CONFIDENTIAL

CC AW. (2)

Prime Minister

To note. The risk is that, if we lose our present place in the IMF, we may go down a number of places and that our position on the Executive Board will be in the long run threatened

MCS 27/4

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

26 April 1982

Michael Scholar Esq.
10 Downing Street
LONDON
SW1

MS

Dear Michael,

WORLD BANK GENERAL CAPITAL INCREASE

The World Bank are currently undertaking a general capital increase, approved in January 1980, to double their capital to $ 80 billion. Some 90 per cent of the GCI shares were to be allocated to member countries in proportion to their existing subscriptions. The Prime Minister may wish to know that Treasury and FCO Ministers have now agreed to accept a proposal from the World Bank that we should give up half the new shares allocated to us. This is one of the rare occasions when we can save public expenditure (at least £60 million) and reduce the multilateral element in the aid budget, while at the same time gaining credit for helping the Bank (which needs the shares to satisfy other claimants such as Saudi Arabia.)

The Chancellor has carefully considered the implications for our position in the IMF because of the traditional link between shareholdings in the two Bretton Woods institutions. It is of course in our general interest to maintain as high an IMF quota as we legitimately can, although our relative position is likely to fall in the long run because of the decline in our relative economic strength. However, because of the special circumstances surrounding the Bank's request, agreeing to it should not prejudice our negotiating position in the current IMF Quota Review. If in the forthcoming Aid Framework discussions Ministers decide to take up the other 50 per cent of the shares allocated to us under the general capital increase, we would still remain comfortably in second place among the shareholders in the Bank.

/Copies of

Copies of this letter go to Brian Fall (FCO), Jonathan Spencer (DOI), John Rhodes (DOT) and David Wright (Cabinet Office).

Yours ever,

John Kerr.

J.O. KERR
Principal Private Secretary

26 APR 1982

c.c. Alan Walters

Economic Policy

10 DOWNING STREET

From the Private Secretary

29 April, 1982.

World Bank General Capital Increase

Thank you for your letter of 26 April about the World Bank General Capital Increase.

I have shown this letter to the Prime Minister, who has noted it without comment.

I am sending copies of this letter to Brian Fall (Foreign and Commonwealth Office), Jonathan Spencer (Department of Industry), John Rhodes (Department of Trade), and David Wright (Cabinet Office).

John Kerr, Esq.,
HM Treasury.

CONFIDENTIAL

FEBRUARY 22, 1982

IMF Survey

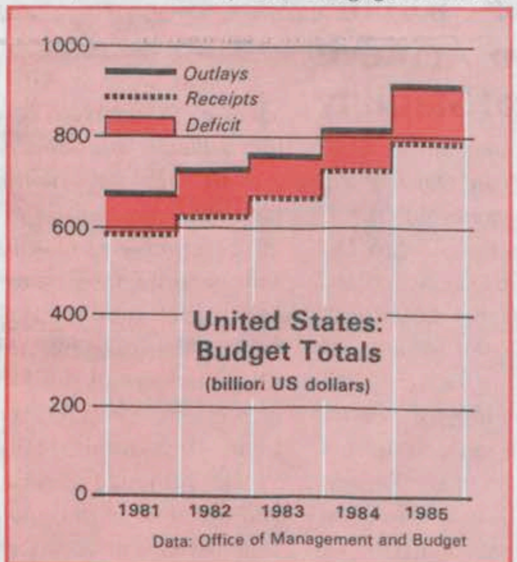
Countries of Sahelian Region Face Problems of Adjustment

The countries of the Sahelian region of Africa face difficult problems of adjustment in their efforts to recover from the external setbacks that slowed their growth during the 1970s. The economic and financial programs of these countries and the role of the Fund in assisting their development efforts are described in two articles which begin on pages 50 and 52 of this issue. The articles are adapted from lectures delivered by Oumar B. Makalou, Deputy Director of the Fund's African Department, and Saleh M. Nsouli, Assistant to the Director, at the Club du Sahel Seminar on Recurrent Expenditures, held in Ouagadougou in January 1982.

in this issue . . .

U.S. Budget Is Designed To Contain Spending and Break Inflationary Spiral

U.S. President Reagan's budget proposals for fiscal year 1983 are designed, in the President's words, to be consistent with his Administration's program to break "the inflation spiral" and "try and bring government spending back in line with government revenue." Under the proposals, which were transmitted to the Congress on February 8, total budget revenues in fiscal year 1983, beginning October 1, 1982, are estimated at $666.1 billion, an increase of $39.4 billion from the $626.8 billion estimated for fiscal year 1982. Outlays are estimated at $757.6 billion in fiscal year 1983, an increase of $32.3 billion over the estimated level of $725.3 billion for fiscal year 1982. The federal budget deficit in fiscal year 1983 is forecast at $91.5 billion, compared with the projected deficit of $98.6 billion in fiscal year 1982.



In his budget message, the President acknowledged that the (Please turn to page 57)

SDR Department Transfers Maintained a High Level In the Third Basic Period

Total transfers in the SDR Department during 1981 amounted to SDR 7,393.6 million—less than in 1980, which included the obligatory use of SDRs to make quota payments, but higher than any other year since the inception of the facility in 1970. The accompanying table summarizes transfers of SDRs in the third basic period, 1978–81.

Among the major categories, transactions with designation amounted to SDR 1,747.5 million during 1981, surpassing the previous annual record of SDR 1,316 million in 1980; as in the past three years, the high volume of this activity largely reflects the simultaneous use of SDRs received as part of the proceeds of purchases by members from the General Resources Account.

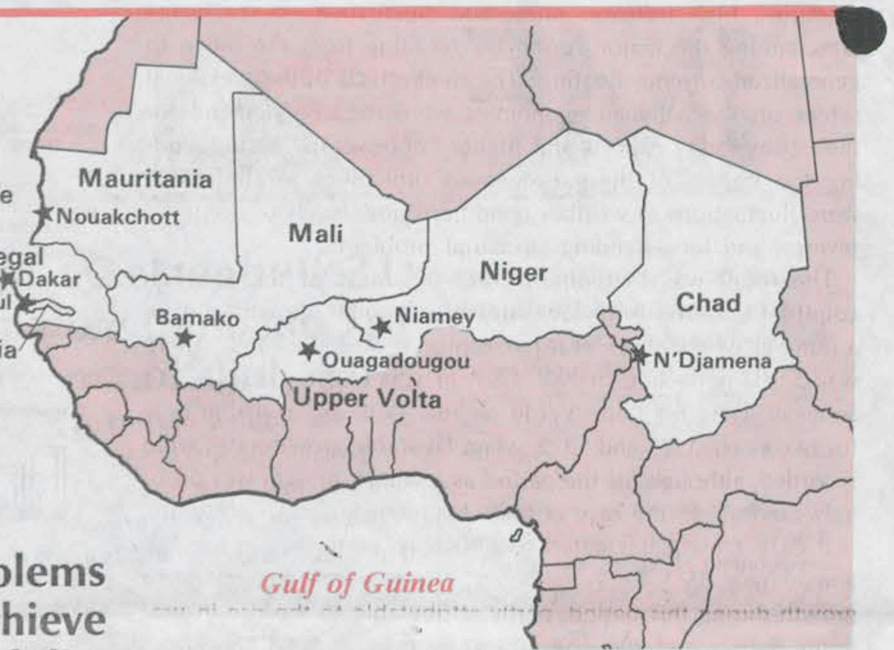
Transactions by agreement between participants and other holders amounted to SDR 896.0 million last year, more than twice the volume in 1979 and 1980; in most cases, the participants (Please turn to page 61)

Transfers of SDRs in Third Basic Period
(million SDRs)

	1978	1979	1980	1981
Total transfers	**5,364.9**	**4,238.0**	**10,889.8**	**7,393.6**
Transfers among participants and other holders				
Transactions with designation	851.7	1,311.3	1,316.0	1,747.5
Transactions by agreement	1,827.1	318.5	346.8	896.0
Prescribed operations	—	—	—	31.3
Subtotal	**2,678.8**	**1,629.7**	**1,662.9**	**2,674.8**
Transfers from participants to General Resources Account				
Repurchases	347.3	492.0	1,274.7	830.1
Charges	746.7	584.2	519.4	718.0
Quota payments	219.9	0.9	5,088.1	267.5
Assessment	0.9	1.7	1.0	1.6
Interest on holdings	39.8	57.1	81.8	265.8
Subtotal	**1,354.6**	**1,136.0**	**6,965.0**	**2,082.9**
Transfers from General Resources Account to participants and other holders				
Purchases	1,024.9	1,266.0	1,555.9	1,962.2
Remuneration	136.3	139.7	219.5	348.2
Reconstitution	120.4	—	5.8	18.8
Repayments of Fund borrowing	15.5	50.1	108.3	220.0
Interest on Fund borrowing	23.2	16.4	31.8	82.4
Acquisition to make quota payments	—	—	340.7	—
Other	11.3	0.1	—	4.3
Subtotal	**1,331.6**	**1,472.3**	**2,261.9**	**2,635.9**

Note: Components may not add to totals because of rounding.
Data: IMF Treasurer's Department

NATIONAL ECONOMIES



In Decade of 1980s . . .

Facing Severe Adjustment Problems Sahelian Countries Seek to Achieve Economic Growth, Financial Stability

This article and the following article are based on lectures by Oumar B. Makalou, Deputy Director, African Department, entitled "The Sahel Countries: Some Macroeconomic Issues," and by Saleh M. Nsouli, Assistant to the Director, African Department, entitled "The Role of the Fund in Financing and Adjustment with Particular Reference to the Sahel Countries." The lectures were delivered at the Club du Sahel Seminar on Recurrent Expenditures, held in Ouagadougou in January 1982.

The Sahelian countries had to cope with a number of external factors during the 1970s that disrupted their growth efforts. These included a severe drought in the first part of the decade, the slowdown in economic activity in the industrial countries, the increase in oil prices, and unfavorable movements in Sahelian terms of trade. As the authorities attempted to cope with these developments while, at the same time, continuing to promote economic growth, internal and external financial imbalances were aggravated. Accordingly, in the decade of the 1970s the Sahelian countries suffered from low rates of economic growth, high rates of inflation, and large external deficits. As they enter the decade of the 1980s, the Sahelian countries face difficult problems of adjustment, the primary objective being to achieve sustainable rates of economic growth under conditions of financial stability. The task is not an easy one, particularly in light of the sober outlook for the world economy.

The Sahelian Countries: Selected Economic Indicators
(per cent)

Real Growth of Gross Domestic Product

	1975	1976	1977	1978	1979	1980	1981
Cape Verde	—	—	—	5.9	10.9	—	—
Chad	7.8	5.0	1.5	3.6	−20.0	−10.0	3.0
The Gambia	−4.3	0.9	−13.2	−1.1	0.9	−1.0	2.0
Mali	13.5	13.6	11.0	−1.4	10.9	−1.2	−0.7
Mauritania	10.1	6.7	−0.4	−7.5	4.3	1.3	4.0
Niger	—	—	3.5	8.1	12.0	5.3	3.7
Senegal	7.9	7.3	1.3	−7.7	12.4	−7.6	−5.2
Upper Volta	7.7	3.8	−2.6	2.3	1.4	2.7	2.0

Inflation Rate (Consumer Price Index)

	1975	1976	1977	1978	1979	1980	1981
Cape Verde	40.9	7.8	11.2	13.3	6.9	—	—
Chad	15.3	3.4	9.3	12.2	20.0	12.0	15.0
The Gambia	25.9	17.1	12.3	8.8	6.1	6.8	9.0
Mali	9.0	8.1	21.9	30.3	−0.1	20.2	6.9
Mauritania	11.8	14.5	10.3	7.1	11.4	10.0	10.0
Niger	—	23.5	23.3	10.0	7.3	10.3	17.0
Senegal	31.6	1.1	11.3	3.5	9.6	8.7	13.0
Upper Volta	18.8	−8.4	30.0	8.2	15.0	12.2	12.0

Data: IMF African Department

Characteristics of the Sahel. The term Sahel refers to a region in western Africa occupied by eight countries—Cape Verde, Chad, The Gambia, Mali, Mauritania, Niger, Senegal, and Upper Volta. Although diverse in several respects, notably in size and distribution of population, area, and per capita income, the Sahelian countries share a number of common characteristics. First, they are predominantly agricultural economies. In most of the countries, about 70 to 80 per cent of the population is employed by the agricultural sector and nearly one third of gross domestic product (GDP) value-added is directly contributed by this sector. The manufacturing sector, as well as the commerce and transportation sectors, is heavily dependent on agriculture, with the result that the overall performance of most of these economies is highly vulnerable to weather conditions. Second, the exports of the Sahelian countries are heavily concentrated in one or two items, in most cases agricultural products or livestock. One exception is Niger, where in recent years uranium exports have risen markedly and currently constitute nearly 80 per cent of total export proceeds. Third, the demand for imports is highly inelastic, as there is little substitutability between domestic products and imported goods. Fourth, the countries share the problem of financial constraints, both domestic and external. Domestic savings are generally extremely low and there is a high resource gap, as reflected in the current account deficits of the balance of payments of these countries. There is a tendency to rely on foreign grants and borrowing and for an accumulation of domestic and external arrears.

