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DEVELOPMENT AND INTERNATIONAL ECONOMIC CO-OPERATION

International co-operation in the fields of money, finance, debt, resource flows, trade and development

Report of the Secretary-General

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I. INTRODUCTION

1. At its thirty-ninth session, the General Assembly adopted, on 18 December 1984, resolution 39/218 entitled "Development and international economic co-operation". The General Assembly emphasized the vital importance of issues related to money, finance, debt, resource flows and trade for development, prosperity and good relations among peoples and the urgency of measures to promote wider co-operation among nations on these issues. It also emphasized the need for consistency between the international trade, monetary and financing systems and policies.

2. In the operative paragraphs of the resolution, the General Assembly requested the Secretary-General to consult Governments of States Members of the United Nations and members of the specialized agencies and to ascertain their specific views on expanding international co-operation in the fields of money, finance, debt and resource flows, including development assistance and trade, with special attention to the interests of the developing countries, taking into account the effects of the economic crisis on their economic and social development; to seek the views of the relevant organs, organizations and bodies of the United Nations system, in particular the United Nations Conference on Trade and Development, the International Monetary Fund and the World Bank, as well as the General Agreement on Tariffs and Trade, on enhancing their effectiveness to support in every respect the actions taken by States to strengthen international co-operation in these areas; and to prepare a report based on the outcome of the consultations to be circulated to Governments not later than the first quarter of 1985 and to be updated subsequently, as appropriate, for submission to the General Assembly at its fortieth session.

3. The consultations undertaken in response to that resolution took the form of (a) a note verbale sent to all Member States, specialized agencies and relevant organs, organizations and bodies of the United Nations system; and (b) the study of documents, statements, declarations, communiqués and reports which, in the views of Governments, articulated comprehensive expressions of positions held by countries and groups of countries on the issues raised by the resolution.

4. The following Governments have replied to the note verbale: Argentina, Bangladesh, Bhutan, Brazil, Byelorussian Soviet Socialist Republic, Canada, China, Cuba, Cyprus, Ecuador, Egypt, Finland, German Democratic Republic, India, Indonesia, Italy (on behalf of the member States of the European Economic Community), Jordan, Libyan Arab Jamahiriya, Mexico, New Zealand, Norway, Pakistan, Philippines, Poland, Qatar, Romania, Senegal, Sweden, Togo, Ukrainian Soviet Socialist Republic, Union of Soviet Socialist Republics, Uruguay, Venezuela and Yugoslavia. In addition, the General Agreement on Tariffs and Trade (GATT), the International Monetary Fund (IMF), the United Nations Conference on Trade and Development (UNCTAD), and the World Bank provided information and documentation.

5. An interim report was circulated to all Member States at the beginning of April 1985. The present report, while drawing heavily on the previous version, incorporates observations made in the course of informal consultations with delegations undertaken in June 1985 and updates, when appropriate, the interim report.

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6. Since the preparation of the interim report, some important events have taken place: the April 1985 meetings of the Interim and Development Committees of the IMF/World Bank; the Bonn summit in May; the release of the report of the Group of Ten on the functioning of the international monetary system in June; the ministerial meeting of the Group of Ten in Tokyo on 21 June; the general debate at the second session of the Economic and Social Council in July 1985; the completion of the report of the Group of Twenty-four on issues in international monetary reform in August; and the publication of the UNCTAD "Trade and development report, 1985" in early September.

7. The present report should be seen as part of this ongoing process. It is a discussion paper, essentially concerned with the identification of key issues and with more effective ways to have them discussed by Governments.

8. The report consists of two main sections. The first assesses major policy issues arising from the present international economic situation and examines the interrelatedness of these issues in the areas of money, finance, debt and trade in the light of the consultations and the general state of international negotiations on these matters. The second details the responses to the consultations and summarizes the proposals raised in them. A selective list of the documents consulted in preparing the report is given in the annex.

II. POLICY ISSUES FOR THE WORLD ECONOMY IN THE MID-1980s

A. Key challenges and policy issues: national and international dimensions

9. A review of the past 10 years, together with an attempt to look ahead to the 1990s based on available projections and new policy perceptions, indicate that the economic challenges facing the international community have not been so great in 40 years, nor the prospects so uncertain for so many countries, as is now the case. However, the achievements of international co-operation during the last four decades are evidence of the capacity to face such challenges if the international community unites to do so.

10. The consultations have revealed widely shared concern about both short- and long-term growth prospects. The intensity and the international propagation of the cyclical economic recovery of the United States of America, which began at the end of 1982 and gathered strength in 1984, provided a significant boost to exports and incomes in many parts of the world and made for a more positive assessment of the immediate prospects. In 1985, however, the United States economy is slowing down, and this slow-down is not offset by an acceleration of growth elsewhere in the world economy.

11. Many uncertainties prevail with regard to the sustainability and wider international propagation of growth during the remainder of the decade. In addition, the first half of the 1980s has been marked by a major shift in policy perceptions and economic philosophies which poses fundamental questions for future international economic co-operation for development.

12. Projections for the remainder of the decade made by international organizations, including the United Nations, show rates of growth of output for developed, developing and centrally planned economies, as well as for world trade, far below the rates observed during the post-war period up to the early 1970s. In addition, many organizations consider that even these projections are not to be seen as predictions about the future but rather as indications of the domestic and international policy challenges that have to be faced if any reasonable degree of growth, stability and economic and social development is to be achieved.

13. For the populations of many countries in the developing world, the 1980s may turn out to be - whatever domestic effort is mobilized by their Governments - a decade of frustrated expectations and worsening standards unless present trends in the world economic environment are reversed. There is now recognition of the fact that a large number of the more vulnerable countries could experience not only economic stagnation but also economic and social decay involving a degree of human suffering and future welfare losses not captured by economic statistics. Thus far, however, little consensus on the means to restore economic and social progress has emerged.

14. It is now generally acknowledged that economic and social development depends on (a) a complex set of interactions between human resources and institutional factors; (b) the efficiency, coherence and thrust of domestic policies; and (c) the international environment. There has been much argument recently about the relative importance of the national and international aspects of the development process. Although not prominent in the responses to the note verbale, the subject has claimed increasing attention in the general debates in international organizations, for instance at the 1985 summer session of the Economic and Social Council. None the less, the distinction between the two aspects is easily exaggerated.

15. In fact, changes in world economic conditions pose challenges to all countries and bring both new constraints and new opportunities. Success in coping with the constraints and exploiting the opportunities depends on the flexibility and adaptability of an economy, and on domestic policies. But while a few countries have great freedom of action, in most countries domestic policies are substantially constrained by external factors. The capacity for an adequate domestic policy response thus differs from country to country depending on economic size, resources, vulnerability to external shocks, the structure and diversification of foreign trade, human resources and institutional factors. In these matters, generalizations conceal more than they reveal.

16. The evolving international economic environment to which every country must continuously adjust its short- and long-term domestic policies is today largely dominated by two factors. The first is the major industrialized countries' macro-economic policies and their interactions, and the second is the functioning of the international trade and financial systems as well as concessional aid programmes. The prospects for economic and social progress in an individual country, while principally dependent on the effectiveness of the country's domestic policies, cannot be assessed in isolation from the growth and stability of the world economy, which in turn depend on the policies of a limited group of major countries and are also affected by political tensions and regional conflicts.

17. Of particular importance to the purposes and the issues addressed in the present report is the structural change required to accommodate shifts in the patterns of comparative advantage among countries. Historical experience has taught two lessons in this regard. First, trade competitiveness is not entirely determined by geography, natural resources and factor endowments, but is partly a matter of choice and achievement, as the Japanese experience, to name only one, clearly indicates. Second, it is easier to accomplish required accommodations to shifting patterns of comparative advantage in the context of a growing world economy enjoying monetary and financial stability than in conditions of widespread unemployment and international monetary instability which nurture protectionist pressures and create uncertainties that hamper exports and trade-related investment decisions.

B. The current situation and the outlook for the rest of the decade

18. In 1984, the real rate of growth of output of the developed countries was about 4.7 per cent, the highest since the mid-1970s and only slightly below the average rate of growth observed during the 1960-1973 period. After four years of virtual stagnation from 1980 to 1983, the rate of increase in the volume of world trade in 1984 was about 8.8 per cent, approximately the same as that between 1960 and 1973. Many developing countries benefited from this recovery, although some did not. However welcome, the recovery was somewhat weaker than recoveries in the past, when underlying trends were more buoyant. At mid-1985, growth in the largest developed market economy seems to be sliding towards an annual rate of 2.6 per cent, and growth in other developed countries is also flagging.

19. This situation has led to significant differences in expectations. Some hope for and expect a continuation and consolidation of the recovery. Others fear a substantial slow-down in world economic activity. Such differences can be traced to implicit assumptions about the sustainability of existing imbalances and about the policies likely to be pursued.

