CARIBBEAN APPROACH TO INTERNATIONAL MONETARY REFORM

by

Bank of Jamaica

1. INTRODUCTION

During its evolution, the international monetary system has passed through three stages - the gold standard under which gold was the only source of international liquidity, the sterling exchange standard under which sterling provided an additional source of international liquidity and the means for settling international payments deficits, and the dollar exchange standard under which the U.S.$ replaced sterling as the major additional source of international liquidity and as the principal means of settling international payments deficits. The last two stages reflected partial solutions to the problems related to the attainment of adequate international liquidity and to a certain extent enabled the postponement of the adjustment of national domestic prices to international prices through changes in the exchange rate. The duration and peculiarities of a particular stage to some extent reflected the problems and conflicts of reconciling domestic economic objectives and policies with the changing realities of the international economy and the relative economic strength of nations and monetary and trading groups in the pursuit of their objectives. The growth and maintenance of the sterling exchange standard was associated with the economic and financial dominance of the United Kingdom, and the growth of the dollar standard with the rise to economic prominence of the United States. The establishment of the Bretton Woods system in 1944 with its system of par value and the attendant code of conduct for the operation of international economic relations was an attempt to reconcile divergent national economic objectives with the realities of international developments within a framework of international co-operation and consultation. However, certain defects of the system, particularly the peculiar position of the United States dollar and the unwillingness of the major countries to submit to the discipline of exchange rate adjustments, did not enable the system to reconcile divergent national economic objectives with the realities of international economic developments and this has resulted in requests for a reform of the system.

In this paper we shall review briefly the international economic changes which have occurred over the past decade, the impact of these changes on the international monetary system, the issues to be resolved, the decision on these issues as indicated in the Morse Report, the outstanding issues to be resolved and the Caribbean approach to the issues.

2. Brief ....

REGIONAL MONETARY STUDIES CONFERENCE, 1974

2. BRIEF REVIEW OF INTERNATIONAL ECONOMIC CHANGES

During the past decade there have been shifts in international political and economic power and consequently in the conduct of international relations.

In the non-communist world the overwhelming political and economic dominance of the United States had been somewhat reduced by the growth of the European Economic Community and the rise to economic prominence of Japan. The enlargement of the EEC to include the United Kingdom and some of her EFTA partners had strengthened this bloc and accelerated the movement toward the creation of two rival monetary and trading areas, the European Economic Community and the United States.

The gradual weakening of the Commonwealth trading pattern with its system of Commonwealth preferences and its network of monetary and foreign exchange arrangements of which London is the center posed certain problems for the countries involved. Many of the countries, particularly those of the Commonwealth Caribbean, though direct participants in the Bretton Woods system, had continued to operate on the sterling exchange standard while increasing the proportion of their trade with non-Commonwealth countries, particularly the United States of America. Should they become part of the enlarged EEC group with its distinct divisions into developed industrial countries and countries providing primary commodities or should they deepen and strengthen economic relationships with other developing countries with similar problems?

3. IMPACT ON THE INTERNATIONAL MONETARY SYSTEM

The growth of the European Economic Community and Japan during the fifties and sixties not only took place within an environment of expanding international trade but to a large extent contributed to this expansion. However, alongside the expansion of international trade there were two developments which should be emphasized. The first was the wide variations in the rates of growth of costs and prices in the various countries and the divergent policies in the management of their economies which contributed to the emergence of fundamental disequilibria in the balance of payments of the major countries. The second was the rising importance of manufactured goods in total trade resulting from the increasing use of new technology and the worsening of the terms of trade against the primary producing countries during the late fifties and sixties.

The large increase in the volume of international transactions required an increase in the volume of international reserves needed to finance those transactions. The supply of newly mined gold and the use of International Monetary Fund facilities met only a portion of the demand for reserves to finance this increase in international transactions and most of the additional reserves was provided by countries' holdings of other reserve currencies primarily dollars, during the sixties. The latter involved large and continuous balance of payments deficits on the part of the United States and acceptance and retention by countries with balance of payments surpluses of a large proportion of U.S. dollars. This meant that these countries were postponing their use of goods and services and were enabling the United States to pursue policies some of which were not acceptable to them. At the same time, this method of increasing international liquidity that is, through continuous balance of payments deficits of the major reserve currencies violated the keystone of the Bretton Woods System, that countries experiencing fundamental disequilibrium should adjust their exchange rates.