Recent Developments. The period 1975–80 was generally a turbulent one for the entire world economy, characterized by large imbalances between the oil exporting and non-oil exporting countries, a slowdown in economic activity in the industrial countries, high inflation rates, and fluctuations in exchange rates among the major currencies resulting from the move to generalized currency floating. The chief effects of these external forces on the Sahelian economies were reduced demand for their commodity exports and higher import costs. Compounding the impact of these exogenous difficulties for the Sahel were fluctuations in weather conditions, low levels of domestic savings, and long-standing structural problems.

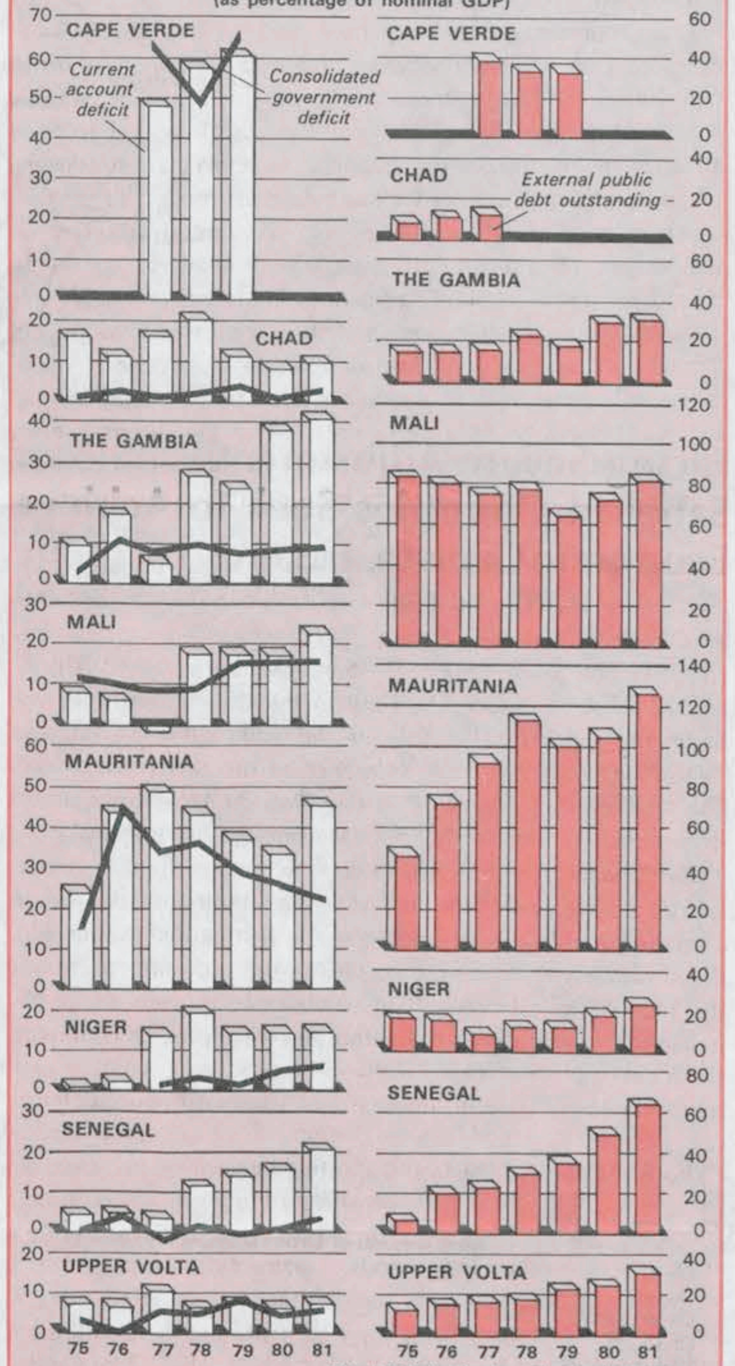
The result was that, during 1975–80, most of the Sahelian countries suffered from low rates of economic growth and, in a number of countries, real per capita income declined. There was a sharp decline in real GDP in Chad, The Gambia, and Senegal. Data for Cape Verde on real GDP are available only for two years, 1978 and 1979, when favorable growth rates were recorded, although for the period as a whole, growth was probably modest. In the case of Mali, Mauritania, and Upper Volta, real GDP growth fluctuated considerably, recording an average annual rate of 3 to 5 per cent. Niger witnessed significant growth during this period, partly attributable to the rise in uranium output and the ensuing increase in financial resources that permitted a high level of capital formation.

Domestic Policy Responses. As the Sahelian countries attempted to stimulate economic activity in the 1975–80 period, notwithstanding the adverse internal and external factors, the financial policies pursued led to a rapid expansion in aggregate demand. The efforts of the authorities to promote economic growth are reflected in the relatively high levels of capital formation as a proportion of GDP, which account in most cases for about 20 to 30 per cent of GDP and as high as about 70 per cent for Cape Verde. Domestic savings were considerably lower, accounting in a number of cases for only a small fraction of investment, while in at least three countries dissaving occurred. As most of the investment effort was carried out by the government sector, and as current expenditures rose rapidly, pressure on budgetary positions was considerable. In some cases these public deficits were relatively small, but in some instances they reached one to two thirds of GDP. Since the government sector deficits were partly financed through domestic bank borrowing, credit to the government in these countries increased rapidly during this period. With credit to the nongovernment sector also expanding at a fast pace, overall domestic credit and domestic liquidity expansion grew sharply.

The fast rise in aggregate demand, notwithstanding the adverse trends in the production sector, exerted pressure on domestic prices in the Sahelian economies. The overall regional rate of inflation was high during this period, fluctuating for most countries between 10 and 30 per cent and averaging between 10 and 20 per cent. It should be noted, however, that the recorded rates of inflation may not fully reflect the inflationary pressures in certain cases, as most Sahelian countries had extensive systems of price controls and subsidies.

The excess demand pressures were also reflected in external sector developments. During this period, exports as a proportion of GDP generally declined, while imports as a proportion of GDP increased. Oil imports as a percentage of total imports also increased. The adverse movements in the terms of trade contributed to these developments. Accordingly, the current account deficits widened for most of the Sahelian countries. In 1981, Cape Verde had a current account deficit equal to nearly two thirds of GDP, while The Gambia, Mali, Mauritania, and Senegal recorded deficits ranging between one fourth and one half of GDP. Chad and Niger had deficits of about 10 to 15 per cent of GDP, and Upper Volta of about only 7 per cent. Again, in certain cases, because of exchange controls on current transactions, these deficits did not fully reflect excess demand pressures.

The Sahelian Countries: Selected Economic Indicators
(as percentage of nominal GDP)



Data: IMF Staff estimates and national sources

Net capital inflows partly offset the current account deficits. However, insofar as these inflows partly consisted of foreign borrowing, the external debt burden of the Sahelian countries rose markedly. By 1981, the external public debt outstanding exceeded GDP for one country, and ranged between one fourth and two thirds of GDP for most of the others. The rising debt burden was reflected in high debt service ratios. These ranged between about 10 and 30 per cent in 1981. Furthermore, the external reserves of the Sahelian countries were reduced considerably as a proportion of imports.

Four important issues may have had an impact on these developments: (1) Most Sahelian countries continued to maintain widespread price controls and to provide subsidies on basic consumer goods. Inadequate producer prices tended to have an adverse impact on the financial incentives to producers, while low fixed prices (as well as subsidies) tended to encourage consumption. The subsidies also constituted a burden on the budget. (2) Interest rates were kept at relatively low levels, discouraging savings, limiting financial intermediation, adversely affecting resource allocation, and in some cases favoring net capital outflows. (3) A number of countries continued to maintain public enterprises in operation, even though some tended to incur losses. (4) Because of pressure on the external sector and limited exchange rate adjustment, a number of Sahelian countries had restrictions on current international transactions.

In sum, the decade of the 1970s was a difficult one in which external developments and domestic financial policies combined to aggravate the economic problems facing the Sahelian countries.

Macroeconomic Issues for 1980s. Apart from the scarcity of financial resources available to the Sahelian countries, they will have to deal with the difficult task of achieving financial stability to promote a satisfactory and sustainable rate of economic growth in the current decade. The large disequilibria that most of the Sahelian countries are suffering from make the process an even more difficult one.

In seeking to improve their economic positions, the authorities in the Sahelian countries will be considering various economic policy responses. The more important aspects include development planning, pricing policies, the role of public enterprises, fiscal policy measures, the role of monetary policy, as well as policies affecting the external sector.

Briefly, in order to promote economic growth, consideration will have to be given to strengthening the development planning process to ensure that comprehensive plans that set priorities within the context of an appropriate macroeconomic framework can be prepared. In addition, in order to improve resource allocation and mobilize domestic savings, as well as encourage private sector investment, close attention will have to be paid to pricing policies. Further, the position of public enterprises, which play an important role in these economies, is being reviewed in a number of these countries to ensure that they operate efficiently and profitably and to determine whether those enterprises, which often incur substantial losses, are providing social services valuable enough to justify government subsidies. On the financial front, many of the Sahelian countries may view the adoption of a more restrained fiscal policy in the 1980s as necessary to allow the pursuit of a more flexible credit policy toward the nongovernment sector, within the constraints of a monetary policy consistent with domestic and external financial stability. With regard to external sector policies, the reduction of restrictions on international current transactions and the pursuit of appropriate exchange rate policies, where applicable, could contribute to stimulating economic growth and reducing external imbalances.

Assistance to Sahelian Countries Is Intended to Help Them Correct Persistent Imbalances in Payments

The Fund has worked closely with the countries in the Sahelian region, providing them with considerable financial and technical assistance in recent years. Several Fund facilities were available to the Sahelian countries in the 1970s. These countries had access to their reserve tranches, to credit tranches—both under stand-by arrangements and the extended Fund facility—with the amounts augmented through the supplementary financing facility and the compensatory financing facility, which provides financial assistance for export shortfalls and, more recently, for the increased costs of cereal imports. They also had access to the oil facilities operational in 1974 and 1975 to assist countries in meeting their higher payments for oil imports. Also available were the Trust Fund and two subsidy accounts, one associated with the oil facility and the other with the supplementary financing facility.

During the decade of the 1970s through 1980, nearly all the Sahelian countries utilized most of the Fund's financial facilities. The chart (page 53) provides the total amount of Fund resources, including SDR allocations, made available to the Sahelian countries from 1970 through 1980. During this period, the level of Fund financial assistance to the Sahelian countries increased sharply. Total net purchases (excluding SDR allocations) rose from SDR 2 million in 1970 to SDR 82 million in 1980. As a proportion of their balance of payments deficits during 1975–80, total Fund financial assistance amounted to about 50 per cent.