20. Baseline projections to date suggest an annual growth rate in the developed countries of the order of 2.5 to 3 per cent in real output for the second half of the 1980s. With a 3 per cent growth rate in industrial countries, the volume of world trade is expected to grow at 5 to 5.5 per cent a year. The export volume of developing countries is projected to increase at nearly twice the growth rate of developed countries. The real output of developing countries is estimated to grow at an average rate of 4 to 4.5 per cent a year. Though well below the growth rates of the 1960s and 1970s, this level would be a considerable improvement over the rates in the early 1980s; however, it would not restore, by 1990, the real income per capita enjoyed by most developing countries in 1980.

21. These projections are necessarily based on specific assumptions about the evolution of world interest rates, prospects for net private bank lending to developing countries and the growth of private foreign investment. In some projections a gradual decline in interest rate to about 8 per cent by the end of the decade is assumed, private foreign direct investment is estimated to resume its

historical growth rate of nearly 11 per cent a year and private bank lending is expected to grow by something between 4 and 7 per cent. The realism of these assumptions depends on political choices and macro-economic policies in key-currency countries, on adjustment programmes in debtor developing countries and on the posture of the private international financial system.

22. In the early 1980s a combination of expansionist fiscal policy and restrictive monetary policy in the United States led to very large budget deficits, higher interest rates, and massive capital inflows, with a swing of over $100 billion in the United States current account between 1981 and 1984 (from a surplus of $11 billion to a deficit of $93 billion). This swing has become even more pronounced in 1985, when the deficit in the current account is expected to be over $120 billion. This trend is widely considered to be unsustainable.

23. The slow-down in the growth of the United States economy could be compensated for by higher growth in other industrial countries. Europe's growth of output has been slow and growth in employment slower still. Its current account has moved from a $0.2 billion surplus in 1981 to a surplus of over $27 billion in 1984, largely owing to the significant stimulus from United States imports. Since European import growth is unlikely to gather strength in the short term, this surplus is likely to grow further in 1985. The current account surplus of Japan rose from $6 billion in 1981 to $36 billion in 1984. Preliminary estimates indicate an even higher surplus in 1985. In these circumstances it is not, for most countries, present balance-of-payments constraints that discourage expansionary policies but rather the fear of rekindling inflation, which has been brought under control, the disinclination to increase budget deficits and also the lesson of previous individual attempts at expansion, which clearly demonstrated how quickly they could ruin the balance of payments.

24. Imbalances in the current account between developing and developed countries are no less important and even more difficult to sustain. The swing here has been dramatic; the combined current account deficit of 123 indebted developing countries dropped from $113 billion in 1981 to $38 billion in 1984. The current account deficit of the seven largest borrowers - $40 billion in 1982 - was virtually eliminated in 1984. To consider these current account positions sustainable in the medium term is to bet on the continuation of a net transfer of resources from debtor to creditor countries in the form of surpluses in trade and non-factor services of the order of 5 per cent of gross domestic product for the major borrowers. Such net resource transfers have been increasing since 1983, and in 1985 developing countries are expected to pay about $70 billion in interest while experiencing a combined current account deficit of $40 billion. This can only be done by generating increased trade surpluses which, if the recovery is thwarted, it will be difficult or impossible to do by expanding exports or cutting imports. There are already indications that surpluses attained by some of the large debtors in the developing world in 1984 will shrink during 1985. Moreover, balance-of-payments difficulties are severe in many developing countries that are not big debtors but that depend on commodity exports and have not shared in the United States recovery because their exports are principally directed to European markets.

25. The sharp curtailment of imports in developing countries has had a deflationary impact on industrial countries. Exports from Organisation for Economic Co-operation and Development (OECD) countries to developing countries were almost $50 billion lower (at an annual rate) in 1984 than in 1980-1981. According to UNCTAD estimates in the "Trade and development report, 1985" this reduction would account for a loss of close to 7 million work-years in OECD Europe and close to 1 million in North America. Rising unemployment in turn has contributed to new restrictions on exports from developing countries, especially in manufactures where about two thirds of such exports are subject to non-tariff barriers of one kind or another.

26. The present fiscal and current account imbalances pose a serious threat to the hopes for less volatile exchange rates, an open trading system, stable interest rates and renewed growth. Unless policies are changed, a slow-down is likely. In such a case, industrial countries might grow on an average at about 2.5 per cent which, combined with present protectionism, would result in developing countries experiencing export growth at no more than 3 per cent per annum. If real interest rates remained unchanged, the debt-service ratios of developing countries would grow, leaving no scope for imports to grow at all. Overall growth in gross national product (GNP) in developing countries would be only 3 per cent, leaving perhaps one half of 1 per cent for per capita growth. This sombre picture highlights the precariousness of the present situation and draws attention to issues of a systemic nature involving the international monetary and trading systems.

C. The international monetary system

27. The system agreed on at Bretton Woods contained explicit provisions concerning the essential aspects of relations among the currencies of independent nation States. Among the provisions were (a) the exchange rate régime; (b) the nature of international reserves; (c) the process of balance-of-payments adjustment; (d) the degree of currency convertibility; and (e) the régimes for short- and long-term capital movements. The agreement also provided, for the first time in history, for the management of the system as a joint international enterprise.

28. Convertibility among key currencies was restored. Long-term capital movements were gradually deregulated, but it was understood at Bretton Woods that short-term capital flows were to be subject to controls. This was required by the logic of a system that relied on discrete and significant exchange rate changes in predictable directions, thus creating one-way options for currency speculation.

29. Only a little more than a decade after the restoration of convertibility, the system began to break down in the other areas. The fixed-but-adjustable exchange rate régime gave way to the floating of key currencies. At Bretton Woods, the reserve system had been left as a gold exchange standard, supplemented by general drawing rights in the IMF, but no provision was made for the orderly expansion of reserves. The introduction of special drawing rights (SDRs) failed to prevent the rapid expansion of dollar reserves increasingly borrowed in the Euromarket, and international liquidity ceased to be internationally managed. Restrictions on short-term capital movements were made obsolete by the rise of the Euromarket and the new flexibility of key exchange rates.

30. There is broad consensus about the achievements and failures of the Bretton Woods system in these policy areas. Also, a fairly high degree of agreement exists about the underlying reasons for the partial breakdown of the system in the early 1970s. There is no consensus, however, on the reasons for the failure of the attempts to achieve international monetary reform or on the successes and shortcomings of the arrangements that emerged after 1973. Nor is there consensus on the need for reforming the present arrangements in the direction of a more stable and durable system or even on the procedures to follow in considering the matter.

31. Although Governments differ in their overall assessments of how the system has been serving the international economy, it would be wrong to think that present controversies can be reduced to an argument between those who press for comprehensive reform and those who, denying the need for it, believe that improving existing arrangements through consultations among a few players would suffice. Many share concerns about the weakness of the present arrangements in several pressing areas:

(a) The misalignments of exchange rates and the high degree of exchange rate volatility permitted by the present régime;

(b) The nature and supply of reserve assets, a topic that has become inseparable from the functioning of private international capital markets;

(c) Surveillance and the interrelated issues of conditionality and the treatment of developing countries.

1. The exchange rate régime

32. It is widely acknowledged that the admission of greater flexibility in exchange rates helped to preserve a relatively open trading and financial system, allowing nominal exchange rates to correct for differences in national inflation rates. However, the belief that floating rates would insulate national economies from external shocks and from the effects of other countries' policies proved mistaken. The experience of more than 12 years of floating rates has shown that national economies have perhaps become even more sensitive to outside shocks and policies, narrowing the scope for national autonomy in the design of domestic policies. Developing countries, in particular, have experienced serious difficulties under the present exchange rate régime.

33. A higher degree of variability of nominal exchange rates was expected, but movements in these rates have far exceeded expectations and have affected real exchange rates (corrected by inflation), which have shown persistent medium-term misalignments and sharp short-run variations usually unrelated to fundamental economic conditions such as trade competitiveness and current account balances. Volatility and misalignments in real exchange rates involve significant costs since misleading market signals and deep uncertainty about future conditions make investment decisions more difficult. Overvaluation may lead to short-term gains against inflation, but it exacerbates trade frictions and encourages protectionism. Undervaluation may promote exports, but it increases inflationary pressures.

34. When exchange rates of key currencies have shown persistent misalignments and have fluctuated widely it has been largely due to three sets of factors: divergent public or private perceptions of the sustainability of fiscal and monetary policies; lack of co-ordination in macro-economic policies; and the new characteristics of the currency markets, in which huge amounts of funds can be shifted around the world.

