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ECONOMIC AND SOCIAL COUNCIL

Resumed Fifty-first Session

OFFICIAL RECORDS

Wednesday, 27 October 1971, at 10.50 a.m.

NEW YORK

President: Mr. Rachid DRISS (Tunisia).

Adoption of the agenda (E/L.1463 and Corr.1)

1. The PRESIDENT drew the Council's attention to the provisional agenda (E/L.1463 and Corr.1) and informed the Council that the United States delegation would not press its proposal to convene a special session of the Commission on Narcotic Drugs in October 1972. He accordingly proposed that item 7 of the provisional agenda (Proposal to convene a special session of the Commission on Narcotic Drugs in October 1972) should be deleted.

It was so decided.

The agenda, as amended, was adopted.

AGENDA ITEM 1

Report of the International Monetary Fund (E/5075)

2. Mr. SCHWEITZER (Managing Director, International Monetary Fund) said that, although the present difficulties of the monetary situation chiefly reflected strains in economic relations among the major industrial countries, they were also of profound significance for the developing countries for without the restoration of orderly trade and payments relations the development efforts of those countries would suffer.

3. The period since the mid-1960s had been marked by recurrent crises in gold and foreign exchange markets, evidenced by enormous shifts of capital among the major financial centres. Such shifts had been accentuated by the increasing size of the funds available for those operations as financial markets throughout the world became more closely integrated. Underlying those crises was the emergence of disequilibria in the balance of payments of a number of leading industrial countries, disequilibria which had been in large measure due to differences among countries in the intensity of inflationary pressures and to inadequate international co-ordination of policies adopted to control those pressures. Moreover, payments imbalances had been further increased by delays in the application of internal or external corrective policies.

4. Those conditions, reinforced by speculative forces, had been responsible for transfers of a large volume of short-term capital from the United States of America to Europe, which had caused five European countries to take exchange rate action in May. Despite that action, the international payments situation had remained precarious largely because of the continuing deficit in the United States balance of payments. On 15 August, the United States authorities had taken wide-ranging measures, such as the suspension of the convertibility of the dollar into gold and other reserve assets and the imposition of a general import surcharge, which might seriously disrupt trade and currency relations within the international community. At the same time those measures afforded an opportunity for strengthening such relations and removing the basic causes of weakness that had characterized the international monetary system over the past few years.

5. When the Governors representing the 118 member countries of the International Monetary Fund had met in September at Washington, they had thus been confronted with both a risk and a challenge: the risk had been that if common understandings were not reached, the situation would continue to deteriorate; the challenge had been for the international community to agree on the appropriate course of action. The Governors had voiced deep concern about the situation but had stressed the opportunity that it offered to devise and adopt new measures, both for the immediate future and for the longer run, that would lead to a strengthening in the performance and structure of the international monetary system in the interest of all members. A consensus had emerged on some important issues and the Governors had unanimously passed a resolution calling upon all members to collaborate with the Fund and with each other in establishing a satisfactory structure of exchange rates, which would be maintained within appropriate margins, in facilitating resumption of the orderly conduct of the Fund's operations, which had been affected by recent developments. That last point had special relevance to developing countries. Because of the limited external financing available to those countries, they must be assured of continued access to the Fund's resources in order to tide them over their payments difficulties.

6. Members had also been called upon to collaborate in efforts to reduce the present restrictive trade and exchange practices and to establish satisfactory arrangements for the settlement of international transactions. As far as the long-term problems were concerned, the Executive Directors of the Fund had been requested to make reports to the Board of Governors without delay on the measures that were necessary or desirable for the improvement or reform of the international monetary system. There had thus been a clear consensus that international action was required to resolve the present difficulties and that such action would serve the economic interests of all members, and not least those of the developing countries, whose vulnerability in the crisis had been widely recognized by the Governors. The view had been expressed that a major collaborative effort was needed to deal adequately with the present imbalance in world payments and that, in particular, the international community should co-operate with the United States of America in the task of achieving a fundamental improvement in its balance of payments. It had been agreed that there should be a realistic new structure of exchange rates for the major currencies and that any such currency

realignment should take place as expeditiously as possible and should be accompanied by some temporary widening of the possible margins of fluctuation around parity.