The Fund has also provided technical assistance of various types to most of these countries. This has consisted of visits by Fund staff to prepare specific technical studies, the assignment of resident experts through the services of the Central Banking Department, and the training of staff from the various countries at the IMF Institute in Washington.

Extent of Current Imbalances. The severity of the economic and financial imbalances that the Sahelian countries will encounter in the 1980s is difficult to assess, since much will depend on the international economic environment. Nonetheless, a review of the basic economic and financial developments in 1980 indicates that, with the exception of Niger, which recorded a real growth in per capita gross domestic product (GDP) of 2.5 per cent, real per capita income declined in most of the countries in 1980. Savings remained negative in about half the Sahelian countries, while in the others the proportion of savings to GDP was low. By comparison, investment continued at a high pace, ranging between 20 and 35 per cent.

The budgetary deficits continued to be high and partly contributed to a rapid growth in domestic credit. The overall growth in domestic liquidity was generally incompatible with financial stability. Largely reflecting these developments, rates of inflation, notwithstanding price controls and subsidies, were above 10 per cent for most Sahelian countries, and the current account deficits as a proportion of GDP increased further in 1980, leading to an additional increase in external debt. Preliminary data indicate that a further deterioration in the economic positions of the Sahelian countries occurred in 1981.

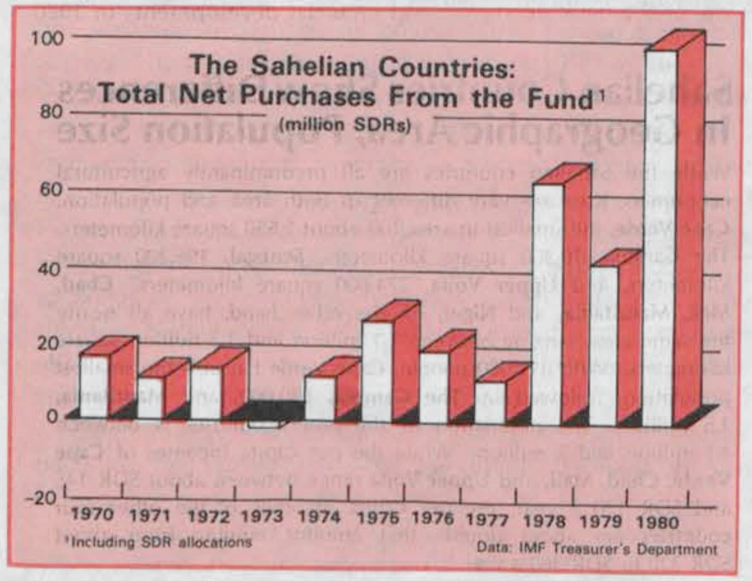
Two indicators—namely, the investment-savings gap and the current account deficit as a proportion of GDP—are particularly useful in assessing the extent of the disequilibria facing the Sahelian economies. Although in general these ratios are close, they may differ due to differences in coverage, particularly due to the inclusion of net transfers in the current account. The concept of savings used here refers to domestic savings, excluding transfers. For 1981, these ratios are shown in the table. The investment-savings gap is over 20 per cent of GDP for most of these countries. The current account deficits as a proportion of GDP are over 40 per cent for The Gambia and Mauritania, over 20 per cent for Mali and Senegal, and between 7 and 15 per cent for Chad, Niger, and Upper Volta. These indicators suggest that the magnitudes of these imbalances are not sustainable and that the adjustment effort facing the Sahelian countries is a major one.

Sahelian Countries Show Differences In Geographic Area, Population Size

While the Sahelian countries are all predominantly agricultural economies, they are very different in both area and population. **Cape Verde,** the smallest in area, has about 1,550 square kilometers, **The Gambia,** 10,300 square kilometers, **Senegal,** 196,200 square kilometers, and **Upper Volta,** 274,000 square kilometers. **Chad, Mali, Mauritania,** and **Niger,** on the other hand, have all nearly the same area, ranging between 1.1 million and 1.3 million square kilometers. With 311,000 people, **Cape Verde** has also the smallest population, followed by **The Gambia,** 620,000, and **Mauritania,** 1.5 million. The population of the other countries is between 4.5 million and 7 million. While the per capita incomes of **Cape Verde, Chad, Mali,** and **Upper Volta** range between about SDR 145 and SDR 170 a year, the per capita incomes of the other four countries are about double that amount, ranging from about SDR 320 to SDR 360 a year.

The Sahelian Countries: Indicators of Financial Imbalances, 1981
(per cent)

	Investment-Savings Gap/GDP	Current Account Deficit/GDP		Investment-Savings Gap/GDP	Current Account Deficit/GDP
Cape Verde	...	...	Mauritania	32.7	45.3
Chad	...	9.9	Niger	12.4	14.2
The Gambia	28.5	40.4	Senegal	23.6	20.5
Mali	21.2	22.3	Upper Volta	29.3	7.0



In assessing the need for adjustment, it is important, in general, to distinguish between balance of payments disequilibria that are self-reversing in nature and those that are not. A self-reversing disequilibrium may arise primarily because of an exogenous shock, such as a change in weather conditions that may affect the export harvest, a development that may be viewed as being nonrecurrent in nature. By contrast, if the disequilibrium has arisen either because of exogenous factors that can be considered to be of a lasting nature, such as a permanent change in the terms of trade, or because of a gradual buildup of excess demand pressures resulting from a faster expansion in domestic demand relative to domestic supply, the country would be considered to have a non-self-reversing disequilibrium.

Under the latter circumstances, the choice facing the country is not one of financing or adjustment. A country that fails to adopt adjustment measures would, inevitably, be drawing down its reserves and/or increasing its net foreign indebtedness. There is obviously a limit to this process that would be encountered when reserves have reached a low level and when new lines of foreign credit have become more difficult to obtain. Furthermore, a vicious circle is created in which the rising debt service ratio contributes to a further weakening in the balance of payments of the country. Moreover, a protracted period of financing without adjustment would simply mean that over time relative prices are maintained domestically at an increasingly incorrect level. In addition, to the extent that restrictions on external transactions are introduced to limit the financing necessary, inflationary pressures and the underlying disequilibria are exacerbated. Accordingly, by deferring the measures necessary to bring about adjustment, a country could create severe distortions in its economy that would adversely affect allocative efficiency and have a potentially damaging impact on growth. Consequently, when adjustment finally becomes unavoidable, drastic measures may be required. This is why the Fund encourages countries to take the initiative in adjusting at an early stage, when disequilibria are beginning to emerge and when the magnitude of the problems is still of a manageable proportion.

Fund Conditionality and Adjustment. The above-mentioned considerations explain the rationale behind the conditionality associated with the use of Fund resources. The essence of Fund conditionality is that, when a non-self-reversing balance of payments disequilibrium emerges, financing and adjustment must go together. The Fund attempts to provide the necessary financing in order to help countries phase in at an appropriate pace their adjustment policies, so as to minimize the burden of adjustment. The Fund has repeatedly emphasized that the corrective strategy of the financial policy program supported by the use of Fund resources is aimed at establishing internal and external financial balances conducive to placing the economy onto a sustainable growth path.

Conditionality has not been a static concept at the Fund; rather, it has evolved over time. In 1979, new guidelines on conditionality were introduced. These emphasized that there was a need to encourage members to adopt corrective measures at an early stage of their balance of payments difficulties; that adjustment periods longer than those normally associated with a one-year or two-year stand-by arrangement were often required; that a flexible approach for the treatment of external borrowing in adjustment programs needed to be adopted; and that due regard had to be given to the domestic social and political objectives, economic priorities, and the circumstances of individual members, including the causes of their balance of payments problems. Within these general guidelines, considerable flexibility in the application of conditionality has been maintained. Greater emphasis has been given to providing large-scale financing to support the adjustment efforts of member countries.

When the Fund is called upon to discuss the possible use of Fund resources with a country, there are four stages involved prior to agreement on a program. First, the Fund undertakes to study carefully the unique economic conditions of each country and to determine the sources of imbalance. Second, an attempt is made to identify the targets to be achieved under the program. Third, once the targets have been determined, the instruments of adjustment are then selected as well as the relative extent of their use. Fourth, the time period needed to achieve the targets is defined. The duration of the adjustment effort will indicate, together with the magnitude of the disequilibria involved, the extent of financing that will be needed.

In assisting the authorities in devising adjustment programs, in addition to emphasizing the importance of demand management policies, the Fund is paying increasing attention to ways and means of stimulating the supply side so that the effort of adjustment is not a purely deflationary one. In particular, a reorientation of resources toward production can help restore equilibrium, while better maintaining employment and capacity utilization. Attempts to achieve such a reorientation, however, can be frustrated by financial imbalances if supply and demand management policies are not implemented simultaneously.

While Fund programs concentrate on broad macroeconomic financial variables, such as fiscal, monetary, and exchange rate policies, the demand and supply effects of these policies, as well as the required consistency of the accompanying macroeconomic policies, including investment and pricing policies, are a primary concern of the Fund. The discussion that follows addresses important aspects of adjustment policy in the Sahelian countries, elaborating further on policy considerations referred to in the preceding article.

Perhaps most important, fiscal policy plays a vital role in the Sahelian countries through its impact on the level of aggregate demand and through government investment. Owing to the rapid growth in government deficits in recent years, however, it would appear important in the Sahelian countries to contain the growth in expenditures and to re-examine government expenditure priorities. The former would be needed to limit the rise in aggregate demand, while the latter would be required to determine the possible shift of government expenditure from pure consumption to recurrent expenditures necessary to maintain past investments and to capital expenditures designed to enhance the productive capacity of the country. In this regard, a strengthening of the development planning process could be helpful in maximizing the return on investment. In a number of Sahelian countries, public enterprises place a considerable financial burden on the budget, as they are used partly to implement some government social policies, incurring in some cases, considerable losses. The re-examination of the operations of these enterprises, with a view to improving their efficiency, could help reduce their dependence on the government and generate savings. On the revenue side, while it would be difficult to increase substantially the tax burden in a number of Sahelian countries, a reform of the tax structure could permit a more equitable distribution of the tax burden and enhance resource allocation.

Second, monetary policy must complement the adjustment role played by fiscal policy. The supply of credit to the nongovernment sector must strike a delicate balance between satisfying the genuine needs of domestic economic activity while not being so expansionary as to lead to excessive domestic credit growth. The temptation in many cases is to squeeze nongovernment credit to meet the requirements of the public sector; this crowding-out effect needs to be avoided to promote economic growth.

In this context, it is important to review carefully interest rate policy. In most Sahelian countries, the tendency has been to maintain relatively low interest rates. While it is debatable whether an increase in interest rates would substantially raise domestic savings in the Sahelian countries, it appears that low interest rates may be discouraging the inflow of savings into the banking system and may be encouraging investment in low-productivity projects. From a purely supply-oriented viewpoint, higher interest rates would contribute under an adjustment program to improving resource allocation by channeling investment into higher-productivity projects. Furthermore, such an interest rate policy would be more in line with the scarcity of capital resources in developing countries and could thereby promote the development of more labor-intensive technology.

Third, exchange rate policy can be an important element of adjustment, depending upon the circumstances of the specific country. It is usually argued that in the case of African countries the impact of an exchange rate devaluation would not be very significant, because of the inelasticity of supply and because African countries are generally price takers on the international market. An exchange rate change would increase equiproportionally prices of imported and exported goods and, with a lag, the prices of nontraded goods and services. As a result, once real monetary balances have adjusted, relative prices will have reverted to their original position, and the only impact of the devaluation will have been an inflationary one. There is a validity to this argument under very specific conditions, namely that the economy is not subject to restrictions on trade and payments and that the prices of nontraded goods and services adjust fully. In the case of many African countries these conditions often do not apply. In order to cope with the excess pressures on the balance of payments, a number of countries have imposed elaborate exchange and trade controls. The ensuing scarcities of imported goods drive up the prices of such goods, while the relative prices of exports, valued at the official exchange rate, are eroded, resulting in a reduction of production incentives for exports. In such a situation, a devaluation, accompanied by a reduction of exchange and trade restrictions, could lead to a rise in the domestic price of exports relative to imports, as the latter would no longer command a scarcity value. Furthermore, with the pursuit of restrained financial policies and a complementary incomes policy, the prices of nontraded goods and services would not rise equiproportionally. Under such conditions, an improvement in the external sector position, accompanied by a reduction in price distortions, would result.