35. The liberalization of short-term capital flows has proceeded far beyond the extent thought advisable at Bretton Woods, and revolutionary developments in electronics and telecommunications have made it possible to move funds around the world in seconds in response to anticipated changes in interest rates or exchange rates. Such capital movements have come to dominate demand and supply in foreign exchange markets. The exchange rates of key currencies can show persistent misalignments unrelated to underlying fundamental economic conditions. Shifts of attitudes and expectations in the foreign exchange market, where herd-like patterns of behaviour and bandwagon effects have been well documented, can lead to sudden and destabilizing switches.

36. Capital movements have become so large that they make it difficult or impossible to control the expansion or contraction of international liquidity. A crude indication of this is a comparison between the maximum daily speculation of under $100 million against the pound sterling in the massive run of August 1947 and the maximum daily speculation of over $1.5 billion into the Federal Republic of Germany in May 1969. At present, the value of transactions in exchange markets carried on in a single day is estimated, very roughly, at between $50 billion and $150 billion. These transactions result from a complex web of trade and payments as well as portfolio adjustments and other financial operations. In annual terms, the value of international currency transactions recorded is in the order of $20 trillion to $40 trillion while the value of world trade is about $2 trillion. These figures raise the issue of what the Bank of International Settlements in its 1985 report terms "the implications for the conduct of monetary policy and prudential supervision, of internationally integrated, innovative and progressively deregulated financial markets".

37. In markets of this magnitude, no central bank can by itself intervene with lasting effect, especially not one seeking to appreciate its currency by selling foreign exchange. Effective intervention requires resources on a scale that rules out the possibility that intervention might be abandoned because of lack of funds. The only central banks with a potentially unlimited supply of a currency are the ones issuing it, and it is not even clear that the laws circumscribing their activities would today permit them to take a sufficiently firm posture, even acting together. Moreover, the implication of intervention for monetary policy would be an increase in the money supply in countries whose currencies are to be depreciated and a reduction in the money supply in countries whose currencies are to be appreciated. The risk of conflict between the objectives of exchange rate stabilization and monetary targets has to be carefully analysed.

38. At the meeting of the Group of Five in September 1985, key-currency countries agreed that exchange rates should better reflect fundamental economic conditions than had been the case, and they discussed co-operation to achieve a smooth decline

in dollar rates. Reducing misalignments of key currencies and establishing greater stability among them are essentially matters of co-operation among the countries. The issue is none the less of deep concern to other countries even if their role in this regard is limited. Other aspects of the functioning of the monetary system, especially long-term ones, concern non-key-currency countries directly and involve their policies; these aspects must be raised in larger forums with general participation or perhaps in representative ad hoc bodies, such as the Committee of Twenty on Reform of the International Monetary System and Related Issues in the early 1970s. Although there is no necessary conflict between key-currency co-operation in a small group and discussions in larger bodies, it seems appropriate to deliberate how different approaches could best be combined so as to ensure efficient and workable arrangements in which the interests of all countries would be fully taken into account.

2. International liquidity

39. The expansion and contraction of international liquidity now depends crucially on the behaviour of private international capital markets and in particular on the developed market economies' large international banks. For bank credit to be made available to deficit countries, two necessary and sufficient conditions must be met: the large international banks should have the capacity to attract funds, and they must decide to increase their international lending. However, the international private banking system is not a closed system. Its total assets and liabilities expand or contract because bank deposits are not the only option available for savers, whether domestic or foreign, nor is international lending the only option available to banks. The volume, terms and conditions of international bank credit are therefore affected by changes in the monetary and fiscal policies, the structure of interest rates and the risks and relative expected profitabilities in the financial and real markets of the key convertible-currency countries.

40. The fact that market-supplied international liquidity acquired through credit arrangements with financial markets has become preponderant in the world economy has far-reaching implications for the management of international liquidity. The most important is that the adequacy of international liquidity can no longer be assessed merely on the basis of recorded reserve holdings but must also take into account market perceptions about borrowing countries' "creditworthiness" and the availability of official sources of financing. A second implication is related to the risk of sudden shifts in the terms and conditions on which international liquidity is made available, owing to the market's late recognition of and abrupt response to changes in perceived creditworthiness. A third implication is that, as the majority of developing countries have only limited access, if any, to market borrowing, the present system does not serve them well.

41. These considerations have an important bearing on the place of SDRs as a reserve asset in the long-term evolution of the international monetary system. In this connection, both the report of the Group of Ten and that of the Group of Twenty-four called attention to the Articles of Agreement of the IMF, which call on members to collaborate with the Fund and with other members in pursuit of the objective of "better international surveillance of international liquidity" (art. VIII, sect. 7).

3. Surveillance

42. Today, the success of economic policy in one country depends a great deal on the economic policies of other countries, and the harmonization of economic policies has become an essential part of international economic co-operation. It is a difficult and delicate task which takes different forms, depending on the closeness and the nature of the association between the countries concerned. International scrutiny and discussion of national policies is an important part of the work of such bodies as OECD, GATT, the European Economic Community, the Association of South-East Asian Nations and the Council for Mutual Economic Assistance.

43. In the Second Amendment to the Articles of Agreement of the IMF, which became effective in 1978, article IV included the obligation of members to direct their economic policies towards fostering orderly economic growth with reasonable price stability, and it introduced, in section 3, the principle of Fund surveillance over the exchange rate policies of members.

44. Recent misalignments of exchange rates have directed new attention towards the need to make national economic policies consistent with the objectives of international adjustment, and the reports of the Group of Ten and the Group of Twenty-four reflect wide agreement that surveillance should be made more effective.

45. Article IV, under which present consultations and discussions with the members of the Fund take place, formally limits surveillance to exchange rate policies. In the different but related context of conditionality, the Fund's attention is much broader, and as the report of the Group of Ten states, there is a need to include in surveillance a wider range of issues, such as the mix of fiscal and monetary policy, structural problems and trade policies.

46. The Group of Ten agreed that surveillance had not been sufficiently effective in inducing policy changes in countries that had adequate access to external financing and did not require an IMF-supported adjustment programme. The Group also agreed that multilateral surveillance should concentrate on countries that had a large impact on the world economy.

47. The Working Group of the Group of Twenty-four concurred. The question was, how could surveillance have greater impact? The Committee of Twenty agreed in its report of 1974 that a process of "graduated pressure" should be incorporated in the procedures of the IMF in order to induce countries to make policy changes called for in the light of the international economic situation; however, there was no agreement on the forms. The Working Group of the Group of Twenty-four revived this idea. The Group of Ten, on the other hand, relied on peer-group pressure and the possible impact of publicity, which was discouraged in the Group of Twenty-four.

48. It is gratifying to find agreement that countries "must be ready to recognize the international implications of their policies and to give them more weight in their decision-making process", as expressed in the report of the Group of Ten, and also that the need for symmetry and even-handedness is expressly stressed.

49. It is perhaps necessary to emphasize that the objective of surveillance cannot be to impose on Governments policies that are not in their own long-run interest but rather to provide Governments with an international voice, warning them when domestic pressures for short-sighted attempts to benefit their own countries at the expense of other countries threaten to jeopardize orderly progress in the world economy and their own long-run interest. Surveillance can only be effective in a spirit of co-operation, which is difficult in a world that is much more integrated economically than it wants to be politically.

50. It should also be recognized that part of the difficulty in surveillance stems from genuine ignorance, uncertainty and the differing views that prevail with regard to the roots of stagflation in industrial economies, the nature of wage and price formation and the role of various rigidities that originate partly in political decisions.

D. The debt problem

51. Nothing has alerted the world community to the precariousness of the international monetary and financial situation so much as the risk of a debt crisis in the form of a widespread inability and refusal by developing countries to pay their creditors, a development that would bring serious disarray to the international financial system. An international debt crisis is not likely in this sense. However, in many developing countries the debt crisis is already a dominant fact of life. The steep rise in interest obligations and the drop in new bank lending have produced severe economic cut-backs in indebted countries.

52. According to World Bank estimates, the total external liabilities of developing countries rose from $610 billion in 1980 to $895 billion at the end of 1984. Of the latter amount, $142 billion is short-term debt of less than one year's maturity, about $35 billion is debt to the IMF and the remaining $717 billion is medium- and long-term debt. Private lenders held $472 billion of the medium-term and long-term debt and public lenders the remaining $245 billion.

53. The combined external debt of 16 major borrowers accounted for $518 billion, or 58 per cent of the total. Eight of these countries are in Latin America and had a joint debt of $330 billion. The other eight, of which six are in Asia, had a total external debt of $188 billion. The remaining nearly 100 developing countries had a total external debt of $377 billion.

54. The debt problem might thus appear to involve only a limited number of developing countries, but this conclusion would be premature. It is natural that the large debt problems are found in large countries having relatively high incomes, and it is also natural that the fate of these countries should be of special concern to the financial community. It should not be forgotten, however, that many smaller and weaker countries, whose debts are not to private banks but to Governments and whose problems do not provoke anxiety in financial circles, are none the less experiencing serious balance-of-payments problems of which their debt service is no small part.