7. For the longer term, improvement or reform of the international monetary system would involve measures relating both to the effectiveness of the international adjustment process and to improvement in control over the volume of international liquidity. To those ends, all aspects of the system were being studied by the Fund, including the role of reserve currencies, gold, and special drawing rights, the arrangements to be made for convertibility of currencies, the provisions of the Articles of Agreement with respect to exchange rates, and possible measures to deal with the problems created by destabilizing capital movements. Many Governors had expressed their belief that the evolution of the international monetary system should include a major increase in the role played by an internationally managed reserve asset. In that context, it had been thought that the special drawing rights could in time become the main asset in which countries would hold their reserves. Experience with that facility since its activation in 1970 left no doubt that a reserve asset, created through international agreement, could function smoothly and effectively. An expanding role for special drawing rights implied that reserves should no longer be subject to major fluctuations as a result of changes in holdings of reserve currencies. At the same time, such a reform meant that the level of global reserves, a matter affecting all members of the Fund, would be controlled by collective decision.

8. He took satisfaction in the fact that the consensus achieved at Washington was in line with Economic and Social Council resolution 1627 (LI) in which the International Monetary Fund was invited to accord the highest priority to seeking long-term improvements of a kind which would be of benefit to developed and developing countries alike. He fully shared the concern that the Council had expressed about recent events and the stress it had laid on finding solutions that should be beneficial to the entire international community. Bearing in mind the interests of all its members, the Fund had already given considerable attention to many aspects of possible reform and would intensify its efforts in that field.

9. With respect to possible changes in the method of adjusting exchange rates, two important points had emerged from the views expressed at the annual meeting. The first was that there was universal recognition of the drawbacks and risks involved in any prolonged departure from agreed rules on the regulation of exchange rates; a breakdown in the observance of such rules posed a serious threat to free and orderly trade and payments relationships. Such a breakdown would bear most strongly on the less developed countries that were not responsible for it and least able to withstand it. The second point was that there must be a substantial improvement in the working of the adjustment process. The experience of the past decade had emphasized the disadvantages for all countries of allowing either deficits or surpluses to cumulate over time. It was generally agreed that payments adjustment must be made a smoother process and must therefore be brought about more promptly. That meant that whatever new rules might be set up, they must bring about and maintain a satisfactory structure of exchange rates. They might allow some measure of flexibility such as the temporary widening of the margins of fluctuation around parity, but all members of the Fund were determined to exclude excessive fluctuations and competitive exchange alterations.

10. The unmistakable message of the annual meeting was that, whatever detailed form the modifications in the international monetary system might take, they must continue to be based on the essential principles underlying the system designed at Bretton Woods. That system had been based on adherence to a set of international rules and on a realistic structure of exchange rates, and it had been universally recognized that those principles must remain the cornerstone of any new system if the needs of world trade and economic development were to be adequately served. At the present juncture it was easy to forget that, in many respects, the Bretton Woods system had been remarkably successful. The principle that determination of the rate of exchange for each currency was a matter of international concern had been generally observed, and trade and payments had largely been carried out in a selling of multilateralism and convertibility. The contrast in those regards with the period before the Second World War had been striking, and the unparalleled growth of production and trade throughout the world in the past 25 years had been even more striking.

11. Some had expressed the view that the difficulties which had confronted the international monetary system could be largely overcome by allowing the free play of market forces to determine exchange rates. However, the external value of a country's currency exerted an important influence on its aggregate output and expenditure, as well as on the allocation of its resources. That was why national Governments could not avoid intervening in the foreign exchange market, but such intervention would in turn affect the exchange rates of other currencies and thereby other national economies. Rules must therefore be retained bearing on the exchange rate policies of national Governments in order to safeguard the interests of all countries.

12. The Fund had always been opposed to exchange rate rigidity. It had, for example, actively supported flexible exchange rate policies in developing countries which were experiencing persistent inflation. Frequent adjustments made by those countries in the exchange rate in response to domestic inflation had helped them to minimize recourse to trade and payments restrictions and to restore or maintain an open economy. However, the authorities of the Fund firmly believed—and experience of the past two decades amply confirmed that belief—that the maintenance of internal and external stability provided the most suitable environment for sustained economic progress. It was therefore important that all countries should make every effort to maintain domestic financial stability, and a large majority of developing countries were doing so.

13. There was a danger that that effort might be undermined by uncertainties and disorder in exchange markets of major trading countries. Changes in terms of trade which resulted from exchange rate fluctuations might affect the capacity of developing countries to import and thereby create difficulties for investment and manufacturing activities. In addition, exchange rate changes might increase the burden of external debt for some countries. The manage-

ment of public sector finances was made more difficult by undue fluctuations in import costs and export prices, which were frequently of substantial importance in determining the levels of revenues and expenditures. In particular, exchange rate uncertainties were likely to frustrate orderly planning for development.