Appropriate pricing policies are essential for improving resource allocation, mobilizing savings, and encouraging private sector investment. In the case of the Sahelian countries, many of which maintain extensive systems of price controls and subsidies, the overall reduction in excess demand pressures under an adjustment program would enable the Governments to reduce any administrative measures to control prices that they may have implemented and to reduce the scope of subsidies. The re-establishment of a degree of financial balance, together with appropriate exchange rate policies, can enable Sahelian Governments in some instances to adjust upward the producer prices of agricultural products, triggering a favorable supply response. In view of current world conditions, it is particularly important that an appropriate pricing policy for energy be adopted as part of the adjustment effort in order to limit external payments for energy imports.

It is apparent that the adjustment program must be comprehensive and affect every facet of the economy. In each case, the Fund designs programs in close cooperation with the local authorities to deal with the specific circumstances facing each country. In monitoring the progress of programs, the Fund focuses only on a few major macroeconomic variables that are used as indicators of whether or not the adjustment effort is on track. The purpose of these performance criteria is to trigger discussions on corrective measures should there be a deviation from the expected evolution.

The emphasis that the Fund is giving to formulating programs that meet the policy objectives of the African member countries, as well as the increase in the duration of the programs and an expansion in the scale of financing, is encouraging more countries to work closely with the Fund. Notwithstanding the increased financial assistance from the Fund, it is clear that Fund resources can contribute only partially to resolving the financing needs of the African countries in the coming years. Other assistance is urgently needed to limit the impact of the current world economic situation on the growth prospects of the Sahelian as well as of other developing countries.

SELECTED TOPICS

Efforts to Develop Islamic Financial Systems Focus on the Abolition of Fixed Interest Rates

A fuller version of this article will appear in the next issue of the Fund's quarterly journal, Staff Papers.

In recent years, a number of steps have been taken toward the Islamization of the financial system in countries in the Middle East and Asia. These measures should be viewed as an integral part of an attempt to move toward the Islamic ideal of a society based on the principle of social justice. As one element of this policy, a number of Moslem countries have made efforts to abolish *riba,* which is the word for usury and interest, and which is more precisely defined as the *fixed* return for the use of money.

The issue of abolishing fixed interest rates was raised in 1973 at the Islamic Conference. Measures to Islamize the financial system have been introduced in various countries, specifically Bahrain, Jordan, Kuwait, Malaysia, Saudi Arabia, Sudan, the United Arab Emirates, and most notably in Pakistan. In general, Islamization has consisted largely in founding Islamic banks that operate without charging or paying fixed interest rates on loans or deposits.

This article describes the Islamic attitude toward interest and profit; then analyzes the working of an Islamic banking system based on a profit and loss sharing (PLS) principle; and discusses the possible impact of such a system on the mobilization of savings, on the allocation of scarce resources through banks, on investments, and on the effectiveness of monetary policy, before drawing some tentative conclusions.

Interest and Profit. In any consideration of Islamic views on interest and profits, it should be appreciated that one important Islamic commitment is the condemnation of usury. In various verses the Koran prohibits *al-riba;* however, the interpretation of this prohibition is controversial, with the main controversy revolving around the question of whether the Koran simply prohibits excessive or exploitative interest or any fixed nominal return on money.

The former "modernist" view regards interest as legally prohibited when money is lent at exorbitantly high interest rates and thereby exploits the borrower. According to this view, interest charges may be permitted in certain cases: (1) where they are used by the government to induce savings; (2) in the financing of trade; (3) as a form of punishment; and (4) on loans for productive investments. As opposed to this rather pragmatic viewpoint, the "conservative" view forbids every form of fixed interest as being prohibited by the Koran. The grounds for this view are the following: (1) interest or usury reinforces the tendency for wealth to accumulate in the hands of a few and dehumanizes man's concern for his fellow men; (2) Islam does not allow gain from financial activity, unless the beneficiary is also subject to the risk of potential loss; and (3) Islam regards the accumulation of wealth through interest as selfish. It is also sometimes argued that interest rates discourage investment and employment creation.

To date, specific measures toward the development of an Islamic financial system have generally aimed at the abolition of all forms of fixed nominal interest and have consequently avoided possible questions about how to define "acceptable" levels of interest or systems of price indexation. Although fixed rates are to be abolished, however, that does not mean there is no remuneration of capital. The making of profit is generally accepted in Islam, unless such profits are "unrestricted" and "abnormal," e.g., from monopolies or cartels.

In contrast to interest, a profit share is not predetermined and fixed, but is uncertain and variable, and may even be negative. As long as profits and losses are shared among savers, investors, and financial institutions, such a financial system would comply with the Islamic principle of *shirakat,* which means partnership or cooperation. In Islamic finance the technical name for partnership between the supplier of capital and the user of capital is *modaraba*.

Methods of Financial Intermediation. The most far-reaching experiments with the PLS system have been carried out in Pakistan, where the abolition of *riba* is an objective of the State's constitution. The aim is not only to phase out fixed interest payments but to replace interest with equity participation arrangements that will allow incentives for savings and efficient resource allocation to be retained consistent with Islamic principles. Since January 1981, "interest-free counters" have been established in almost 6,600 branches of the five nationalized banks, permitting depositors to choose between interest-bearing deposits and "interest-free" accounts. By opting for the latter, depositors are entitled to share in the profits and losses of the investments financed by the banks.

"Investment" deposits correspond to "fixed deposit" or "time deposit" accounts and to savings accounts in Western banks. The funds raised in "investment" accounts are invested by banks on the basis of the PLS principle, with the banks sharing the amount of profits resulting from their investments with depositors. The calculation of profits and losses and a dividend declaration can be undertaken annually or every six months. In Pakistan, the PLS principle is applied to the fixed deposit accounts of banks that issue fixed deposit receipts, which are only accepted in amounts denominated in multiples of one thousand rupees.

Current account deposits in Islamic banks are held for transaction and contingency motives, with the investment motive playing a strictly secondary role. Funds mobilized in current accounts can legally be used only to meet short-term financial needs, such as balancing the liquidity position of companies, and cannot be used for long-term finance.

Whereas in Western financial systems companies raise funds mainly through the issuance of equity shares, debentures, or by medium-term and long-term borrowing from banks at fixed interest, the latter two possibilities are not in accord with Islamic principles. Consequently, Islamic countries are taking various steps to change their existing financial systems and bring them into conformity with Islamic tenets. For example, the Government of Pakistan passed the *modaraba* law to base financial transactions on the PLS principle and introduced "Participation Term Certificates" (PTC) to replace interest-bearing debentures. Banks and other financial institutions are asked to grant long-term loans on a PLS basis as another possibility of providing long-term finance to industry and commerce.

Under the *modaraba* law, management companies, banks, and financial institutions can register themselves as *modaraba* companies. These can be of two types: a multipurpose *modaraba* with more than one specific objective and a *modaraba* having a specific purpose (e.g., for raising household finance). *Modaraba* companies may only engage in business that is permitted under the Islamic religious law, the *Shariah*. A "Religious Board" ensures that the firm's activities are not contrary to the injunctions of Islam. Funds collected on a *modaraba* basis can be used, on a PLS basis, for most types of investment except, of course, those that are proscribed on religious grounds.

Under a *modaraba* business, banks and other financial institutions are able to provide risk capital in the form of equity and loans with equity features. For the amount of capital provided, banks receive "*Modaraba* Certificates," which are transferable certificates with a specific face value issued to the subscriber of the *modaraba*. Before profits are distributed, the board of the *modaraba* company decides which part of them should be retained as reserves.

In addition to the *Modaraba* Certificates and the PTCs mentioned above, another way to enable banks and other financial institutions to provide medium-term and long-term finance is the leasing system (*baj muajjal*). Banks acquire certain fixed assets and lease them for a specified period to their customers for a hire fee. Banks and their leasing subsidiaries are sharing in the profits and risks of the entrepreneur's business as long as the rent for the leased assets is not fixed in advance, but related to financial success.

The provision of short-term loans by banks is an integral part of modern business, but one that raises problems in a situation in which fixed interest charges are not permitted. A number of proposals have been advanced to remedy this difficulty, such as that the banks should provide short-term loans free of charge or that the profits of an enterprise could be computed for the period covered by the loan in a manner consistent with PLS principles.

In the agricultural sector, the need for finance arises mainly from the seasonal nature of agricultural activity. As a means of reducing the reluctance sometimes found in rural areas to use the services of banks, the introduction of a banking system that works on the principles endorsed by religious leaders could be helpful. Applying the PLS principle to agricultural lending could be done by sharing output, or net profits, at an agreed percentage between the bank and the farmer.

Consumer credit has become a very important business activity for commercial banks in developed countries, and Islam does not absolutely forbid lending for consumption purposes. In a number of countries, special consumption loans—the *quarz-i-hasana*—existed, which were granted in hardship cases by neighbors or friends without any financial consideration. However, the application of the partnership principle to consumption loans does not seem an acceptable solution, since these generally do not yield profits that could be shared by lender and borrower. It has been proposed that such loans be granted through a government state agency or through cooperative societies, but this does not solve the problem of remuneration. An alternative way of providing consumer credit is the hire-purchase (*bai salam*) arrangement, under which the title of ownership gradually passes to the customers with the paying of installments. In Pakistan, the House Building Finance Corporation (HBFC) advances loans for housing on a hire-purchase basis. Under this arrangement, the purchaser pays installments to the HBFC until the entire principal is paid. The Corporation assesses both the total value of the house and its rental value and is entitled to a share of the rent, from which it derives its profits. By using the formula of an "interest-free" housing loan, the purchaser in effect has to pay the same rate of interest as he would in obtaining a straight loan.

Alternatives to a PLS System. Providing finance on a PLS basis requires thorough vigilance by the banks over the utilization of funds and involves numerous practical

problems that may require banks to increase the size of their staffs.

Being aware of these practical difficulties, the Government of Pakistan has considered possible alternatives that would be a substitute for the PLS system but would not rely on fixed interest rates. One proposal is to introduce a system of indexing bank deposits and advances, with the rate of indexation related to some multiple of the rate of inflation. Although this does not include the PLS principle, it could be considered to be in accordance with Islam because the indexation rate is tied to the variable and uncertain inflation rate. Another proposal aimed at long-run financing is the Investment Auctioning System under which financial institutions would auction investment authorization to investors. Supply of and demand for investable funds determine the scarcity price of available capital. Within the framework of such a system, entrepreneurs would remain solely responsible for their investment decisions, whereas banks would only act as financial intermediaries. Scarce capital resources would flow into those investments that yielded the highest expected rates of return.

Effects of an Islamic Financial System. The introduction of financial intermediation based on the PLS principle has potential impacts on the behavior of savers, banks, and investors. The PLS system turns savers into entrepreneurs, at least to some extent, by encouraging them to participate directly in the financial success of the investor's business, thereby also sharing the risks involved. In an Islamic banking system not only is the expected rate of inflation a risky variable but so also is the nominal yield on investment deposits.

An argument based on religious grounds is that an Islamic banking system could attract resources from devout savers, who are not willing to accept fixed interest payments on their deposits under the traditional banking system. If the PLS system were to be introduced as a complement to the traditional banking system, overall savings within the financial system may increase.

Where an Islamic banking system works side by side with traditionally operating banks, the effects on savings are unambiguously positive, since the variety of savings instruments is expanded and no existing savings outlet is eliminated. It could also be argued that yields to depositors could be higher under the PLS system than under the conventional system, and that the PLS system offers a better chance for compensating depositors for an unexpected acceleration in the rate of inflation.