55. The emergence of generalized debt-servicing difficulties in developing countries has been due to reduced export volumes, increased interest rates and deteriorating terms of trade. The global recession has undermined export volumes and weakened the export prices of primary commodities. High interest rates and the overvaluation of the dollar have contributed to the weakening of prices by reducing demand for stocks and by depressing the dollar prices of most commodities. This, and the fact that most of the debt is denominated in dollars and subject to variable interest clauses, has reduced developing countries' capacity to service debt.

56. This has led to the sudden withdrawal of private bank lending which has been a major element in the debt crises of the last few years. After years of rapid expansion, net lending by banks to developing countries has not grown at all since 1982, if involuntary lending under IMF-sponsored rescheduling packages for major debtors is excluded. In countries without exchange control, an outflow of capital has often aggravated the situation.

57. Low-income countries have had to rely mostly on concessional borrowing, which has not been subject to this sharp decline. None the less, many of these countries' debt-service ratios are now as large as or larger than corresponding ratios in the major debtor countries.

58. The present international debt problem is a cloud that hangs heavily over the prospects of the world economy. A reduction in the threat that it poses depends on the prospects for (a) sustained recovery in the industrial countries and a further fall in real interest rates; (b) a roll-back of protectionism in industrial countries; (c) a recovery in commodity markets; (d) a resumption of voluntary bank lending; and (e) continued adjustment programmes in debtor countries. Of all these factors, only the last is under the control of developing debtor countries themselves.

59. International efforts have so far followed a case-by-case approach in which the external environment has been taken as given. Adjustment programmes under rescheduling packages have consisted of policies that debtors were expected to adopt so that full debt servicing was ensured in the prevailing external situation. Such measures have had a deflationary impact on the world economy. The obligation of creditors has been limited to rescheduling repayments and providing new loans. In spite of multi-year rescheduling for three major debtors, the debt restructuring exercises of the past three years have not led to a very significant deferral of amortization. About 60 per cent of the debt will fall due within the next five years. Of particular concern is the large repayment of IMF advances scheduled for the coming years, which will reach almost $8 billion by 1987, much of it due from African debtors.

60. The quest for a solution of the debt problem in the short- and the medium-term should encompass ways of enlarging the resources available to developing countries and an intensification of multi-year debt rescheduling as well as a continuation of necessary domestic adjustment measures in the debtor countries. For the low-income countries in particular, an increased flow of concessional financing is essential. The cancellation of the official debt of poorer countries remains a matter of high

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priority. An intergovernmental dialogue on these matters, taking a realistic view of the prospects for the indebted countries, has been suggested and deserves serious consideration.

61. The debtor countries' ability to impose harsh domestic adjustment programmes and to endure lasting austerity rests on the expectation that these sacrifices have a meaning and a purpose, and that within a reasonable period of time foreign credits and expanding foreign markets will become available and real interest rates will fall. Socially and politically painful adjustments in the structures of production, consumption and factor utilization are being made on the assumption that developed countries will, for their part, adjust to observed shifts in comparative advantage instead of closing their markets. Any strategy for resolving the debt problem in a smooth manner must seek to ensure that such expectations are met.

E. Trade, protectionism and structural adjustment

62. The principles that guided international efforts to liberalize trade at the end of the Second World War and that became part of the General Agreement on Tariffs and Trade were multilateralism, reciprocity and non-discrimination in the form of the most-favoured-nation principle. The rules of GATT bind its signatories to obligations directed towards the objective of freer trade, while recognizing the need for escape clauses. The Agreement was soon amended to recognize that developing countries could not fully participate in GATT on a basis of equality and reciprocity.

63. Throughout the process of trade liberalization that has taken place since the end of the Second World War, a number of fields, notably agriculture and textiles, have been kept outside of multilateral trade negotiations. As tariff barriers were gradually reduced, non-tariff barriers became more prominent except where regional economic integration took place. The arguments for keeping agriculture and textiles outside the scope of trade liberalization were eventually extended to other fields, contributing to a proliferation of quantitative restrictions. International trade became increasingly "managed", and arrangements were made outside of GATT rules, as in the case of "voluntary" export restraints.

64. The international community has already agreed to a number of trade policy measures in favour of the developing countries. A system of generalized, non-reciprocal and non-discriminatory tariff preferences - the Generalized System of Preferences - was thought to be a significant contribution but it has not, as implemented, lived up to expectations owing mainly to the limited product coverage. Furthermore, the overall reductions in tariffs under the Tokyo Round have reduced the preference margins. All the existing schemes have now been renewed but, as most have been modified in product coverage, ceilings and designated beneficiaries, it is difficult to establish whether, on balance, the schemes have been improved.

65. In recent years, structural change in industrial countries has produced frequent calls for protection of domestic industries from foreign competition. The

adjustment policies and industrial policies that emerged in developed countries during the 1960s often became instruments of protectionism and sources of extensive subsidies. Although public policy is now shifting towards market principles and non-intervention, this shift has not prevented a resurgence of protectionist sentiment, and Governments have yielded in varying degrees to demands for import restraint. Thus, although the need for gradually phasing out uncompetitive industries is recognized by Governments, their ability to resist the pressures to support them has been uneven.

66. A major reason for the rising demand for protection of declining industries has been the persistent and unusually high level of unemployment in the developed market economies, a problem that must be addressed in its own right. In 1985, the third year of recovery from the depths of the world recession, progress in cutting back overall unemployment rates remains painfully slow except in North America. According to the OECD, unemployment in OECD countries is expected to increase in 1986 to over 31 million.

67. Overvaluation of currencies reinforces demands for protection. It erodes the competitive strength of industries that under more normal conditions would have a comparative advantage. A relatively stable but flexible exchange rate régime, which reflects the fundamental economic conditions guiding international trade, is not only an integral part of a properly functioning international monetary system but also necessary for the maintenance of an open trading system.

68. The commitments made at the 1982 Ministerial Meeting of GATT to roll back recent trade barriers have not yet been followed by much action. This has been one of the objections of some developing countries to the proposal for a new round of multilateral trade negotiations in GATT, but developed countries have seen it as an argument for a new round, since multilateral and reciprocal liberalization is easier to realize than unilateral. Another issue has been the wish for assurance that parallel efforts will be made to achieve greater exchange stability, without which it is thought by some that trade negotiations will be difficult or meaningless. The proposal to include services and investment issues in the next round has also met with objections, since an innovation of this kind would call for new rules and involve new agencies. One solution might be to hold parallel talks on trade in goods and trade in services. These difficulties seem likely to be overcome, and a new round would be helpful if an attempt were made to strengthen and improve the GATT framework and to bring under it the sectoral arrangements currently negotiated outside, which threaten to erode completely respect for GATT principles. It is important, however, that a new round should be carefully prepared so that it reflects the interest of all participants.

69. The Integrated Programme for Commodities is another international effort that has not met expectations. Had a comprehensive set of mechanisms to reduce international fluctuations of commodity prices been in place in the early 1980s - as envisaged by the Integrated Programme - it might well have softened the impact of recession on the export earnings of the developing countries. As things stand now, the Agreement Establishing the Common Fund for Commodities will not become operative without further support from some major developed market economies or from Eastern Europe. Recent experiences also suggest that, in negotiating renewals

of individual agreements, participants should make greater efforts to improve the agreements and not allow them to be weakened.

70. In view of the limited capacity of commodity agreements to stabilize export earnings, there remains a need to supplement such arrangements with enlarged and improved compensatory facilities. In 1983 and 1984, the conditions and procedures of the IMF Compensatory Financing Facility, and maximum drawings therefrom, were changed in a restrictive direction, and there is now a need to liberalize access to the Facility.

71. Greater efforts to enhance stability in primary commodity prices are necessary, but diversification of national economies in order to reduce reliance on one or a few primary commodities is the only way, in the long run, to lessen their vulnerability to adverse external developments.

F. Final observations

72. The consultations undertaken in the course of preparing this report and the consideration of other relevant information have confirmed that considerable differences of view persist in government approaches to the present international economic difficulties. These disagreements arise not only from perceived conflicts of national interests but also from different perceptions of the ability and responsibility of Governments to guide economic affairs, whether nationally or internationally.

73. The need to examine and understand the serious international economic situation in the mid-1980s has brought greater agreement in some important respects. The international debt situation has demonstrated the interaction of trade and finance and the international monetary system as well as the mutuality of interest in overcoming the present disorder.

74. Although no agreement has been reached so far on an agenda for national and international steps to improve the functioning of the world economy and restore stability, growth and development, the multilateral discussions in different forums have in 1985 shown a certain convergence of views in identifying problem areas and analysing the issues.

