the Board of Governors on May 16, 1983 concerning the Salary of the Managing Director has been adopted.

Very truly yours,

Leo Van Houtven  
Secretary

The Rt. Hon. Lord Richardson  
of Duntisbourne, M.B.E., T.D., P.C.  
Governor  
Bank of England  
London, EC2R 8AH, England



INTERNATIONAL MONETARY FUND

WASHINGTON, D. C. 20431

5 JUN 1982

Mr. [unclear]	✓
Mr. [unclear]	
Mr. [unclear]	
Mr. [unclear]	

(Handwritten initials)

June 18, 1982

212

This is to inform you that, in accordance with the vote recorded on the provisions of Section 12 of the By-Laws, the Resolution submitted to the Board of Governors on May 18, 1982 concerning the Salary of the Managing Director has been adopted.

Very truly yours,

David M. [unclear]  
Secretary

(Handwritten signature)

The Rt. Hon. Lord [unclear]  
of Bantshoune, M.S.E., T.D., F.C.  
Governor  
Bank of England  
London, EC2H 8AH, England

MAIL ADDRESS  
INTERNATIONAL