The limited evidence demonstrates that Islamic banks have operated quite successfully in recent months. In Pakistan, the commercial banks have declared dividends for the first half of 1981 on PLS savings accounts of 9 per cent and on PLS term deposits of from 11.5 per cent (for periods of less than one year) to 15.25 per cent (for periods of more than five years). The Jordan Islamic Bank registered an overall profit of 8.2 per cent on investment accounts for 1980. Depositors with the Bahrain Islamic Bank received a dividend of 9–9.5 per cent on deposit accounts and 5.25 per cent on savings accounts for 1980.

Conclusion. The practical handling of banking operations under an Islamic financial system based on the PLS principle raises a number of unresolved issues. In particular, remunerating lenders for making short-term loans to industry and commerce and for providing consumer credit remains difficult if the PLS system is to be applied fully. Another problem that has not been dealt with explicitly is that of the foreign operations of Islamic banks. In Islamic jurisprudence, transactions between Islamic and non-Islamic countries have to be treated differently. Investments abroad by the Islamic Development Bank yielding fixed rates of interest are in conformity with Islamic principles; however, the interest earnings have been kept in a special account outside the general account of the Bank. Recently, consideration has been given to adapting transactions with non-Islamic banks to the PLS system.

If the PLS system is introduced on an optional basis, it appears likely that the enlargement of choice would have generally beneficial consequences, particularly for savings. A complete transformation to a PLS system, however, would require satisfactory handling of a number of issues that still have to be resolved, particularly those concerning the allocation and remuneration of short-term financing.

Ingo Karsten, 1981 summer intern,
IMF Middle Eastern Department

U.S. Budget for 1983 Seeks to Curb Inflation

(continued from front page) original objective of achieving a balanced budget in 1984 was no longer achievable. He stressed that "the factors that have postponed its realization are neither permanent nor cause for abandoning the goal of eventually living within our means. In the near term, the most important setback to our budgetary timetable is the recession now under way. . . . While the recession will end before this fiscal year is over, its budgetary impact will spill over for many years into the future."

Economic Report. On February 10 the President transmitted to the Congress the *Economic Report of the President*, together with the *Annual Report of the Council of Economic Advisers*, which outlines the conceptual framework for the Administration's economic policy. The President's Report expresses the hope that 1981 would later "be described as the watershed year in which the more than decade-old rising trend of inflation was finally arrested." The basic solution, it emphasizes, lies in combining strict control of the money supply with tax cuts to overcome economic stagnation, adding that "what some people have referred to as 'monetarism' and 'supply-side economics' should be seen as two sides of the same coin—compatible and necessary measures both to reduce inflation and increase economic growth." In discussing the problem of "stagflation," the Report states that "there is no long-term tradeoff between unemployment and inflation. The increasing role of the Federal Government in the economy . . . contributed to our declining economic performance." The Federal Government, it adds, "bears the most direct responsibility for the increases in inflation and interest rates."

Position of the Federal Reserve. The issue of inflation was also addressed on February 10 by Paul A. Volcker, Chairman of the Board of Governors of the U.S. Federal Reserve System. Testifying before the Committee on Banking, Finance, and Urban Affairs of the House of Representatives, he emphasized that "consolidating and extending the heartening progress on inflation will require continuing restraint on monetary growth, and we intend to maintain the necessary degree of restraint."

Economic Report States Commitment to Open Trade

A strong U.S. economy requires the maintenance of open markets both within the United States and overseas, the *Economic Report of the President* states in a chapter devoted to the international economic system. "Open trade based on mutually agreed upon rules is consistent with, indeed integral to, the Administration's commitment to strengthening the domestic economy," it notes. "The maintenance of open markets has become increasingly important in recent years as the shares of foreign trade and investment have grown relative to the size of the U.S. economy."

Trade Policy. In a section on trade policy, the Report restates the Administration's commitment to pursue policies aimed at achieving open trade and reducing price distortions. The five central components of this policy are (1) restoring strong noninflationary growth within the United States; (2) reducing self-imposed trade disincentives such as needlessly complex laws and regulations; (3) effective and strict enforcement of U.S. trade laws and international agreements; (4) a more effective approach to industrial adjustment problems that would place primary reliance on market forces rather than on government "bail-outs"; and (5) reducing government barriers to the flow of trade and investment among nations.

The Report notes that "concern with the country's international payments position is appropriate when the basis of that concern is that the country is simultaneously experiencing a sustained deficit in its current account and a persistent depreciation of its currency in the exchange markets." It stresses: "It is particularly important not to become unduly preoccupied with the trade or current account balances with a single foreign country. Any policy to reduce a bilateral imbalance by restricting imports is likely to reduce the absolute volume of trade and, in consequence, the level of economic well-being of both countries, and could have wider repercussions. A far more constructive approach would be for the nations with restrictive trade practices and institutional barriers to imports to reduce systematically those obstacles to the freer flow of trade and investment."

International Organizations. The Report identifies three issues affecting the open international system: (1) the conflict between domestic short-term interests and long-term external interests; (2) the need to maintain an open international economic system; and (3) the call to respond to the aspirations of the developing countries for greater growth and development. In connection with the last issue it states that, in its view, recent studies of the problem have placed "too much emphasis on resource transfer and not enough emphasis on resource development through private market institutions."

In commenting on the role of the Fund, the Report emphasizes that "the administration strongly supports further development under the IMF surveillance procedures of what has become known as the Article IV consultation process." It notes that "effective balance of payments adjustment frequently requires wider acceptance of market-oriented solutions" and also cautions that "even a modest new allocation of special drawing rights in present circumstances would appear to conflict with the policies of monetary restraint being pursued in many countries."

Noting that there had been a sharp increase in the money supply in January 1982, which was "unusual in a period of declining production and economic activity," he announced new targets for the money supply which were, he said, "consistent with an economic recovery later this year" (see page 62).

Budget Objectives. The budget document states that the effects of reforms introduced as a result of the fiscal year 1982 budget (*IMF Survey*, February 23, 1981, page 49) and of actions proposed in the fiscal year 1983 budget "result in two fundamental changes: a new environment to foster economic prosperity, and a rational and lean realignment of domestic programs, combined with an adequate defense force." In particular:

- Tax, spending, and management initiatives proposed in the budget are designed to reduce the deficits by $239 billion over the next three years from the level they would have reached without such measures.
- The overall growth rate of government spending, which peaked at 17 per cent in 1980, is projected to decline to 10 per cent in 1982 and 4 per cent in 1983.
- The federal deficit, measured as a share of gross national product (GNP), is projected to decline from a level of 3.4 per cent in both 1980 and 1981 to 2.6 per cent of GNP in 1984 and to 1.3 per cent by 1987.
- Defense spending will rise by $44.1 billion to $263.0 billion in 1983 and will continue to rise rapidly in the next few years, with the share of defense in the federal budget climbing rapidly.

The President's plan to reduce the federal deficit concentrates largely on five areas: (1) nonsocial security entitlements, such as medical programs, school loans, and retirement programs; (2) domestic programs for purposes ranging from agricultural research to housing subsidies and manpower training; (3) user fees that predominantly benefit a limited group of businesses or individuals that make use of public services; (4) wastage and inefficiency in the executive branch of government; and (5) the elimination of tax loopholes and obsolete tax incentives.

The U.S. GNP, adjusted for inflation, is expected to rise by 3.0 per cent from the fourth quarter of 1981 through the fourth quarter of 1982 and by 5.2 per cent during calendar year 1982.

Economic Outlook. A critical element in the outlook for the economic proposals, the Economic Report cautions, "is the assumption that inflationary expectations will, in fact, continue to recede. If they recede at a relatively fast rate, market rates of interest will decline significantly, wage demands will continue to moderate, and the pro-inflationary biases that have developed throughout the economy over the past decade will quickly disappear."

In a section devoted to prospects for 1982 and beyond, the Economic Report states that "the current recession is expected to end early in 1982, followed by a resumption of growth in mid-year," with the key areas of strength expected to be in consumer goods (including automobiles), housing, and defense. It projects that "1982 and 1983 should become the first of several years of prosperous growth and declining inflation occurring simultaneously."

The Report also advises that there should not be excessive concern if the U.S. current account should move into deficit. "With strong domestic performance, U.S. import demand will also strengthen; the effects of this revitalization on U.S. exports will take more time. Thus, a deficit on current account will simply reflect the adjustment process at work."

In a discussion of monetary policy, the Report notes that as many as eight quarters typically have to pass before monetary restraint produces a reduction in the inflation rate. "However," it adds, "the whole process of renewed economic growth without inflation can be speeded up if the policy of monetary restraint is believed by the public, since it is an unanticipated decrease in the rate of monetary growth that significantly affects output and employment in the short run."

Role of the Dollar. The Report comments that, since the U.S. dollar remains the principal currency for international commercial and financial transactions, both the United States and the rest of the world would benefit from a stronger and more stable U.S. dollar. "The strength and stability of the dollar depend directly on the ability of the United States to pursue noninflationary economic policies," it states. "In the late 1960s and the 1970s the United States failed to meet this objective."

The study observes that, when the previous Administration left office at the beginning of 1981, intervention by the United States in the exchange markets was being conducted at a relatively high level. "Early in 1981, the new Administration scaled back U.S. intervention in foreign exchange markets," it continues. "In conjunction with a strong emphasis on economic fundamentals, this Administration has returned to the policy of intervening only when necessary to counter conditions of severe disorder in the market."

United States: Short-Range Economic Forecast
(calendar years; billion U.S. dollars)

	Actual 1980	1981[1]	Forecast 1982	1983
Gross national product				
Current dollars				
Amount	2,626	2,922	3,160	3,524
Per cent change: fourth quarter over fourth quarter	9.4	9.3	10.4	11.0
Constant (1972) dollars				
Amount	1,481	1,510	1,513	1,591
Per cent change: fourth quarter over fourth quarter	−0.3	0.7	3.0	5.2[1]
Incomes (current dollars)				
Personal income	2,160	2,404	2,641	2,887
Wages and salaries	1,344	1,483	1,605	1,747
Corporate profits	246	230	215	260
Price level (per cent change: fourth quarter over fourth quarter)				
GNP deflator	9.8	8.6	7.2	5.5
Consumer price index[2]	12.6	9.4	6.6	5.1

[1] Preliminary actual data.
[2] For urban wage earners and clerical workers.
Data: Office of Management and Budget

United States: Long-Range Economic Assumptions
(calendar years; billion U.S. dollars)

	Assumptions 1984	1985	1986	1987
Gross national product				
Current dollars				
Amount	3,883	4,258	4,651	5,068
Per cent change: fourth quarter over fourth quarter	10.0	9.4	9.1	8.9
Constant (1972) dollars				
Amount	1,670	1,750	1,827	1,905
Per cent change: fourth quarter over fourth quarter	4.9	4.6	4.3	4.3
Incomes (current dollars)				
Personal income	3,121	3,411	3,723	4,057
Wages and salaries	1,887	2,065	2,256	2,458
Corporate profits	314	330	317	334
Price level (per cent change: fourth quarter over fourth quarter)				
GNP deflator	4.9	4.6	4.0	4.4
Consumer price index[1]	4.7	4.6	4.6	4.4

[1] For urban wage earners and clerical workers.
Data: Office of Management and Budget

FUND ACTIVITIES

Importance of Budgeting And Expenditure Control Is Stressed by Seminar

The planning of public expenditures, the formulation and execution of government budgets, and the administration of expenditure controls were among topics discussed at a seminar on budgeting and expenditure control, the second in a series, organized by the Fund at its headquarters on January 20–28. The first seminar was held in June 1980 (*IMF Survey*, July 7, 1980, page 203). The purposes of the seminar were to promote a greater awareness of the role of budgeting and expenditure controls in the current context and to bring together senior policymaking officials from industrial and developing countries to exchange views on policies and practices. The seminar was attended by representatives from 22 countries—Australia, Austria, Bangladesh, Barbados, Brazil, Canada, Egypt, The Gambia, Italy, Japan, Libya, Malaysia, Nepal, Pakistan, the Philippines, Somalia, Sudan, Sweden, Tanzania, Thailand, the United States, and Zimbabwe.