75. A first area in which further discussions are required is the analysis of the current situation and the likely evolution of the world economy in the years ahead. The issue is not merely to consider how current differences of opinion influence the forecasts; more crucial is to discuss how common interests might best be pursued in an international context and to identify the key policy areas.

76. On the basis of the consultations and the previous analysis, four policy areas seem to deserve particular attention:

(a) If Governments are serious about co-ordinating macro-economic policies among major countries, they must address the lack of consistency in the mix of monetary and fiscal policies of key-currency countries, including the possible need

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for official intervention in exchange markets in order to reduce the excessive misalignments and volatility now prevailing;

(b) A second broad area relates to the functioning of the international monetary system and in particular to the way in which international liquidity is provided. The need for discussion about ways to achieve smooth changes in international liquidity and about the role of SDRs as an international reserve asset remains urgent. Regarding the framework for adjustment, a strengthened surveillance process with more workable forms of conditionality and an improved mix of financing and adjustment seem called for. Given the interrelation among these issues, a case can be made for exploring further the possible contribution, in due course, of an international conference, as proposed by several developed and developing countries, specifying more clearly than has been done so far just what such a conference would add to the present process;

(c) The improvement of the trading system is another area of critical importance. Countries should bring to an early conclusion the unfinished business from the Tokyo Round and should implement the commitments undertaken at the 1982 Ministerial Meeting of GATT and reaffirmed at the sixth session of UNCTAD. Further, efforts should be made to improve and strengthen GATT rules and to bring into its legal framework sectoral arrangements negotiated outside of it. Careful preparation of a new round of multilateral trade negotiations, the agenda and the scope of which must reflect the interests of all countries, should begin soon;

(d) Much more rapid progress towards restoring growth in indebted developing countries is required. Although wide agreement exists on the crucial need for domestic policy reforms and improved domestic management in these countries, there is also a need to seek more imaginative forms of co-operation between public and private flows. For lower-income developing countries that have to rely on official capital flows, a further write-off of foreign debts is important. But also required are definite steps towards a more comprehensive solution. A first step could be taken in intergovernmental dialogue on these matters, taking into account the short-term as well as the medium-term prospects for indebted countries, as well as for creditor countries.

77. The consultations undertaken for the preparation of this report have contributed to the identification of key issues and policy challenges to be addressed at the national and international levels in the near future. Although tending to confirm previously expressed positions in the separate areas covered by the report, they produced a vivid picture of different countries' views of the overall situation and the interrelatedness of the sectoral issues. The consultations also indicated that, in the search for ways and means to meet current problems, it is important not to lose sight of the need to address longer-term systemic problems and improve the effectiveness of international economic co-operation. Reaching agreement on such measures will involve many steps that have to be taken more or less in parallel, for example a new round of multilateral trade negotiations and follow-up of the important proposals on further reform of the international monetary system put forward by the Group of Twenty-four, the Group of Ten, the non-aligned countries, the Commonwealth Secretariat and individual Governments. The consultations also revealed extreme concern about the

international debt problem, which threatens, in the countries particularly affected by it, to become seriously destabilizing and to impede future development. It is clear that, even without a slump in the world economy, the debt problem could recur as an international problem.

78. The multilateral dialogue on the several issues raised in the present report has been gathering momentum in recent months. At the 1985 session of the Economic and Social Council, the function of discussions of international economic issues at the United Nations was given special attention. Many Governments emphasized the usefulness of comprehensive consideration of the different aspects of the world economy within a single framework, taking into account the broad political implications of a failure to improve the functioning of the system and the benefit of taking early notice of future trends and threats to the world economy. Such discussion should not interfere with the mandates and spheres of competence of the specialized agencies but should contribute to greater coherence and a clearer sense of purpose in the management of international interdependence.

79. It was also stressed, however, that such discussions in United Nations bodies require careful preparation and focus if they are to be helpful. The issues to be discussed should be carefully specified so that it is possible to enhance agreement where it seems attainable and to clarify the underlying reasons for disagreement where it does not.

80. The United Nations is a universal forum for discussing these critical issues in a comprehensive manner, which discussion should not conflict with the work of the specialized agencies but instead facilitate it. The discussion should help countries to take a long-term view and to build up support for the implementation of policies required to achieve both sustained growth and development and longer-term reform of the trading, monetary and financial systems.

III. SUMMARY OF CONSULTATIONS

81. The responses from Governments of Member States on the question of expanding international co-operation in the fields of money, finance, debt, trade and resource flows for development, show a broad common theme. All agree that the various problems confronting the international economy in these areas are highly interrelated and that their solution requires concerted action on a number of fronts. Although the groups of countries differ widely on the scope and urgency of action as well as on the proper forums for addressing the issues, all recognize that international co-operation in these fields needs to be strengthened. In the following paragraphs an attempt has been made to summarize the position of the different groups of countries on major issues, focusing mainly on the convergence of views within individual groups but also pointing, where appropriate, to a few areas in which the position of one group has found support in another.

A. Developing countries

82. In their responses, developing countries have emphasized the close linkages that exist in the international economy and the interrelationship among the various issues raised by General Assembly resolution 39/218, in particular among the slow growth of the world economy, the growth of developing countries and questions relating to flow of resources, international trade, the growing debt burden and aspects of the monetary and financial system. While recognizing that some of the problems facing the international economy are of recent origin, developing countries emphasize that these problems are manifestations of structural imbalances and asymmetries in the system. They call for an improvement in the co-ordination of the macro-economic policies of the major developed countries, for a reform of the international monetary system to take into account the changes in economic relations that have taken place since Bretton Woods and for equitable participation in the decision-making process that affects the global economy. Furthermore, developing countries stress that significant progress towards the solution of the problems of international economic co-operation can be made if commitments already undertaken by the international community in various fields are implemented. They want the reform of the international monetary, financial and trading system to start with effective action in areas in which broad consensus and agreed commitments already exist.

83. Developing countries recognize the importance of domestic policies for economic growth as well as for meeting the challenges that face them at present. They accept the necessity for adjusting to changing economic conditions. They feel, however, that domestic action alone is not enough; it is essential that international economic arrangements should create conditions in which such action can be effectively undertaken. Many countries have maintained that in considering the adjustment process in their economies, much greater emphasis must be placed on investment, growth and supply-oriented policies for long-term development than on restraining demand.

1. Flow of resources and debt

84. Developing countries emphasize that a major factor behind the difficulties they face is the lack of an adequate flow of resources on appropriate terms from the developed world. A primary reason for this lack is that little progress has been made towards attainment of the 0.7 per cent target for official develoment assistance (ODA) established in the International Development Strategy. Between 1980 and 1984, ODA increased in real terms at around half the rate of the 1970s. In order to regain the momentum of growth in developing countries, it is essential to make early progress towards attainment of ODA targets, including those of the Substantial New Programme of Action for the 1980s for the Least Developed Countries, and to make ODA available on an assured and predictable basis. A significant part of the foreign-exchange resource requirements of the developing countries must be met from institutional sources. It is therefore urgent that the resource base of the World Bank and of other financial institutions should be expanded. This expansion should include a general capital increase in the World Bank, speedy agreement on the seventh increase in International Development

Association supplementary financing (IDA-7) and replenishment of the International Fund for Agricultural Development. There is also a need for greater flexibility in the provision of ODA, including increased programme lending and balance-of-payments support.

85. While official financial flows have virtually stagnated, funds from other sources have failed to increase. In fact, there has been a net outflow of resources from the developing countries on a scale that is becoming unsustainable. The growth of private bank lending, which was a major source of funds for many developing countries during the 1970s, has declined sharply since 1982 largely as a result of the debt crisis. High rates of interest reduced the attractiveness of bank loans to developing countries. Direct foreign investment in these countries has also not increased significantly. Policies to increase both types of finance for development need to be improved and actively pursued concurrently with measures to increase the flow of official finance.

86. Developing countries are aware of their responsibilities in the solution of the current debt problem. The debt crisis cannot, however, be seen in isolation from other aspects of international economic relationships. The crisis was due largely to circumstances beyond the control of any developing country. A strategy of growth based on external borrowing was well received and advocated by the international community, particularly the developed countries, during the 1970s. The events that touched off and aggravated the problem, including the deepest recession since the 1930s and high interest rates, could not have been foreseen. Macro-economic policies in the developed market economies hold a large share of the responsibility in the evolution of the problem.

87. No solution to the problem of international indebtedness will be possible without an expanding world economy, particularly sustained growth in the developed countries, and a corresponding expansion of international trade. Measures of domestic adjustment alone are wholly inadequate to the task. Developing countries point out that drastic adjustments in their domestic economies have already been undertaken or are under way in a large number of these countries, often at great costs in terms of lowered living standards, rising unemployment, cut-backs in social services and the resulting human suffering. The international environment must be supportive of these efforts. Meanwhile, measures aimed at better crisis management have to be pursued, including stretching out maturities and reducing the cost of debt servicing, in an atmosphere of shared responsibility involving both creditor and debtor countries, both private banks and multilateral institutions.

