BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
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CONFIDENTIAL (FR)

TO: Federal Open Market Committee

FROM: Arthur L. Broida

Enclosed for your information is a copy of a report by Governor Wallich and Mr. Truman on the recent annual meetings of the International Monetary Fund and World Bank.

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Edwin M. Truman
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CONFIDENTIAL (FR)

Report to the F.O.M.C. on
The Annual Meetings of the Governors of the I.M.F. and World Bank
September 30 - October 4, 1974

The immediate problems facing the world economy, rather than long run monetary reform, received the primary focus in speeches and private discussions at the Annual Meetings of the Governors of the I.M.F. and World Bank held in Washington September 30 - October 4.

Inflation is still regarded as the major problem in the context of the business cycle. But considerable concern was also expressed about the risks associated with the slowdown or reduction in the rate of growth of real economic activity in many countries. Among the developed countries, this latter theme was stressed by the representatives of Italy, the United Kingdom and Canada. Moreover, most representatives from developing countries emphasized their worries that a slowdown in the industrialized countries would aggravate the already serious economic problems of those developing nations that are not oil exporters.

Massive oil-related current account imbalances were the particular aspect of the world economic situation that attracted principal attention. No optimism was expressed that the price of petroleum would come down in the near future and reduce the root cause of these imbalances. The focus was on means of financing countries' oil deficits. It was generally agreed that under the circumstances the mechanisms presently available for the financing of oil deficits had worked reasonably well over the past year. But it was argued by many -- for example, the British, the Italians, and the Germans -- that the private market mechanisms could not accomplish the whole job.

Denis Healey, U.S. Chancellor of the Exchequer, proposed that a new international facility much larger than the I.M.F.'s present Oil Facility should be established. The British apparently favor the establishment of such a facility in the I.M.F. along side the present, concessional Oil Facility at terms closer to commercial rates. This new facility might borrow not only from oil-exporting countries but also from countries receiving disproportionate shares of the investments of the oil exporters. The French and the Japanese, among others, urged that this proposal receive serious consideration. The Managing Director of the Fund, Johannes Witteveen, apparently prefers to enlarge the scale of the Oil Facility that has already been established. The German Minister of Finance, Hans Apel, while not ruling out an expansion of the I.M.F.'s Oil Facility, spoke in favor of "the creation of a specialized investment institution, operated jointly by oil producing and oil consuming nations, that would facilitate the placement of oil revenues in a stable and mutually advantageour manner." By implication, this institution would operate outside of the I.M.F.

The U.S. position, as expressed publicly by Secretary Simon, was that "existing financial arrangements" will continue to respond "reasonably well to the strains of the present situation." The United States did not rule out additional international lending mechanisms if it was demonstrated that there was a clear need for them. "Various alternatives for providing such supplementary mechanisms should be given careful study."

Against this background, the I.M.F.'s new Interim Committee, the successor body to the Committee of Twenty, agreed at its first meeting on October 3 that it should give urgent attention to the "recycling question." It commissioned the Executive Directors of the I.M.F. to prepare a study of the need for further governmental involvement, either through the I.M.F. or otherwise, in facilitating the recycling process. The Committee will meet on January 15-16, 1975, to consider this study.

The Annual Meetings seemed to create some support for the Witteveen view that "the problem of recycling . . . requires a bigger role for various forms of official financing, with the I.M.F. having a primary responsibility in this field." The prospects for further discussion of the many proposals in this area depend not only upon the political willingness of many of the same countries to make funds available in connection with any arrangements that might be agreed in principle. It should be remembered that the I.M.F.'s present Oil Facility with its comparatively modest $3.5 billion in resources required more than six months of intense discussions before it was agreed upon.

Other possible means of financing countries' payments imbalances also received attention during the Annual Meetings.

First, the G-10 countries agreed to renew with modifications the General Arrangements to Borrow, although some of the technical details have not yet been worked out.

Second, on the enlargement of I.M.F. quotas in connection with the current, quinquennial review of quotas, the developing countries strongly supported a general enlargement of 70-100 percent. Many of the developed countries spoke in favor of a significant or substantial enlargement of quotas, which might be as large as 50 percent. German Finance Minister Hans Apel, on the other hand, said that there was no need for a general increase in international liquidity; "the Fund as the guardian of the international monetary system should not, by its own actions, engender new inflationary pressures." The United States did not refer to a specific figure for quota enlargement, but Secretary Simon observed that the question should be considered "in light of today's needs and under present conditions of relative flexibility of exchange rates." The Interim Committee agreed to consider the question of quota enlargement, which is scheduled for decision by February 8, 1975.

Third, on gold, both the Italians and the French spoke in favor of further steps facilitating countries' mobilization of their gold holdings. The French Minister of Economy and Finance, Jean-Pierre Fourcade, forcefully stated the French view that "the special status of gold should be eliminated, that is to say, it should be treated like any other monetary asset." He also argued that the I.M.F. should not be authorized to sell its gold in the private market. Secretary Simon stated the opposite view on this question. The Interim Committee agreed that it would review the role of gold in the I.M.F. Articles of Agreement in connection with the question of quota increases -- 25 percent of which heretofore have been paid in gold -- and in connection with other proposed amendments to the Articles.

Fourth, many representatives of developing countries gave their support for a renewal of SDR allocations. Speaking for Italy, Emilio Colombo expressed qualified interest in new SDR allocations, "at least to the extent that oil-producing countries indicate their willingness to accept them in payment for oil." The issue of SDR allocations, of course, is bound up with the issue of establishing a link between SDR allocations and development assistance, which also has been assigned to the Interim Committee.

Except on the part of the French and a some representatives of developing countries, there was general disinterest at the Annual Meetings in promoting the role of the SDR and the general evolution of the international monetary system. Nevertheless, the new Interim Committee consisting of Finance Ministers and Central Bankers was established. It met and elected John Turner, the Canadian Minister of Finance, as its chairman for two years. The evidence from the first meeting suggests that the Interim Committee may become a vigorous body that will be active in the supervision of the operation and evolution of the international monetary system.

The first meeting of the new joint Fund/Bank Development Committee, was less auspicious. This ministerial committee has been assigned the task of dealing with the problems facing those developing countries most seriously affected by the present world economic situation. The difficulties faced by this enterprise were reflected in the wrangling that preceeded the selection of Henri Konan Bedie, Minister of Economy and Finance of the Ivory Coast, as its chairman and the selection Henry Costanzo, of the United States, as its executive secretary.