The seminar dealt with a wide range of subjects including fiscal policies for budgeting, determinants of public expenditure, institutional and operational issues in expenditure controls, financial planning and expenditure forecasting, inflation budgeting, development planning and budgeting, the current status and future direction of budgetary innovations, short-term adjustments in public expenditures, budget execution and cash management, and government accounting and financial information systems.

Discussions at the seminar focused on the interaction between fiscal policies, institutions, and budgetary techniques and procedures and centered around three major elements: (1) improving budgetary processes through the use of different policy instruments such as taxes, expenditure, and credit; (2) strengthening expenditure controls to ensure a better appraisal and a more efficient use of resources, as well as the right choice of policy instruments; (Please turn to page 61)

TRANSACTIONS FOR SEPTEMBER, OCTOBER, NOVEMBER, AND DECEMBER 1981

General Resources Account

(million SDR equivalents)

	SEP	OCT	NOV	DEC
Purchases	**631.5**	**126.7**	**1,246.0**	**472.7**
Burma		9.0		5.0
Dominica		0.7		0.7
Ethiopia	11.7			11.7
Grenada			0.6	
Guatemala			95.6	
Guinea			0.6	
Guinea-Bissau	1.8	0.5		
Haiti				17.0
India			300.0	
Ivory Coast	158.2			44.2
Jamaica		33.4		4.7
Korea			144.0	
Liberia	11.0		0.9	11.0
Malawi	12.0			
Malaysia	189.8			
Mauritius				7.5
Pakistan				170.0
Papua New Guinea			45.0	
Philippines	50.0			50.0
Romania	36.3			
Senegal	49.9			7.9
Sierra Leone				0.2
Somalia			10.8	
Sri Lanka		18.8	37.5	37.8
Thailand			90.0	105.0
Turkey	100.0		100.0	
Uganda			40.0	
Viet Nam		5.0		
Yemen, People's Dem. Rep. of	10.8			
Yugoslavia			126.0	
Zaïre			75.0	
Zambia		59.3	180.0	
Repurchases	**94.9**	**180.4**	**139.1**	**153.2**
Bangladesh	0.8	4.0	0.9	
Barbados				0.7
Bolivia		1.9		
Burma		2.0	3.8	4.0
Cameroon	0.5	0.3	0.3	0.5
Central African Rep.	0.3	0.1		0.3
Chad	0.1	0.1		0.1
Chile	2.6	7.6	5.0	
Costa Rica			1.1	2.4
Cyprus	0.4	1.0	0.5	0.4
Dominican Rep.	5.4			
Egypt	9.3		7.7	9.3
Equatorial Guinea				0.2
Finland	2.6		7.2	4.4
Ghana	2.4			2.4
Greece	2.3	3.5	3.9	
Grenada		0.0		
Guinea		1.1	0.6	
Guyana		1.1	0.2	
Haiti	0.1	0.3	0.2	
Iceland	1.8	0.5	0.1	1.8
Israel		5.1	3.9	9.1
Jamaica	2.8	9.2		6.2
Kenya		1.5	0.2	
Korea	7.0	4.3	4.5	5.7
Madagascar		0.5	1.4	
Malawi	0.1	0.1		0.1
Mali	1.1	0.3	0.3	
Mauritania		0.2	0.1	
Morocco			8.1	0.8
Nepal		0.2		
Nicaragua		0.5		
New Zealand	2.9	1.5	23.5	2.9
Pakistan	8.4	6.4	27.0	6.5
Panama	0.5	0.4	0.6	3.6
Peru	3.3			11.0
Philippines	6.0		3.4	13.8
Portugal		7.2		
Romania	6.2			
Senegal	0.6	1.0		0.9
Sierra Leone	0.2	0.1	0.3	1.4
Spain			12.3	14.4
Sri Lanka	2.6	11.6	1.4	9.6
Sudan	0.6			2.5
Tanzania	3.1		0.2	2.7
Thailand		8.6		8.6
Turkey	7.1	9.3	9.3	7.1
Uganda				0.3
United Kingdom		62.5		
Viet Nam		9.0		
Western Samoa		0.0	0.3	0.0
Yemen, People's Dem. Rep. of	0.1	0.3	1.0	0.2
Yugoslavia	8.7		4.5	6.2
Zaïre		11.0	4.8	8.3
Zambia	5.0	6.1	0.7	5.0

Currency Units per SDR

Currency	February 2	3	4	5	8	9	10	11	12	15	16
Deutsche mark	2.68144	2.66965	2.67335	2.66645	2.66974	2.68577	2.68143	2.67844	2.69034	2.69841	2.69741
French franc	6.81995	6.79372	6.79599	6.78241	6.79235	6.81167	6.80698	6.79645	6.82743	6.83877	6.84249
Japanese yen	265.079	265.485	266.744	265.198	266.349	265.976	267.407	...	268.244	269.234	270.933
Pound sterling	0.611956	0.608891	0.609397	0.610454	0.611337	0.613459	0.612145	0.612328	0.613749	0.615231	0.614238
U.S. dollar	1.13524	1.13893	1.13750	1.13990	1.13727	1.13085	1.13308	1.13397	1.12850	1.12415	1.12467
Argentine peso	11409.2	...	11403.4	11427.5	11401.1	11336.8	11359.1	11368.0	11313.2	11269.6	11274.8
Australian dollar	1.03751	1.04240	1.04138	1.04224	1.04174	1.03853	1.04220	1.04254	1.03904	1.03915	1.04213
Austrian schilling	18.8166	18.7240	18.7574	18.6784	18.7286	18.8332	18.8273	18.7887	18.8471	18.9318	18.9158
Bahrain dinar	0.427985	0.429377	0.428838	0.429742	0.428751	0.426330	0.427171	0.427507	0.425445	0.423805	0.424001
Belgian franc	45.6452	45.5202	45.4972	45.4934	45.5363	45.6637	45.7084	45.6395	45.8510	45.9412	45.9400
Brazilian cruzeiro	151.861	152.355	152.163	155.106	154.748	153.875	154.178	154.299	153.555	155.537	155.609
Canadian dollar	1.36933	1.37492	1.37057	1.37449	1.37473	1.37579	1.37590	1.37176	1.36831	1.36820	1.37052
Colombian peso	67.9782	68.2447	68.2159	68.4168	68.3158	67.9754	68.1661	...	67.9470	...	67.8176
Danish krone	8.78676	8.74357	8.75591	8.71568	8.74561	8.80649	8.79440	8.76559	8.78989	8.83301	8.82585
Ecuadoran sucre	28.3810	28.4733	28.4375	28.4975	28.4318	28.2713	28.3270	28.3493	28.2125	28.1038	28.1168
Finnish markka	5.11312	5.09785	5.09941	5.08509	5.09383	5.10466	5.11246	5.10287	5.10195	5.12050	5.11050
Guatemalan quetzal	1.13524	1.13893	1.13750	1.13990	1.13727	1.13085	1.13308	1.13397	1.12850	1.12415	1.12467
Indian rupee	10.4339	10.3816	10.3902	10.4998	10.4539	10.4901	10.4065	10.4096	10.4337	10.4589	10.4420
Indonesian rupiah	734.500	736.888	735.963	737.515	735.814	732.225	733.953	734.529	731.268	729.011	730.192
Iranian rial	92.3000	92.3000	92.3000	92.3000	92.3000	92.3000	92.3000	92.3000	92.3000	92.3000	92.3000
Iraqi dinar	0.335252	0.336342	0.335920	0.336628	0.335852	0.333956	0.334614	0.334877	0.333262	0.331977	0.332131
Irish pound	0.759358	0.755509	0.757828	0.757157	0.759699	0.761003	0.761991	0.761054	0.765864	0.766135	0.766908
Italian lira	1434.66	1428.79	1429.27	1426.36	1428.13	1434.20	1432.78	1430.79	1435.45	1438.07	1437.89
Kuwaiti dinar	0.323180	0.323934	0.323835	0.324518	0.323519	0.322077	0.322826	0.322966	0.321408	0.321012	0.321127
Libyan dinar	0.336091	0.337184	0.336760	0.337471	0.336692	0.334792	0.335452	0.335715	0.334096	0.332808	0.332962
Malaysian ringgit	2.60867	2.61453	2.61716	2.61846	2.62653	2.62120	2.62229	2.62718	2.61947	2.62253	2.62532
Malta pound	0.453751	0.452567	0.453061	0.451607	0.452429	0.452666	0.453958	0.453099	0.452904	0.454386	0.453734
Mexican peso	30.2607	30.3818	30.3664	...	...	30.2338	30.3165	30.3630	30.2391	30.1446	30.1814
Netherlands guilder	2.93687	2.92648	2.93020	2.92498	2.93302	2.94417	2.94318	2.93698	2.95159	2.95651	2.95620
Nigerian naira	0.736308	0.738702	0.737774	0.739331	0.737625	0.733461	0.734907	0.735484	0.731937	0.729115	0.729453
Norwegian krone	6.79157	6.74247	6.74993	6.73225	6.74742	6.74891	6.76109	6.74826	6.74956	6.76176	6.75702
Omani rial	0.392112	0.393386	0.392893	0.393721	0.392813	0.390596	0.391366	0.391673	0.389784	0.388281	0.388461
Portuguese escudo	77.2803	77.1135	77.1578	77.1393	77.2366	77.4044	77.4166	77.3470	77.5674	77.6945	77.6933
Qatar riyal	4.13227	4.14571	4.14050	4.14924	4.13966	4.11629	4.12441	4.12765	4.10774	4.09191	4.09380
Saudi Arabian riyal	3.87684	3.88945	3.88456	3.89276	3.88378	3.86185	3.86947	3.87251	3.85383	3.83897	3.84075
Singapore dollar	2.38230	2.38492	2.38898	2.38877	2.40021	2.39231	2.39510	2.39755	2.38903	2.39219	2.39375
South African rand	1.11593	1.11474	1.11367	1.11351	1.11301	1.11370	1.11601	1.11556	1.11073	1.10983	1.11122
Spanish peseta	113.274	112.779	113.215	113.083	113.075	113.246	113.445	113.193	113.502	114.046	114.008
Swedish krona	6.53331	6.50215	6.50536	6.48717	6.50518	6.52105	6.53674	6.51919	6.52273	6.54368	6.53939
Swiss franc	2.14424	2.14062	2.14498	2.13868	2.14808	2.15970	2.15059	2.14797	2.15995	2.16174	2.15802
Trinidad & Tobago dollar	2.73479	2.74368	2.74024	2.74602	2.73968	2.72422	2.72959	2.73173	2.71856	2.70808	2.70933
U.A.E. dirham	4.16747	4.18101	4.17576	4.18457	4.17492	4.15135	4.15954	4.16280	4.14272	4.12675	4.12866
Venezuelan bolivar	4.87302	4.88886	4.88272	4.89302	4.88173	4.85417	4.86375	4.86757	4.84409	4.82541	4.82765

Note: The value of the SDR in terms of the U.S. dollar is determined as the sum of the dollar values, based on market exchange rates, of specified quantities of the first 5 currencies shown above. The value of the SDR in terms of any currency other than the U.S. dollar is derived from that currency's exchange rate against the U.S. dollar and the U.S. dollar value of the SDR. An exception is the Iranian rial, the value of which is officially expressed directly in terms of rials per SDR.