88. Although the largest concentration of external debt is in the Latin American countries, the problem is not peculiar to that region. The growing debt burden of some low-income and least developed countries has not received the attention it deserves. In some of these countries the absolute level of indebtedness may not be very high, but the capacity for adjustment is low, particularly in some African countries now facing acute economic difficulties brought about largely by exogenous factors.

2. International trade

89. Developing countries emphasize that adequate growth of their exports is essential for more satisfactory growth of their economies as well as for the solution of their debt problem. This condition needs to be fulfilled in the context of overall liberalization of international trade.

90. In the years since the Second World War, a significant degree of trade liberalization has been achieved, permitting, or at least accompanying, an impressive growth in world output. At the same time, the inherent initial difficulties of many developing countries to take advantage of international trade came to be recognized, and the need to accord them preferential treatment has been widely acknowledged.

91. Developing countries point out that in recent years there have been increasingly frequent departures from the principles of non-discrimination and multilateralism in international trade. GATT rules governing international trade have come under severe strain. A large number of sectors are now subjected to bilateral restrictive arrangements such as "voluntary" restraints that especially affect exports from the developing to the developed economies. In many developed countries, quantitative restrictions have been put on export products of interest to developing countries, in particular textiles, clothing, footwear and steel. Agreements governing trade in clothing (for example Multifibre Arrangements), themselves a derogation of GATT rules, are becoming increasingly restrictive.

92. To bring about an orderly expansion of world trade it is essential to take concrete action to strengthen the multilateral trading system, in particular by eliminating discriminatory actions by of the leading trading partners. The conclusion of the multilateral trade negotiations under the Tokyo Round was a major step in the right direction. Developing countries stress that the decisions taken during these negotiations should be speedily implemented and the still unsettled questions resolved. In this regard, they feel it is necessary to implement as soon as possible the current GATT work programme, as called for in the Ministerial Declaration adopted by the Contracting Parties of GATT in November 1982, especially in such areas as safeguards, quantitative restrictions and other non-tariff measures, and trade in agriculture, tropical products, textiles and clothing; it is also necessary to continue and complete work on structural adjustment. A number of developing countries have also called for an end to Multifibre Arrangements in an effort to extend the accepted principles of non-discrimination and multilateralism to a major item of world exports.

93. Developing countries are increasingly concerned about the rising incidence of protection against their exports. They have called the attention of the developed countries to the latter's commitments to free trade and to the provision of special and favourable treatment for developing countries' exports. Specifically, at different forums including the recently held fortieth session of the Contracting Parties of GATT, developing countries have called for a standstill on all protectionist measures against their exports and the beginning of a roll-back of these barriers. Developing countries also feel that little has been done in the industrialized countries by way of structural adjustment which would not only facilitate exports from developing countries but also lead to improved allocation of resources in developed countries.

94. Developing countries also stress the necessity of improving and broadening the Generalized System of Preferences which so far has had only limited success because of its multiplicity of restrictive rules. On the question of special treatment of their trade, they argue that the case for preferential arrangements in their favour remains valid and that reciprocity in trade relations between developed and developing countries, as called for by some countries, is highly inequitable for developing countries.

95. While emphasizing the link between trade and international monetary arrangements, a number of developing countries have pointed out that efforts to curb protectionism in the industrial countries would not produce the desired result without a corresponding effort to avoid the persistent fluctuation and misalignments of exchange rates that give rise to calls for increased protection.

96. A new round of multilateral trade negotiations is being suggested by some countries. In the absence of implementation of commitments already made and given the lack of progress in the current GATT work programme, developing countries have expressed reservations about the usefulness of such new initiatives. Many developing countries have expressed reservations about including services in trade negotiations in the immediate future, proposing parallel but separate negotiations. Some have expressed willingness to participate in a new round provided that it is confined to trade in goods only and priority is given to implementing the Declaration of the 1982 GATT Ministerial Meeting.

97. Developing countries have noted with concern that the prices of primary commodities have remained far below their 1980 levels in spite of the recovery in industrial countries. Given the importance of commodities in the total export earnings of many developing countries, the continuing weakness of these prices has serious implications for the economies of these countries, including their capacity to repay their external debt. In this context, the developing countries stress the need for bringing the Common Fund for Commodities into operation and call for urgent ratification of the Agreement for its establishment.

3. Monetary issues

98. Developing countries have called attention to a number of major aspects of the international monetary system in which reform and improvements are urgently needed as a concomitant to measures in the fields of trade, debt and resource flows for development. These aspects concern the exchange rate régime, international liquidity and SDR allocations, the process of balance-of-payments adjustments, IMF surveillance, IMF conditionality and the adequacy of IMF resources.

99. With regard to the exchange rate régime, most countries noted that, while it was generally expected that the system of floating rates would lead to an increase in the variability of nominal and real exchange rates, it was not expected that these would be as volatile as they had been. Moreover, interest-responsive and speculative capital flows and a lack of co-ordination of economic policies among the major industrial countries have caused exchange rates to become and to remain for some time, out of line with the requirements of basic balance in international

payments, as indicated by competitiveness and other long-term factors. The persistent overshooting and misalignment involve significant costs as, for example, owing to wrong signals and uncertainties, investment decisions are made more difficult, trade frictions are exacerbated and protectionism is encouraged.

100. Developing countries in particular have experienced greater difficulties under the system of floating rates. Their economies are less diversified and frequently lack the necessary institutional arrangements to protect them from volatility and uncertainty. On the other hand, floating rates have also reduced the external discipline on the larger industrialized economies - particularly the major reserve-currency country - making it possible for these countries in effect, to export their problems to the rest of the world.

101. Many countries therefore consider it important to initiate a serious discussion leading to the establishment of an exchange rate system designed to overcome both the recognized rigidities of a fixed par-value system and the destabilizing influences of floating rates. Both fixed and floating rate régimes need rules relative to domestic macro-economic policies. At present, many countries, developing and developed alike, recommend the adoption of target zones supported by official intervention for the major trading currencies, combined with and reinforced by co-ordination of macro-economic policies and firm multilateral surveillance.

102. With respect to adjustment, many countries stress the need for an effective and equitable adjustment process through which countries can adjust their balance-of-payments positions to sustainable levels, consistent with the pursuit of other macro-economic objectives such as growth and stability. This process should be symmetrical in its treatment of all countries - deficit as well as surplus and reserve-currency countries - so that the burdens of adjustment are shared by all.

103. The present system is highly asymmetrical in the sense that it imparts a deflationary bias to the adjustment process of the deficit countries - except for the major reserve-currency country - forcing them to reduce expenditures and absorption, but it does not exert parallel pressures on surplus countries to take expansionary measures. The result is that a disproportionate share of the burden of adjustment is transferred to capital-importing countries.

104. Many developing countries feel that, in considering the adjustment process, much greater emphasis must be placed on growth and supply-oriented structural adjustment, with special attention to fostering investment, production and exports. At present, in these countries' view, neither IMF conditionality nor IMF resources support this approach.

105. Developing countries as well as a number of developed countries consider that IMF surveillance of domestic policies has been too country-specific and that it has concentrated, in effect, on developing countries. They emphasize the need for strengthening surveillance by making it more effective, extending it to the economic policies of all major countries and examining, in particular, the way in which their policies interact with each other and affect the international economy.

106. With respect to the nature and supply of reserve assets and the role of SDR allocations, many countries note that the creation of international liquidity should be effected through truly collective actions, in line with the requirements of an expanding world economy and the special needs of developing countries. The total supply and distribution of international liquidity should not be unduly influenced by any single country or group of countries. Developing countries maintain, and many developed countries agree, that reserves supplied by the financial markets are subject to sharp changes and that many developing countries have little access to such reserves. Moreover, for non-oil-exporting developing countries the level of reserves is inadequate and has been falling. Most developing countries feel that SDRs should be made a major reserve asset, as originally envisaged, and they call for allocation on an annual basis. In the view of the developing countries, the case for establishing a link between the allocation of SDRs and development assistance continues to be strong.

107. Regarding some of the existing IMF operations, developing countries call for the continuance and improvement of such facilities as the Extended Fund Facility, Compensatory Financing Facility and the Buffer Stock Financing Facility, and they emphasize the need for relaxing the conditionality attached to many of the Fund's financing measures. As regards IMF resources, developing countries point out that the increase in quotas adopted under the Eighth Review of Quotas was inadequate. Furthermore, access to quotas was reduced after the quota increase. They urge a major and early increase in quotas under the Ninth General Review, which should be brought forward.