14. The importance to the developing countries of restoring the rules governing trade and currency relationships had been underlined by the developments of recent months. The currency disturbances appeared to have contributed to a slippage in commodity prices, particularly of metals. Another disquieting result of the recent crisis had been a stalemate in the negotiations for the untying of development loans. The prospect of a much-needed increase in the volume of development aid also seemed to have suffered a setback. Perhaps even more serious were the effects of recent events on the efforts of developing countries to diversify their exports. In the case of manufactured products, which were the key element in diversification efforts, exporters in many developing countries were working in new markets with thin profit margins, and any unexpected changes in prices, exchange rates or trade barriers might discourage exports altogether. Exchange rate fluctuations, together with commercial restrictions such as the import surcharge recently imposed by the United States, had, therefore, particularly unfavourable effects on the economies of many of those countries. It was especially unfortunate that those disturbances had occurred when the developing countries were already faced with a rising burden of external debt and the difficult task of creating new opportunities for productive employment for their rapidly growing populations.

15. It was of great importance to those countries that international rules in the field of trade and exchange policies should be observed by the major industrial countries. Such rules were an important protection which smaller and weaker countries had from the possibility that larger and more powerful countries might employ exchange and trade policy for their own advantage. It was appropriate that all countries, developed and developing alike, should participate in international collaboration on matters which profoundly affected their own interests, but such participation was only possible if there existed an accepted code of procedures operating through established international institutions.

16. Referring once again to the necessity of maintaining principles of international collaboration and orderly procedures for the determination and regulation of exchange rates, he said that at a time when an effort was being made to reform the international monetary system it must not be forgotten that a successfully operating system of any sort presupposed responsible monetary and fiscal policies in all countries, especially the major ones. There were thus challenges both to the international economic community and to each Government individually. Collectively, all Governments must collaborate in strengthening the international monetary system, especially with respect to the method for adjusting exchange rates and for controlling the level of international reserves. Individually, each Government must do its utmost to maintain financial stability, without sacrificing the goals of high employment and rapid growth it had set itself. In that regard, the Governments of the major developed countries bore an especially great responsibility, since economic stagnation or excessive price inflation in those countries would be reflected in increased difficulties for the developing countries. Indeed, the development needs of members called for additional efforts on the part of the more fortunate nations. There was urgent need for an improvement in the international climate for development; in particular, there must be a substantial increase in the flow of official capital and aid to the developing nations. Without such improvement it would be difficult to achieve the goals that had been set for the Second United Nations Development Decade.

17. After a hesitant beginning following the developments of mid-August, an attempt was now being made to devise a durable solution to the present problems. That approach, in itself, represented important progress and spoke well of the constructive attitude of the international community. There was, however, no time for pause. Any undue delay would tend to harden what were currently temporary measures into entrenched practices in the future; that would make a satisfactory solution immensely more difficult. Consequently, the sense of urgency must not be forsaken in accomplishing the task that lay ahead. It would require much hard thinking and complex negotiation and, above all, a continuing spirit of accommodation and support on the part of all nations. He had every hope that that endeavour would be successful.

18. Mr. PALEWSKI (France) briefly traced the monetary situation since 1970, referring to the doubts surrounding the dollar, the persistence and worsening of the United States balance-of-payments deficit and the massive movements of short-term capital from the United States to Europe and Japan. That capital had gone, in particular, to those countries which had not protected themselves by adequate exchange control arrangements or by an interest rate policy consistent with the international rates and whose liquid assets had been further increased by the granting of special drawing rights.

19. In 1971, the central banks of the Federal Republic of Germany and of the Netherlands had stopped supporting the exchange rate of the dollar against the mark and the florin on the exchange markets, so that a large number of countries no longer discharged their obligation under the articles of agreement of the International Monetary Fund to keep the exchange rate of a currency within 1 per cent of its declared parity. After pointing out that speculation had obliged certain currencies to revalue, he said that the United States Government had, in August 1971, taken commercial and monetary measures which had completed the breakdown of the international monetary system. As could be seen from the report of the Fund, which emphasized that it was essential to rectify the American balance-of-payments position if there was to be a return to equilibrium in international payments, the foreign trade deficit of the United States was at the root of the present crisis.