Data: IMF Treasurer's Department

Special Drawing Rights Department

(million SDRs)

	SEP	OCT	NOV	DEC
Transfers	**694.9**	**258.0**	**651.1**	**525.3**
Austria				10.0
Canada		7.4		101.6
Chile		7.7		
Germany, Fed. Rep. of		33.9	117.3	68.2
Guatemala		27.0	51.9	
India			59.4	
Israel		5.1		
Ivory Coast	45.0			14.1
Jamaica		7.0		
Korea	7.0		8.4	
Malawi	7.0			
Malaysia	89.8			
Pakistan	8.4	6.4		
Peru				11.0
Philippines			8.3	
Saudi Arabia	265.0			
Senegal	29.2			
Spain			12.3	14.4
Sri Lanka				27.0
Thailand		8.6		
United Kingdom		62.5		
Yemen Arab Rep.	10.8			
Yugoslavia	8.7		10.6	
Zambia		17.3		15.0
Swiss National Bank	4.0			
Other Participants[1]	23.7	16.7	122.1	82.0
IMF General Resources Account	196.4	58.5	260.8	182.0
Receipts	**694.9**	**258.0**	**651.1**	**525.3**
China, People's Rep. of				140.0
Ethiopia	5.3			
Guatemala			54.1	
Ivory Coast	45.0			22.1
India			50.8	
Israel		10.0	10.0	
Jamaica		11.0		
Korea			50.0	
Malawi	8.0			
Malaysia	89.8			
Mexico	10.0			11.5
Nigeria		9.8		
Papua New Guinea			33.0	
Pakistan				39.3
Peru				19.0
Romania		5.6		
Senegal	29.4			
Spain			50.0	
Sri Lanka			9.1	37.8
Thailand				47.7
Turkey		6.5		
United Kingdom	59.8	17.3	43.0	10.5
United States	102.6	27.0	49.1	38.6
Yemen Arab Rep.	10.8			
Yugoslavia			58.2	
Zaïre			9.3	
Zambia		24.3	23.6	
Other Participants[2]	25.5	43.2	53.8	82.6
IMF General Resources Account	308.8	103.3	157.1	76.2

[1] Number of other participants (transfers): 27 in September, 20 in October, 67 in November, 34 and 1 Other Holder in December.

[2] Number of other participants (receipts): 15 in September, 32 in October, 26 and 1 Other Holder in November, 31 and 1 Other Holder in December.

Note: Components may not add to totals because of rounding.

Data: IMF Treasurer's Department

(continued from page 59) and (3) strengthening public expenditure planning for dealing with uncertainties. In each of the sessions, the progress made so far was reviewed, and the current and future tasks of fiscal managers were identified. The participants felt that a threefold approach was needed to improve financial management in government: (1) medium-term financial planning by central agencies to assess current policies and to formulate future policies; (2) the building up or strengthening of financial management capabilities in spending agencies; and (3) greater attention to vulnerable areas such as personnel management in government, indexation of benefits and programs, implementation of public works programs, implications of transferring certain business activities from public agencies to the private sector, and financial relationships with state-owned enterprises and regional and local governments.

A. Premchand, Advisor,
IMF Fiscal Affairs Department

PRESS RELEASE

Bangladesh: Compensatory Financing

The Fund has agreed to a purchase equivalent to SDR 60 million by the Government of Bangladesh under the compensatory financing facility. The drawing compensates for a shortfall in export earnings experienced by Bangladesh in the 12-month period ending March 1982 under a provision that permits export data for up to six months of the shortfall year to be estimated.

The shortfall during this period derives largely from lower prices of raw jute and jute products—which account for almost 70 per cent of Bangladesh's total exports—reflecting depressed demand in the industrial countries.

Bangladesh's quota in the Fund is SDR 228 million, and its outstanding financial obligations to the Fund resulting from past operations and transactions, excluding Trust Fund loans, currently total the equivalent of SDR 281.07 million.

Press Release No. 82/6, February 10

SDR Department Transfers Maintain a High Volume

(continued from front page) acquiring SDRs in these transfers did so to replenish their holdings so as to meet obligations to the Fund that were payable in SDRs.

Participants and other holders engaged in a number of prescribed operations for the first time in 1981; these included the use of SDRs in loans and to settle financial obligations and totaled SDR 31.3 million.

The Fund's holdings of SDRs declined by SDR 553.0 million during 1981 to SDR 5,018.9 million at the end of the year. Inflows totaled SDR 2,082.9 million and included SDR 830.1 million in repurchases and SDR 718.0 million for the payment of charges. Outflows amounted to SDR 2,635.9 million, made up largely of sales of SDRs to members purchasing from the General Resources Account (SDR 1,962.2 million—up more than 25 per cent from the previous record of SDR 1,555.9 million in 1980), remuneration (SDR 348.2 million), and the use of SDR 302.4 million by the Fund in repayment of, or interest on, Fund borrowing.

Operations Division for SDRs
and Administered Accounts,
IMF Treasurer's Department

BRIEF NOTES

International Finance

An officially recognized Japanese gold exchange will begin operations on March 23 as a result of the Government's decision last September to revise Japan's Commodity Exchange Law ordinance to permit establishment of the Tokyo Gold Exchange. Initially, gold transactions by the new exchange, which is the eighth officially recognized commodity exchange in Japan, are projected to average 880 kilograms a day. Under the rules governing the operations of the exchange, the official standard purity of gold for transactions will be 99.99 per cent, trading in futures will be subject to a maximum time limit of six months, and there will be six daily trading sessions. The constitution of the Tokyo Gold Exchange, which was patterned after the constitution of the New York Commodity Exchange, contains provisions to exclude gold traders who have been blacklisted elsewhere and to caution potential investors regarding the inherent risks of gold trading. With the establishment of the Tokyo Gold Exchange, the Government expects that unofficial gold exchanges, which have proliferated in Japan since 1980, will cease to operate.

Japan Economic Journal, Tokyo, February 9

Economic Trends

Industrial production in the EC as a whole contracted by about 2.5 per cent in 1981, according to provisional data by the Commission of the European Communities. The data show that, of the ten Community members, only Denmark registered an increase in industrial production during the year, although the increase, estimated at 0.2 per cent, was only marginal. The largest contraction occurred in Luxembourg, whose index of industrial production fell by 7.9 per cent, followed by the United Kingdom, whose industrial output declined by 4.7 per cent.

Financial Times, London, February 10

Fiscal and Monetary

U.S. monetary growth targets for 1982 were announced on February 10 by Paul A. Volcker, Chairman of the Board of Governors of the Federal Reserve System. The targets adopted by the Federal Open Market Committee are:

- For M-1, which includes all currency in circulation plus demand deposits, other checkable deposits, and travelers checks, and which replaces M-1B (adjusted for shifts to other checkable deposit accounts since the end of the preceding year), a growth rate of 2.5–5.5 per cent.
- For M-2, which comprises M-1 plus savings deposits under $100,000, certain overnight bank borrowings, repurchase agreements between banks and individuals, and noninstitutional money market mutual funds, a growth rate of 6–9 per cent.
- For M-3, which is composed of M-2 plus large negotiable certificates of deposit issued by banks, other bank borrowings, and institutional money market mutual funds, a growth rate of 6.5–9.5 per cent.

Money Supply Growth
(per cent)

	1981 Target (fourth quarter to fourth quarter)	1981 Actual (fourth quarter to fourth quarter)	1982 Preliminary Target
M-1	3.5–6	2.3	2.5–5.5
M-2	6–9	9.4	6–9
M-3	6.5–9.5	11.3	6.5–9.5
Bank credit	6–9	8.8	6–9

- The target for growth of bank credit is 6–9 per cent for 1982.

A comparison of the monetary targets for 1982 with the targeted and actual monetary growth rates during 1981 is shown in the table. In addition to announcing the monetary growth targets for 1982, the Federal Reserve Board on February 10 also issued its *Monetary Policy Report to Congress*, in which the Board reviews the performance of the monetary aggregates during 1981. The Report notes that, while growth in shift-adjusted M-1B was below what might have been expected, the broader aggregates expanded rapidly during the year, largely owing to changing financial practices. Looking toward the future, the Report stresses that "a policy of restraint on the growth of the monetary aggregates is a key element in an anti-inflationary strategy. Targets for the monetary aggregates have been set with the aim of slowing the expansion of money over time to rates consistent with the needs of an economy growing in line with its productive potential at reasonably stable prices." It notes that, in January 1982, the rate of increase in M-1 was well above the average level during the fourth quarter of 1981, but states that this increase was probably the result of temporary factors, rather than signaling a basic change in the amount of money needed to finance nominal growth of the gross national product.

Statement by Paul A. Volcker, Chairman, Board of Governors of the Federal Reserve System, before the Committee on Banking, Finance, and Urban Affairs of the House of Representatives, and *Monetary Policy Report to Congress* of the Board of Governors of the Federal Reserve System, Washington, February 10

French investment in product development will be stimulated as a result of a three-part policy to be introduced by the French Government for promoting increased research and development activities by domestic companies. The measures, which will provide firms with easier financial terms for investment in research and development, form part of the Government's plan that such investment amount to about 2.5 per cent of France's gross national product by 1985. Under the Government's new policy, companies requiring medium-term loans for investment in projects to develop new products will be able to apply for special credits, which will carry competitive market rates and which will not be subject to existing credit restrictions on bank loans. The Government will also provide additional funds and guarantees to the system of participating loans, under which banks extend loans to companies in exchange for equity participation. Under the new measures, the maximum loss that banks will be exposed to under this system will amount to 15 per cent of the loan. Finally, the Government will set up a new fund with a capital of 1 billion francs to provide long-term financing for research and development projects.

Financial Times, London, February 8

Balance of Payments

Japan's balance of payments deficit fell to $2.14 billion in 1981, compared with a deficit of $8.4 billion in 1980, reflecting an improvement in the current account that helped partially to offset deteriorations in the long-term and short-term capital accounts, according to official data. The current account swung to a surplus of $4.73 billion in 1981, from a deficit of $10.75 billion in 1980, primarily because of a substantial improvement in the trade surplus that more than offset a higher deficit on the invisibles account. The data show that the deficit on invisibles grew to $13.67 billion in 1981, compared with a deficit of $11.34 billion in 1980. The merchandise trade surplus, however, grew sharply in 1981, reflecting a substantial increase in the value of exports that more than offset a much smaller advance in the value of imports. The trade surplus grew to $20.03 billion in 1981, from a surplus of $2.13 billion in 1980, reflecting an 18 per cent advance in the value of exports, to $149.38 billion, and a 3.8 per cent increase in the value of imports, to $129.35 billion. Regarding the capital accounts, the Government estimates that both long-term and short-term capital outflows exceeded inflows in 1981, resulting in deficits of $6.46 billion in long-term capital and $822 million in short-term capital, compared with surpluses of $2.39 billion and $3.07 billion, respectively, in 1980.

Asian Wall Street Journal, Singapore, February 1

Australia's balance of payments position deteriorated in the seven months ended January, primarily as a result of a substantial increase in the current account deficit that more than offset an improvement in the capital account, according to official data. Australia's overall balance of payments registered a deficit of 1.7 billion Australian dollars in the period July 1981–January 1982, compared with a surplus of $A 294 million a year earlier. The data show that the current account deficit almost doubled in the seven months ended January 1982 to just over $A 5 billion, from $A 2.6 billion in the seven months ended January 1981. The deterioration in the current account reflected a 3 per cent decline in the value of exports, primarily owing to lower commodity prices, and a 16 per cent increase in the value of imports, especially those of machinery and transport equipment. Preliminary data on capital transactions indicate that net apparent inflows, excluding government borrowings, amounted to $A 3 billion in the period under review, compared with about $A 2.5 billion in the seven months ended January 1981.

Financial Times, London, February 12

Energy

Energy production in the United Kingdom grew by 4 per cent in 1981 to the equivalent of 350 million tons of coal, while consumption fell by 3.7 per cent to the equivalent of 315.9 million tons, according to preliminary data by the Energy Department. This was the second year in which the United Kingdom achieved self-sufficiency in energy, and the first calendar year in which production of oil exceeded demand. According to the data, oil production, primarily in the North Sea, rose by 11 per cent in 1981 to 89.4 million tons, while consumption fell by 7.7 per cent to 74.5 million tons. By comparison, production of coal fell by 1.7 per cent in 1981 to 127.6 million tons, but this level was still above the consumption total of approximately 117 million tons. With both production and consumption of nuclear power and hydroelectricity growing by 4 per cent to the equivalent of 16 million tons of coal, natural gas was the only energy source to register a production shortfall relative to domestic demand in 1981. The Energy Department data show that natural gas production in the United Kingdom increased by 0.2 per cent in 1981 to 54.5 million tons of coal equivalent, while consumption rose by 1.6 per cent to 71.5 million tons.