4. International conference

108. The developing countries have strongly urged the convening, under United Nations auspices, of an international conference in the fields of money, finance and trade. They also feel that the meetings of the IMF Interim Committee are too brief for a thorough consideration of all the issues and proposals.

B. Developed market economies

109. The consultations and the several statements of the position of developed market economies in different international forums in recent months have shown that these countries recognize the importance of a coherent approach to the interlinked problems of money, finance, debt and trade. They also recognize the importance of the United Nations and its subsidiary bodies for discussion of economic issues at a political level. They point out that these issues are under continuing consideration at various forums within the United Nations system.

110. None the less, developed countries emphasize that the jurisdiction and competence of specialized bodies to deal with specific aspects of the international economy must also be recognized. They have pointed in particular to the meetings of the Interim Committee and the Development Committee as one such forum and have expressed the hope that the April and October 1985 meetings of the Committees would provide a new opportunity to discuss the various aspects of international economic co-operation, including external indebtedness, flow of resources and trade policies.

111. Concerning the flow of resources, a number of developed countries have, in various forums in recent months, affirmed their commitment to the ODA targets agreed upon, namely the provision of 0.7 per cent of their GNP for the developing countries as a whole and 0.15 per cent of their GNP for the least developed countries. They have urged other developed countries to live up to their commitments to the ODA targets. Many have also expressed disappointment that the results of IDA-7 and the second IFAD replenishment were unsatisfactory. A number of countries are ready to support a general increase in the capital of the World Bank. Most countries have also expressed support for current international efforts to meet the serious situation in Africa, including the Special Africa Facility of the World Bank. At the same time, the developed countries emphasize efficiency in aid utilization through better co-ordination and technical assistance as well as through greater efforts by the less developed countries to mobilize and effectively use their domestic resources.

112. All developed countries agree that a free flow of international trade is essential for the prosperity of the world economy and they are thus in agreement in principle with developing countries anxious to see a significant expansion of their exports. There is nevertheless a widespread recognition of the fact that a resurgence of protectionism in international trade has occurred in recent years, especially in the form of quantitative restrictions. Although all developed countries are parties to GATT, the rules of the Agreement are often violated or circumvented. Wide differences of opinion exist among the countries on the interpretation of GATT rules and on the balance of rights and obligations under them.

113. Regarding the preferential access of developing countries to their markets, many developed countries, while generally accepting the need for such preference, point to the high level of protection that developing countries offer to their own domestic economies. The position of many developed countries appears to be that these barriers must also be lowered, especially in the more advanced developing countries, so that developed countries can have increased access to their markets. In other words, there appears to be a rising call for reciprocity in trade liberalizing measures, in contrast to the position of the developing countries, which maintain that such measures do not have the same effects on the developing as on the developed countries. None the less, there is recognition among developed countries, as among developing, that protective measures hampering international trade need to be rolled back. The question is how to bring this about.

114. A number of developed countries have called for a new round of multilateral trade negotiations in order to further liberalize international trade. Apart from its intrinsic merit, a new round is seen by some of these countries as politically necessary in their efforts to combat the current surge of protectionist sentiments. These countries also feel that such negotiations should cover services as well as trade in goods in a comprehensive manner. At the same time, a number of developed countries have stressed careful preparations for new negotiations and the need for consensus regarding scope and participation.

115. On the question of money, finance and debt the developed countries in general emphasize the importance of sound domestic policies and continuing adjustment

efforts, particularly in the major borrowing countries. Although country positions vary on particular aspects of the agenda to be discussed, the dominant view appears to be that, given what they perceive to be the somewhat brighter prospects for the world economy in the remainder of the decade, debtor countries' persistance in their adjustment efforts is the key to the restoration of their creditworthiness and the resumption of bank lending. Therefore, domestic economic policies are ultimately the major factors in determining market access to and cost of credit for major developing countries. Continuing co-operation between debtor and creditor countries, the IMF/World Bank and the major banks is considered crucial to success. While a global view of the world debt problem is needed, debt restructuring, according to many developed countries, has to be undertaken on a case-by-case basis.

116. At the same time, many developed countries accept that the efforts of the developing countries need to be supported by adequate external finance and trade liberalization. They recognize that many developing countries do not have access to private international capital markets and that they must rely on resources provided essentially through multilateral and bilateral official channels, the medium-term outlook for which is, however, becoming increasingly unclear.

117. On reform of the international monetary system, developed countries in general seem to suggest that the present system has served the international economy well and needs strengthening rather than a major overhaul. The system of floating exchange rates has, according to these countries, worked reasonably well, and a return to fixed parities is impractical at present. Nevertheless, they agree that the system has also shown some weaknesses. It is recognized that a greater degree of exchange stability than has been witnessed so far is desirable, and is to be achieved through close co-operation among the major industrialized countries, the convergence of their economic performance and the strengthening of IMF surveillance. Some developed countries also support the idea of a target zone for exchange rates, which is advocated by many developing countries.

118. On international liquidity, the developed countries in general feel that its supply has been adequate and they fear that excessive liquidity could reignite inflation. The supply of liquidity is now being largely determined by international credit markets and, for an individual country, its availability depends mainly on the country's creditworthiness. According to this view, it will be mainly through the restoration of creditworthiness by means of adjustment measures that many developing countries now facing difficulties can hope to obtain a steady supply of liquidity in the future. The developed countries also recognize, however, that there are countries that do not have sufficient access to international credit markets and that should be provided with adequate official finance while they are making adjustment efforts.

119. The original objective of the creation of special drawing rights was to make the supply of international resources less dependent on the balance of payments of the major reserve-currency country and to make SDRs the principal reserve asset in the long run. The developed countries now feel that changes that have taken place in the international monetary and financial field over the past decade, in particular the increased importance of credit markets, appear to have altered the

role originally envisaged for SDRs. They call for a further examination of the question. Some developed countries, however, see a continuing and important role for SDRs and call for a new allocation of SDRs.

120. In respect of IMF operations, developed countries in general emphasize that the monetary character of the institution must be preserved. They maintain, furthermore, that the conditionality attached to access to IMF resources is essential for promoting adjustment and for ensuring a sound international monetary system. As regards the resource base of the IMF, they feel that the increase in quotas recently effected and the recent extension of its General Arrangements to Borrow are adequate for the immediate future.

C. Centrally planned economies

121. Countries with centrally planned economies in general view the present economic crisis and the difficulties being faced by developing countries as a result of the working of the Western world's economic system, with its unequal relationships among countries. They emphasize the close interrelationships between various current problems, among them the arms race and the huge waste of resources it implies, financial flows, the growing debt burden, stagnant exports, and increasing protectionism in international trade, and they call for a comprehensive approach to these problems.

122. These countries view the existing system of international relations as under the domination of the developed market economies. Some of the latter are said to continue to exert much the same influence over most of the developing countries as during the colonial era, albeit with different means; to practise policies that exploit economic relations as a means of achieving political goals; and to have transferred the burden of the recent global economic and financial crises to other States by depressing commodity prices, shrinking the purchasing power of export revenues as a result of higher import prices, raising interest rates and generally worsening borrowing costs, and draining off profits from the developing countries. Unless all participants in the world economy make a clear commitment to eliminate such policies, the countries with centrally planned economies doubt that a lasting restructuring of global economic relations can be undertaken or that durable gains can be obtained from assisting in the development process.

123. The countries with centrally planned economies are interested, as a matter of principle, in enhancing international relations and they are prepared to expand their trade and other forms of economic co-operation when such relations are mutually advantageous and can be conducted on the basis of an equitable division of labour. In these countries' view, this requires at the outset the acceptance, and full implementation, of a set of basic principles of behaviour in international relations, including non-interference in the internal affairs of other countries, strict respect for the territorial integrity of countries and the inviolability of national frontiers, equality in international life and unconditional recognition of the sovereignty of each State over its natural resources.

124. With reference to the basic issues affecting relations among different groups of countries, the countries with centrally planned economies hold that economic development is primarily the responsibility of the developing countries themselves. None the less, restructured international relations based on the above principles will exert a positive influence on the development process. These countries stress the need to implement the Declaration on the Establishment of a New International Economic Order, the Charter of Economic Rights and Duties of States and the progressive provisions of the International Development Strategy for the Third United Nations Development Decade. They express their support for the role that the United Nations can play in promoting international economic co-operation and enhancing confidence-building measures and thus contributing to the solution of global economic problems. In the same vein, they support the convening of an international conference, under United Nations auspices, to deal with the problems of trade, debt, money and finance. A key objective of such a conference should be the democratization of the existing monetary and financial system on a just and equal basis. A reform of the existing system from within, such as a simple reorganization of the IMF, is held to be an inadequate approach.