20. He then reviewed the negative effects of the present situation. First of all, from the monetary point of view, he noted that the stability of the international monetary system was threatened. From the point of view of trade, he would regret to see any failure of the efforts made since the

end of the war to free international trade from protectionism, especially as the American balance-of-payments deficit was due not mainly to trade but largely to movements of capital and investments abroad. From the point of view of relations with developing countries, he was afraid that the target of 1 per cent of the gross national product which had been recommended by the United Nations Conference on Trade and Development (UNCTAD) and included in the International Development Strategy for the Second United Nations Development Decade would be in jeopardy and that the prices of basic commodities would be subject to increasingly substantial fluctuations.

21. He feared that the International Monetary Fund might lose the importance and standing it had so far enjoyed and he hoped that its member States would reach a minimum of agreement on economic and monetary matters. The real danger lay not so much in the persistence of uncontrolled inflation as in a lack of awareness of a world employment problem. That was why his country believed that a lasting settlement could be achieved only by international negotiation which should start as soon as possible and should take into account the views of the developing countries.

22. Some of the proposals for the solution of the current crisis made at the last annual IMF meeting appeared to have met with the implied agreement of the representatives. They were: a realignment of all currencies, without exception; return to fixed parities; moderate widening of spread of permissible fluctuation, at least temporarily; more equitable distribution of certain burdens between the United States and the partners concerned; stronger and more consistent world effort in favour of the developing countries; measures to restrict disturbing movements of capital; and a composition of international liquidities which, apart from gold, decreased the role of the reserve currencies and increased that of such "neutral" liquidities as special drawing rights.

23. His delegation approved such measures but felt that they should be supplemented by special provisions in favour of the developing countries, which were directly concerned because of the effects of monetary instability on their economies and suffered from the decreased purchasing power of the currency in which most of their commodities were sold in the world market. The industrial countries should endeavour to establish or improve machinery to protect commodity prices from market fluctuations, and to return to a system of fixed parities, which was a necessary if not a sufficient condition for stable prices of raw materials. The industrial countries should also increase their assistance to the third world so as to keep pace with their increases in public expenditure. His delegation still could not accept the establishment of an organic link between the issue of special drawing rights and the volume of assistance, but it would be prepared to support a scheme whereby industrial States which had not yet attained the goal of 1 per cent would, in order to come closer to that goal, commit themselves to spending on assistance part of the special drawing rights allocated to them.

24. He praised the report of the International Monetary Fund, which was a model of clarity, intelligence and hope.

25. Mr. AYOUB (Tunisia) said that his delegation has listened with even greater attention than usual to the statement just made by the Managing Director of the International Monetary Fund because of the fact that it was being made after the collapse of the Bretton Woods system.

26. Even though the 1971 IMF report had been prepared before the United States decision of 15 August, it emphasized, as it had in previous years, the need to combat world inflation, and it reiterated the statement in the 1970 report that the need to rectify the United States balance-of-payments position remains the most urgent task in the field of international payments. Unfortunately, the repeated warnings of the Fund had not been heeded, and the result was the monetary crisis of the current year followed, on 15 August, by the collapse of the Bretton Woods system.

27. There was no single or simple cause of the crisis, but it stemmed from a succession of economic events and policies in the main industrial countries over a period of years. The main origins of the situation were therefore the disequilibrium in the balance of payments of certain industrial countries and the uncontrolled movements of short-term capital. The resulting instability of exchange rates would probably mean a re-evaluation of the currencies of several developed countries and, consequently, an increase in the prices of the finished products and capital goods which the third world had to buy. The poorer countries were thus suffering the consequences of a certain failure to act on the part of several industrialized countries, which had not only not heeded the repeated warnings of the International Monetary Fund but had also not abided by the Bretton Woods agreements, while the poorer countries obviously had no decision-making power whatever over the functioning of the system. In addition, the continued inflationary pressures in the industrial countries were already having repercussions on the terms of trade.

28. That situation was due to disregard for collective responsibility in the spheres of economic development and international monetary policy. There were many people who still remembered the serious and protracted upheavals which had affected the world during the 1930s following unilateral measures relating to economic controls and monetary safeguards. In the present crisis, certain industrial countries had resorted to the same methods to solve domestic problems resulting from the monetary confusion and had disregarded the interests of other industrial countries and of the poorer countries.