4. PRESSURES FOR REFORM OF THE INTERNATIONAL MONETARY SYSTEM

The dissatisfaction with the system , (because of the reluctance of countries to change their exchange rates) did not encourage prompt balance of payments adjustment through movements in the exchange rate, but left the creation of the major portion of international reserves to persistent balance of payments disequilibrium and led to pressures for reform of the system. The creation of the facility for special drawing rights (SDRs) in 1969 was an important step on the road to reform. It provided an international reserve asset which would be subject to conscious collective control to complement gold and at the same time reduce the excessive accumulation of reserve currencies. However, while the creation of the SDRs offered a partial solution to the liquidity problem, the problem of exchange rate adjustment remained. Because of the unique position of the U.S. dollar in the international monetary system - the currency of the largest economy in the international system, the principal reserve currency and the main intervention currency - it was difficult in practice to change the exchange rate of the United States dollar in terms of other currencies. The suspension of the convertibility of the dollar into gold in August 1971 removed the means through which the United States could fulfill its various exchange stability

/ obligations ....

obligations. It also paved the way for the realignment of the world's major currencies during the Smithsonian Agreement in December 1971. Despite the realignment and the floating of the pound sterling in June 1972, and a further de facto realignment upon the devaluation of the United States dollar in February 1973 there have been recurring monetary crises with disruptive effects on international trade and capital movements.

The Commonwealth Caribbean countries were particularly vulnerable to the recurring crises. Prior to the realignment in December 1971, the Commonwealth Caribbean countries maintained the same exchange rate with the pound sterling and operated what was in effect a sterling exchange standard. Balance of payments deficits between the member countries were settled on a quarterly basis in sterling in accounts held with the Bank of England by the monetary authorities of the various countries. Balance of Payments deficits between the countries of the Caribbean Commonwealth and the rest of the world were settled through sterling from accounts held in London. The devaluation of the Guyana dollar in December 1971 led to a change in the exchange rates between the Guyana dollar and the other currencies of the region but as all the countries continued to maintain a fixed relationship with sterling (the intervention currency of the member countries), fixed relative values for all currencies of the region were automatically maintained. The devaluation of the Jamaican dollar in January 1973 and the decision to continue the same relationship with the U.S. dollar when it was devalued in February 1973 and to choose the U.S. dollar as the intervention currency not only changed the exchange rate relationships but introduced an element of exchange rate instability between a floating pound and the U.S. dollar. This introduced an element of uncertainty regarding exchange rates and consequently uncertainty with respect to inter-regional trade and investment. Banking and foreign exchange operations become more complex, particularly in the absence of facilities for hedging on receipts and payments for trade and capital transactions in the area. However, it should also be acknowledged that the changes in relative exchange rates reflected changes in domestic prices and costs of some of the member countries and to that extent contributed to the more efficient functioning of the adjustment process. A system allowing narrower exchange margins within Commonwealth Caribbean countries than between members and non-member countries would constitute a further improvement.

In the light of the dissatisfaction with the working of the international monetary system and the growing pressures for reform a Committee of Twenty representing the entire membership of the IMF was appointed in August 1972 to submit concrete proposals for the reform of the international monetary system.

5. ISSUES TO BE RESOLVED

The main issues to be resolved were:-

(i) arrangements for exchange rate adjustment including details of a reserve indicator structure and procedures for a multi-currency intervention system;

(ii) the establishment of a mechanism for the creation of a suitable volume of international liquidity and the determination of the composition and importance of the various international reserve assets;

(iii) the problem of convertibility of the reserve currencies and the consolidation and management of currency reserves;

(iv) the transfer of real resources from developed to developing countries through the international monetary mechanism.

(i) THE ADJUSTMENT PROCESS

The problem was to ensure that balance of payments adjustments for both surplus and deficit countries should take place promptly and smoothly without impeding the free flow of trade and capital. Solutions were sought to the problem of finding suitable indicators to signal the need for corrective action and the appropriate procedures for inducing such action. In this regard two main alternatives were proposed. Under the first, United States sponsored alternative, countries would be expected to take corrective action if their reserves rose or fell below specified indicator points and remained there for a specified period of time unless there was a contrary movement in the country's basic balance of payments or unless the IMF Executive Board decided on other grounds that such action was unwarranted. Under the second alternative, supported by most European countries, the main reliance for inducing corrective action would be based on assessment by the IMF of the movements of the country's reserves and its basic balance of payments.

(ii) International ... ..