125. Countries with centrally planned economies ascribe primary responsibility for the economic backwardness of developing countries to former colonial policies, transnational corporations and the economic policies of dominance practised by some developed market economies. They do not consider themselves obliged to commit part of their resources to financial transfers to the developing countries. Such assistance is seen as a restitution for the wrongs of the past and present and is therefore a moral imperative only for the developed market economies. Nevertheless, the countries with centrally planned economies have been rendering financial and other types of development assistance voluntarily and are prepared to continue such efforts in the future. But they consider strong domestic policy measures in the developing countries and the restructuring of international economic relations along the principles mentioned above to be the primary vehicles for enhancing the development process.

126. Countries with centrally planned economies view with concern the already unsustainable debt burden of developing countries and the outflow of resources from them caused largely by large debt-servicing obligations and a decline in the flow of official financial resources from Western countries. They note that developing countries have to undertake additional borrowing merely to meet the interest costs of accumulated debt and to repay it. The outflow of resources that this entails has created serious social tension as well as economic problems in many developing countries.

127. The problem of debt and resource flow cannot, in the view of these countries, be dealt with in isolation from other aspects of the international economic and political problems, which aspects are closely interlinked. As immediate measures, they propose a combination of debt relief for the least developed countries and debt rescheduling for other developing countries on terms that take into account the capacity of individual countries to pay, including a reduction of interest rates. In addition, they advocate increased access for all developing countries to new sources of credit. As a measure for reducing the outflow of resources from developing countries, they suggest a curb on the tax and other privileges that foreign private investors enjoy in these countries and on the profits they make.

They also call for an increase in the flow of official development assistance from Western countries to developing countries.

128. In the view of countries with centrally planned economies, a large part of the problems faced by developing countries is the result of inequitable trade relationships among nations. They call for the establishment of a fair relationship between the prices of raw materials, food and manufactures. They view with concern the growing protectionism in international trade, which restricts entry of developing countries' exports into the developed market economies. These restrictions need to be removed and trade preferences for developing countries expanded. In addition, countries with centrally planned economies urge Western countries to undertake structural adjustments in their economies, including a reduction of the size of uncompetitive industries.

129. Countries with centrally planned economies point out that the international monetary system has not served the interest of all countries equitably and has failed to perform satisfactorily. Small countries have little access to capital markets which are dominated by the powerful Western countries. The instability of exchange rates has actually increased with the adoption of the system of floating exchange rates, creating further problems in international payments. Countries with centrally planned economies call for a system that reflects the requirements of equitable international relations and the need for greater stability as a pre-condition for maintaining buoyant growth and equitable access to international capital and trade markets.

130. These countries argue that an international monetary system based on one or more domestic currencies as vehicle currencies is inherently unstable and should therefore be dispensed with. In order to attain greater stability and predictability in international monetary affairs, these countries emphasize the need for greater control over the creation of international liquidity in line with the requirements of smoothly functioning and stable international trading and financial relations. They are also in favour of greater regulation of private financial markets that now escape the supervision of Governments or the regulations of the official multilateral financial institutions. They regard the SDR as a useful international currency unit that could replace national currencies as sources of international reserves. They have, however, expressed reservations about the procedures available to guarantee, through the medium of the SDR, greater stability in international liquidity and the value of international reserves. Regarding exchange rates, the countries with centrally planned economies advocate a new system that would allow for stable but flexible exchange rates. They feel that these and other aspects of the international economic system should be discussed in a comprehensive way under United Nations auspices.

D. International organizations

1. International Monetary Fund/World Bank

131. In their responses, the International Monetary Fund and the World Bank drew attention to the April 1985 meetings of the joint IMF/World Bank Development Committee and the Interim Committee and to the documentation prepared for them.

Before the meetings, the IMF had observed that their aim would be to encourage an open dialogue on a wide range of issues relating to adjustment efforts, balance-of-payment prospects and structural and developmental problems in developing countries. The background documentation would cover such subjects as the short- and medium-term outlook for the world economy, developing countries' indebtedness to official creditors and commercial banks, export credit policies, and trade policy issues and developments. The IMF was also preparing documentation on matters related directly to the Fund, such as the considerations governing an allocation of SDRs and possible ways of making IMF surveillance over members' exchange rate policies more effective. The IMF expressed the hope that progress on a number of these issues would be achieved during the meetings, thus enabling subsequent decisions to be taken for strengthening international economic co-operation.

132. The meetings of the two Committees were held from 17 to 19 April 1985. The following paragraphs summarize the communiqués issued at their conclusion.

133. The communiqué of the Interim Committee addressed three main areas: world economic prospects, the debt problem and the international monetary system. Concerning economic prospects, the Committee stressed the need for action, especially by industrial countries, to free world trade, reduce fiscal deficits, improve the functioning of markets and prevent misalignments in exchange rates. On debt, the Committee advocated appropriate adjustment policies by debtors and also adequate new lending and multi-year reschedulings by creditors. In that respect, close collaboration between the Fund and the World Bank for supporting adjustment programmes and financial flows was envisaged. Regarding the international monetary system, the importance of effective Fund surveillance over the policies of all members was emphasized. The Committee could not reach an agreement on the proposal for SDR allocation but agreed to consider the matter at its next meeting. Proposals for the improvement of the international monetary system were under review and would be taken up at its next session.

134. Development Committee addressed mainly the issues of international trade and capital flows. On the first, there was a consensus that proliferation and continuation of non-tariff barriers, especially those applied in a discriminatory fashion, were harmful to the multilateral trading system and impeded the growth prospects of all countries. Consequently, the Committee urged that unfinished business from the 1982 work programmes of GATT should be completed and a new round of trade negotiations be set under way. On the issue of capital flows, the World Bank was encouraged to undertake discussions on a possible increase in its capital base and also on the creation of a multilateral investment guarantee agency to promote investment flows. In addition, it welcomed the Special Facility for Sub-Saharan Africa in support of domestic policy reform and suggested that steps should be taken to enhance the developmental impact of export credits.

2. General Agreement on Tariffs and Trade

135. GATT informed the Secretariat, by making relevant documents available, of the recent efforts to liberalize international trade under GATT auspices, including those reflected in the Ministerial Declaration of November 1982 and decisions taken

at the fortieth session of the Contracting Parties in November 1984. Referring to the need for consistency between international trade, monetary and financing systems and policies emphasized in General Assembly resolution 39/218, GATT also pointed out that it co-operated with the IMF in matters relating to trade and finance, particularly in areas of balance-of-payments restrictions. Recently, a study entitled "Trade policies for a better future: proposals for action", commissioned by GATT and undertaken by a group of independent experts, has been completed and released.

3. The United Nations Conference on Trade and Development

136. UNCTAD emphasized the interdependence of recovery and development on the one hand and growth, changes in productive structures and trade on the other. It called for improvement of the mechanism for transmitting recovery among countries; co-ordinated action in the fields of debt, trade, finance and commodities; policies for short-term recovery that would also contribute to long-term development; vigorous growth in the major developed countries; and removal of the technological, financial and other constraints facing developing countries. A number of specific policy proposals were put forward.

(a) Measures to reduce the burden of official development assistance debt

137. Among the specific measures to reduce the burden of ODA debt, UNCTAD suggested the outright cancellation of the whole or part of existing bilateral ODA debt; the waiving of debt service payment; the provision of cash grants equivalent to the amount of debt relief contemplated; and the adoption of other "equivalent measures".

(b) Measures to decrease protectionism in the field of non-tariff measures

138. UNCTAD drew attention to the proliferation of non-tariff measures in recent years and the lack of overall progress in implementing international commitments to bring about trade liberalization. Some of the actions taken recently had in fact increased discrimination against developing countries' exports. UNCTAD therefore emphasized the need for liberalizing non-tariff measures in order to pave the way for increased exports from developing countries, which could make an important contribution to the solution of the debt crisis; it called for development of modalities for dealing with non-tariff measures in multilateral trade negotiations; and it urged the implementation of commitments made at the sixth session of UNCTAD regarding a standstill on and roll-back of protective measures.

(c) Proposals for a new scheme of compensatory financing

139. A group of experts was convened by UNCTAD recently to study the problem of the instability of export earnings in developing countries. The group concluded that it was necessary to focus efforts on reducing supply instability, the root cause of instability in earnings, and that a scheme of commodity-specific compensatory finance could be designed to deal with the problem. The proposal is to be further studied by an intergovernmental group.

(d) Proposals relating to the least developed countries

140. In view of the serious economic crisis confronting the least developed countries, UNCTAD called for early implementation of the commitments already made by the international community including the ODA target of 0.15 per cent of GNP set down in the Substantial New Programme of Action; the provision of bilateral ODA in grant form; greater flexibility in the form in which assistance is provided; urgent relief measures; immediate financial assistance in the form of debt relief and balance-of-payments support; and policy measures in favour of the least developed countries in such areas as compensatory financing, reduction of trade barriers and transfer and development of technology.

ANNEX

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