29. There was, however, some hope that the bankruptcy of the agreements—still partially in force—would make it possible to start afresh on a new and more equitable foundation. In his delegation's view, the proposals made by the International Monetary Fund might serve as such a foundation and make possible a universally acceptable outcome to the recent negotiations of the Group of 10. In those negotiations, however, the members of the Group of 10 must take into account the need to involve the undeveloped countries in the decision-making process and to set up machinery to compensate them for the losses which they were bound to sustain as a result of the realignment of currencies. While it was difficult to dispute the need for a wider permissible spread in the fluctuation of exchange rates so as to strengthen the mechanisms of adjustment, it was no less urgent to draw attention to the adverse effects which such action would have on the

developing countries. The central banks of those countries already found it difficult to protect their assets from the effects of speculation under the system of fixed parities. Those difficulties would certainly be increased under a system of wider fluctuations margins which would be of more benefit to speculators, banks and firms with large financial and technical means at their disposal than to small firms and countries, which would be practically defenceless against speculative manoeuvres. That was why the Tunisian delegation was in favour of maintaining the fixed parity system with fluctuation margins that were as narrow as possible.

30. The creation of a neutral reserve currency such as the special drawing rights would have to be supplemented by a link between the special drawing rights and aid to development, in conformity with the relevant provision of the International Development Strategy.

31. He hoped that the negotiations now in progress would result in agreement before the end of 1971, or at least before the third session of UNCTAD, to be held in April 1972, lest that session should result in a failure that would do irreparable damage, particularly with respect to the target of transferring to the developing countries financial resources equivalent to 1 per cent of gross national product.

32. He also expressed the hope that the optimism of the Managing Director of the International Monetary Fund was well founded, and that the consensus adopted in Washington would soon be put into practice on the basis of the underlying principles of Bretton Woods.

33. Mr. CABRIĆ (Yugoslavia) said that the report of the International Monetary Fund, the views expressed to the 1774th meeting of the Council on 6 July 1971 by the Managing Director of the Fund and the statement which Mr. Schweitzer had made at the present meeting gave the Economic and Social Council an excellent picture of the situation, so that the Council could make a realistic judgement of international monetary developments and their consequences for economic development as a whole, and especially for the progress of the developing countries.

34. His country continued to maintain active relations with the International Monetary Fund, not only through current business activities, but also with regard to the establishment of new stand-by arrangements, and the distribution and utilization of special drawing rights.

35. Since the Yugoslav Federal Secretary for Finance had already presented the views of his Government regarding the present monetary situation at the annual meeting of IMF, he would refer to some of the problems which required special attention and which were of interest not only to the international community in general but also, and especially, to the developing countries.

36. The Group of 77 had recently examined the international monetary situation in detail and had formulated its position and its views in a statement which would be circulated to all the States Members of the United Nations through the Second Committee.[1]

37. As his delegation had already observed during the general debate in the Second Committee, the present crisis was the consequence of a series of developments that had accumulated in the course of post-war economic growth. In the consideration of that economic growth, particular emphasis should be placed on the fact that the majority of the countries of the world had lagged behind the industrial countries.

38. After having just adopted the International Development Strategy, the international community was already faced by an extremely serious crisis which was liable to disrupt the programme for the Second Development Decade. Since the developing countries were particularly vulnerable, although they were in no way responsible for the crisis, they were following it with concern. They recognized the primary role of the highly industrialized countries in solving the problem, but they could not reconcile themselves to the status of mere onlookers. It was therefore essential that when national and international decisions were made, full account should be taken of the possible effects of those decisions on the economic growth of the developing countries. Moreover, consideration might be given to exempting the developing countries from the obligation of applying any decision which could adversely affect their economic development.

39. His delegation was convinced that the solution of the current problems required close co-operation at the international level. The International Monetary Fund should pursue its present activities in conjunction with all the other United Nations bodies concerned with development, and with all interested organizations outside the United Nations system. There was no need to change the existing monetary system totally in order to solve the current problems since, despite its weaknesses, the system had worked successfully so far. It would be enough to introduce certain corrections into it so as to render it more flexible and thereby enable it to adapt more easily to new situations. The International Monetary Fund had a very important role to play and, in fact, could be said to be irreplaceable at the moment.

40. His delegation was prepared to continue to co-operate with the International Monetary Fund and, within the limits of its possibilities, to lend it necessary support.

The meeting rose at 11.55 a.m.

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1 A/C.2/L.1166.