

INTWI - ADJ

# Adjustment and Financing in the Developing World

---

The Role of the  
International Monetary Fund

edited by  
TONY KILLICK

*Published by the*

INTERNATIONAL MONETARY FUND

*in association with the*

OVERSEAS DEVELOPMENT INSTITUTE, *London*

Washington, D.C. 1982

TECHNISCHE HOCHSCHULE  
DARMSTADT

Inv.-Nr.:

H 6623

WIRTSCHAFTSPOLITIK  
(W.11)

# Contents

Foreword	v
Acknowledgment	vii
Seminar Papers	viii
Seminar Participants	ix

AN OVERVIEW	<i>Tony Killick and Mary Sutton</i>	1
-------------	-------------------------------------	---

Global Disequilibria and the Non-Oil Developing Countries	2
Summaries of the Seminar Papers	13
Tony Killick and Mary Sutton <i>Disequilibria, Financing, and         Adjustment in Developing Countries</i>	13
Manuel Guitián <i>Economic Management and         International Monetary Fund         Conditionality</i>	16
Daniel M. Schydrowsky <i>Alternative Approaches to Short-Term         Economic Management in Developing         Countries</i>	19
Richard O'Brien <i>Roles of the Euromarket and the         International Monetary Fund in         Financing Developing Countries</i>	21
Bahram Nowzad <i>Some Issues and Questions Regarding         Debt of Developing Countries</i>	22

Brian Tew

*The Position and Prospects of the  
International Monetary System in  
Historical Context* 24

Graham Bird

*Developing Country Interests in  
Proposals for International Monetary  
Reform* 26

Commentary 28

*What actually is the problem?* 29

*The design of adjustment and  
conditionality* 32

*The adequacy of the system* 40

The recycling process 41

Asymmetries and codes of conduct 43

Normative aspects 43

Role of the Fund 44

References 46

*Tables*

1. World Payments Balances on Current Account 3
2. Price and Volume Trends in Merchandise Trade of the Non-Oil Developing Countries 4
3. Contribution of Oil and Other Items to Deficits of Non-Oil Developing Countries 5
4. Current Account Deficits in Relation to Gross Domestic Product, Exports, and Imports, 1980 6
5. Non-Oil Developing Countries: Trends and Projections of External Debt Burden 7
6. Composition of External Debt of Non-Oil Developing Countries 8
7. Trends in Interest Rates Paid by Developing Countries for Euromarket Credits 9

- 8. Trends in Aid Flows 10
- 9. Growth of Per Capita Gross Domestic Product in Non-Oil Developing Countries 12
- 10. Inflation Rates for Consumer Prices 13

## DISEQUILIBRIA, FINANCING, AND ADJUSTMENT

IN DEVELOPING COUNTRIES *Tony Killick and Mary Sutton* 48

## Solutions to Payments Disequilibria:

Financing and Adjustment 49

*Complementarity of financing and adjustment* 49*National objectives versus international adjustment?* 50*Is adjustment feasible?* 54

## Alternative Responses to Disequilibria 57

*Objectives and program types* 57*Conventional responses* 60*New orthodox programs* 62*Structuralist/populist responses* 64*Politics of stabilization programs* 66

Conclusions 68

References 71

## ECONOMIC MANAGEMENT AND INTERNATIONAL

MONETARY FUND CONDITIONALITY *Manuel Guitián* 73

## The Principle of Conditionality 74

*Broad aspects of conditionality* 74*Basis and implications of conditionality* 76

Domestic financial policies 77

External debt management 81

Role of the exchange rate 83

## Recent Developments in Conditionality

Practices 85

*Nature of the adjustment* 86

Need for structural-adjustment 86

Supply management	87
Collaboration with the World Bank	88
<i>The need for financing</i>	89
Scale of Fund assistance	89
The Fund as catalyst	90
Some Issues in the Context of	
Conditionality	91
<i>Policy objectives and the period of</i>	
<i>adjustment</i>	93
Economic activity and growth	93
The rate of inflation	94
The balance of payments	95
<i>Policy instruments and the period of</i>	
<i>adjustment</i>	96
Demand and supply measures	96
Macroeconomic and microeconomic	
variables	97
<i>Assessment and interpretation of</i>	
<i>results</i>	98
Standards of measurement	99
Problem areas and unresolved	
issues	101
References	102
ALTERNATIVE APPROACHES TO SHORT-TERM	
ECONOMIC MANAGEMENT IN DEVELOPING	
COUNTRIES	Daniel M. Schydrowsky 105
Balance of Payments Management	105
<i>Price elasticities in the foreign trade</i>	
<i>of developing countries</i>	108
Price elasticity of export supply	108
Price elasticity of the demand for	
imports	113
Size of nontraded goods sector	115
<i>Policy alternatives for balance of payments</i>	
<i>management</i>	118
Compensatory export bounties	120
Compensated devaluation	121