Financial Times, London, February 4

Trade

The U.S. trade deficit, measured on a balance of payments basis, rose to $27.8 billion in 1981, compared with a deficit of $25.3 billion in 1980, according to preliminary estimates by the Department of Commerce. The data, which are seasonally adjusted, exclude military trade of U.S. defense agencies and reflect adjustments for timing, coverage, and valuation to the data released by the Census Bureau. The higher trade deficit reflected a 6 per cent increase in the value of imports, to $264.0 billion, that more than offset a 5 per cent advance in the value of exports, to $236.1 billion. In the period 1975–80, the value of imports had grown at an average annual rate of 20 per cent, while exports had advanced at an average annual rate of 16 per cent. According to the Department, the lower rates of growth of both imports and exports in 1981 reflected worldwide recessionary conditions. The data for 1981 show that the increase in the value of imports reflected higher imports of nonpetroleum products—especially machinery, iron and steel, and manufactured consumer durables—which grew by 9 per cent to $186.4 billion. This increase more than offset a decline in the value of petroleum imports, which fell by 2 per cent in 1981 to $77.6 billion. The data for exports show that the 1981 increase reflected a 6 per cent advance in the value of nonagricultural exports—primarily machinery, automotive products, and hard coal—and a 5 per cent increase in the value of agricultural exports—especially wheat and soybeans. Commerce Department data on the volume of merchandise trade in 1981 show that imports grew by 4 per cent, reflecting a 6 per cent advance in the volume of nonpetroleum imports that was partially offset by a decline in the volume of petroleum imports. It is estimated that imports of petroleum fell to 6.25 million barrels a day in 1981 from a daily average of 7.08 million in 1980. The volume of total exports fell by 3 per cent in 1981, reflecting a 4 per cent decline in nonagricultural exports and unchanged agricultural exports.

Press Release, U.S. Department of Commerce, Washington, February 5

FINANCIAL CALENDAR

February

4 Central bank governors of the five member countries of the Association of South East Asian Nations, meeting in Bangkok, agree to extend for a further five years the ASEAN swap arrangement.

5 Italy lifts the 15 per cent deposit requirement on imports and foreign exchange payments.

5 Bolivia announces new economic measures, including a devaluation of the peso, a price freeze on certain items, tariff reductions on selected imports, tax revisions, and restrictions on government outlays.

11 South Africa imposes a surcharge of 10 per cent on certain imports and announces that the sales tax will be increased. The measures are designed to help arrest the deterioration in its external accounts resulting from falling gold prices and to increase government revenues.

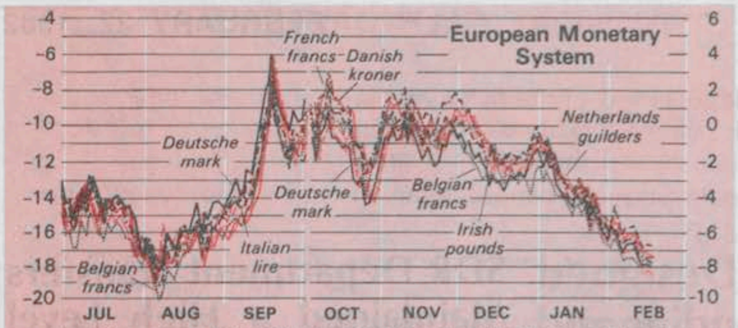
Forthcoming Events

23–25 Board of Governors of the International Energy Agency meets in Vienna.

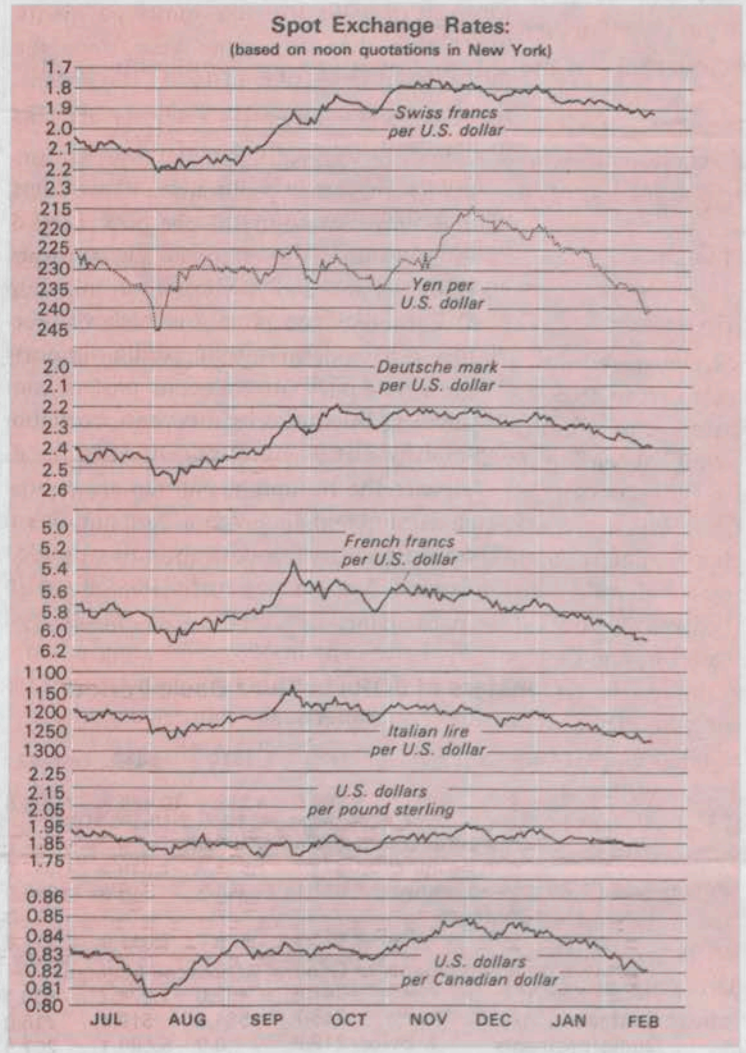
Exchange Rate Adjustments
(currency units per U.S. dollar; buying/selling)

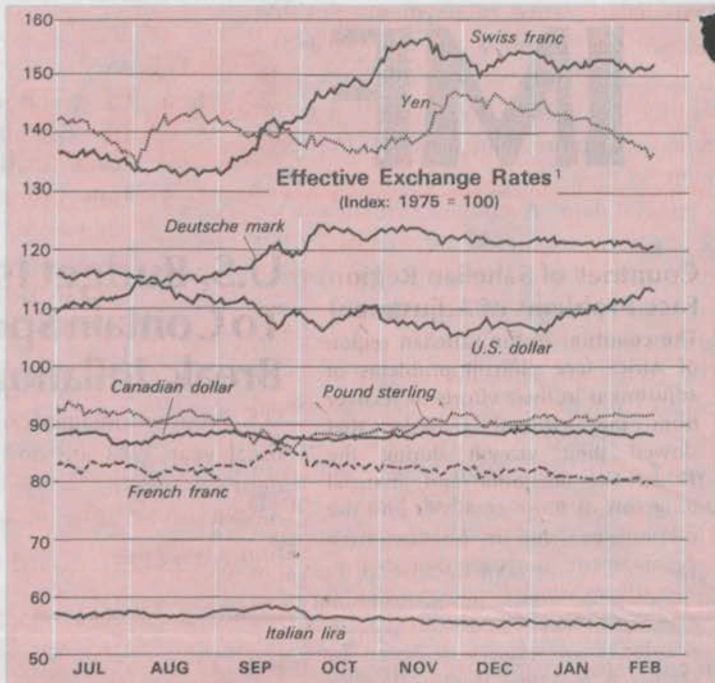
February	Old Rate	New Rate
5 Brazilian cruzeiro	133.77/134.44	136.07/136.75
5 Indian rupee[1]	17.05	17.20
8 Bolivian peso	24.51	44.00
8 Indian rupee[1]	17.20	17.10
10 Indian rupee[1]	17.10	17.00
16 Brazilian cruzeiro	136.07/136.75	138.36/139.05
17 Uruguayan new peso[2,3]	11.722/11.752	11.798/11.828

[1] Per pound sterling.
[2] The "Old Rate" represents the last figure published by the *IMF Survey*; the "New Rate" represents the latest available information.
[3] The Uruguayan new peso is being depreciated on a daily basis according to a preannounced schedule.



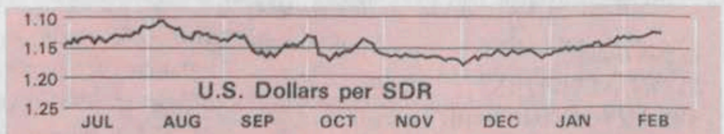
Premia/discounts over declared ECU central rates converted to U.S. dollar terms on the basis of March 23, 1981 rate of 1 ECU = $1.21315. Following the realignment of the central rates on October 4, 1981, they are calculated on the basis of the rate on October 5, 1981 of 1 ECU = $1.0918.
Effective October 4, the Deutsche mark and the Netherlands guilder were revalued by 5.5 per cent and the French franc and the Italian lira were devalued by 3 per cent against the other participants in the EMS.



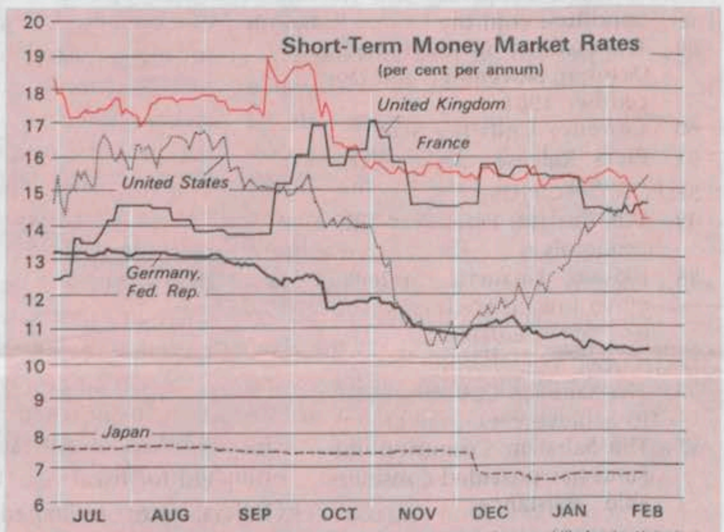


[1] Computed using weights implicit in the Multilateral Exchange Rate Model (MERM). The weights take account of the relative importance of a country's trading partners in its direct bilateral relations with them, of competitive relations with "third countries" in particular markets, of differences in the importance of the foreign sector in the overall economy in affecting, e.g., the sensitivity of wages and prices to changes in import costs), of the commodity composition of trade as among 4 major categories, and of estimated elasticities affecting trade flows.

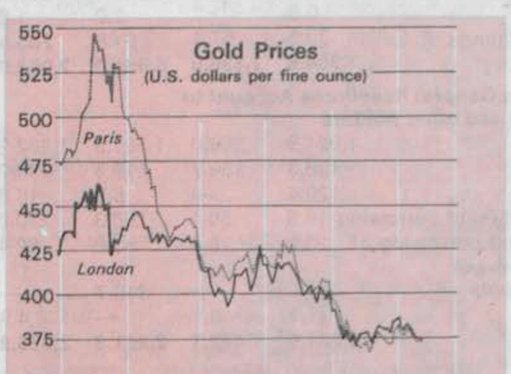
Data: IMF Treasurer's Department



Data: IMF Treasurer's Department



Short-term domestic interest rates are the yield on three month Treasury bills for the United Kingdom and the United States (the latter on a coupon equivalent basis); three-month interbank deposit rates for France and the Federal Republic of Germany (calculated on a 365 instead of 360 day year from March 1981); and for Japan, the discount rate on two-month (private) bills.



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