Domestic tax and price measures	122
Management of Inflation and Price Stabilization	122
<i>Types of inflation</i>	125
Demand-pull inflation	125
Domestic cost-push inflation	126
Exchange rate inflation	127
Spiral inflation	128
<i>Alternative management of inflation and price stabilization: prophylaxis</i>	128
<i>Alternative management of inflation and price stabilization: therapeutics</i>	129
Low-grade inflation	130
Virulent spiral inflation	130
Empirical Applicability of Alternative Management Techniques	132
References	134

*Tables*

1. Effect of Currency Devaluation on  
Relative Prices 114
2. Typical Exchange Rate System of a  
Semi-Industrial Developing  
Country 116
3. Alternative Modifications to the  
Exchange Rate System 123

*Figures*

1. The Supply and Demand Curves of  
Exportables and Importables 107
2. Marginal Costs of Export Products 109

ROLES OF THE EUROMARKET AND THE  
INTERNATIONAL MONETARY FUND IN  
FINANCING DEVELOPING COUNTRIES

*Richard O'Brien* 136

Position of the Banks in 1981 136

Banks and the Fund 143

*The banks* 144

*The Fund* 145

Unequal Access and the Efficiency of Recycling Methods	148
Conclusions	153
References	154

*Tables*

1. Developing Country Borrowing:  
    Syndicated Bank Credits 138
2. Banking Group Exposures in Lending to  
    Developing Countries 141
3. Lending by Arab Banks: Distribution by  
    Borrower 142

SOME ISSUES AND QUESTIONS REGARDING DEBT OF DEVELOPING COUNTRIES	<i>Bahram Nowzad</i>	155
---	----------------------	-----

External Debt as an Important Issue	155
-------------------------------------	-----

*Underlying developments* 157

*New focus on debt issues* 162

Issues for the Future	163
-----------------------	-----

*Supply of financing* 163

*Demand factors* 163

*Mechanism of transfer* 164

*The interest rate issue* 165

*Framework for debt renegotiations* 168

*Tables*

1. Multilateral Debt Renegotiations 156
2. Total External Debt of Developing  
    Countries 158
3. Medium-Term and Long-Term Debt  
    of Developing Countries 159

THE POSITION AND PROSPECTS OF THE INTERNATIONAL MONETARY SYSTEM IN HISTORICAL CONTEXT	<i>Brian Tew</i>	170
---	------------------	-----

Role of the Group of 10	170
-------------------------	-----

*Restrictions on trade and payments* 173

*The Bretton Woods exchange rate  
regime* 175

<i>Floating by the Group of 10 countries</i>	179
<i>Practical monetarism</i>	181
Benign neglect	182
Monetary targets	183
<i>A deflationary bias?</i>	184
Role of the Fund	186
Position of the Non-Oil Developing Countries	192
<i>Recession</i>	192
<i>Inflation</i>	193
<i>The OPEC surplus</i>	193
Role of the Group of 24	195
References	196
<i>Tables</i>	
1. Use of Fund Resources Under Compensatory Financing and Buffer Stock Facilities	188
2. New Loan Commitments to Developing Countries and Other Use of Fund Resources	189
3. Net External Borrowing by Non-Oil Developing Countries	191
4. Non-Oil Developing Countries: Deficits on Current Account	193
DEVELOPING COUNTRY INTERESTS IN PROPOSALS FOR INTERNATIONAL MONETARY REFORM	
	<i>Graham Bird</i> 198
Developing Countries as a Special Case	199
The SDR Link	201
<i>Benefits to developing countries from a link</i>	203
<i>The case for a market-equivalent interest rate</i>	205
<i>The link and market interest rates</i>	206
<i>Different links and developing country preferences</i>	208
Proposed Substitution Account	211
<i>Effect on the SDR</i>	213



<i>Effect on international adjustment</i>	213
<i>Effect on exchange rate stability and global liquidity management</i>	214
<i>Developing countries as holders of reserves</i>	215
<i>Financial arrangements of the account</i>	216
Gold	217
Fund Conditionality	221
A Commodity-Backed International Currency	224
Financial Arrangements Among Developing Countries	227
Some Remaining Issues	228
References	230