(ii) INTERNATIONAL LIQUIDITY AND THE COMPOSITION AND IMPORTANCE OF RESERVE ASSETS

While it was agreed that the Executive Board of the IMF would continue to make decisions regarding international liquidity it was recognised that there was need for appropriate procedures for the determination of global reserve needs and for decision making on SDR allocation, cancellation and its use in international transactions.

Having accepted the need to reduce the proportion of the national reserve currencies in world reserves it became necessary to determine the roles and importance of the two remaining sources of world reserves - reserves with the IMF, mainly the SDR, and gold. In addition to the problem of the general acceptance of the SDR as the principal reserve asset there were certain features of the SDR - the limitation and reconstitution requirements and the low rate of interest payable on SDRs - which would require modification if the role of the SDR was to be expanded, while certain procedures regarding the use of gold would have to be established.

(iii) CONVERTIBILITY, CONSOLIDATION AND THE MANAGEMENT OF CURRENCY RESERVES

The issue of convertibility revolves around the need to convert national currencies into some internationally acceptable asset for the settlement of claims among various countries. The suspension of dollar convertibility into gold in August 1971 left the way open for the choice of another primary reserve asset (SDRs) to replace gold as the asset in which international claims could be settled. But certain questions had first to be solved. What was to be done with the outstanding stock of dollars? Should countries whose currencies are held in official reserves, for example, the United Kingdom and the United States be compelled to convert their currencies into a primary reserve asset, or mandatory settlement of assets as it is called, or should such official balances be converted into primary reserve assets only to the extent that other countries required them to do. Further, should settlement include the large outstanding balances of reserve currencies, or should they be restricted to new accumulations? Once these issues were settled, the problem of the mechanism for settlements would have to be faced. Should there be direct settlement between countries or should it be wholly or partly centralized in the International Monetary Fund? The latter would involve the establishment

of a substitution facility within the IMF into which countries with balance of payments deficits would transfer reserve assets while countries with balance of payments surpluses would receive SDRs.

The growth of these official balances would have implications for the volume of international liquidity, and steps would have to be taken to ensure that currency reserves be managed in such a manner as to avoid undesirable changes in the volume of international liquidity.

(iv) THE TRANSFER OF REAL RESOURCES FROM DEVELOPED TO DEVELOPING COUNTRIES

During the past decade the flow of financial aid from developed to developing countries has been much slower than that needed to meet the requirements of the developing countries or the targets suggested by certain international bodies. It was,therefore,proposed that the supply of development resources be supplemented by the establishment of a link between the allocation of international reserve assets, primarily SDRs, and the provision of resources to finance development. The establishment of a new facility to provide long-term balance of payments finance for developing countries was also proposed.

The main issue facing the link proposal was whether the use of the SDR as a means of providing development finance would weaken confidence in the SDR and inhibit its development as the principal reserve asset of the international monetary system. Subsidiary issues involved the allocation of SDRs and the establishment of appropriate mechanisms for the transfer of resources to the developing countries.

6. RECOMMENDATIONS OF THE COMMITTEE OF TWENTY

At the annual meeting of the IMF held in Nairobi in September 1973, the first outline of reform was submitted to the IMF Board of Governors, outlining the issues on which broad agreement had been reached, and the outstanding issues to be resolved or on which further work was required.

In addition to agreement on technical issues discussed below, it was envisaged that a consultative body at an appropriate level would be established to survey the world payments situation "in relation both to the general working of the adjustment process and to developments affecting global liquidity", including a review of the aggregate flow of real resources to developing countries and its financing.

(i) The ....

(I) THE ADJUSTMENT PROCESS

(a) Issues on which agreement has been reached.

The need for a more timely and effective balance of payments mechanism was agreed upon. Adjustment action may be either domestic or external and would be based on reserve limits agreed on from time to time in the Fund. The choice of the adjustment method would be left to the individual country but countries would be expected to take into consideration repercussions on other countries as well as the internal effects.

Particular cases of imbalances with significant international repercussion would be examined by the consultative body. A country could become subject to such examination if "there had been a disproportionate movement in its official reserves" or in the judgment of the Managing Director of the IMF the country was facing significant imbalance, even though this was not indicated by a disproportionate movement in its official reserves.

In order to prod member countries where necessary to implement the necessary policies, provisions will be made for graduated pressures to be applied to both surplus and deficit countries.

External adjustment through exchange rate changes will continue to be a matter of "international concern and consultation", and "competitive depreciation or undervaluation will be avoided". The exchange rate mechanism will continue to be based on the old par value system and will entail a system of stable but adjustable rates. Countries will be expected to continue to maintain market rates for their currencies, including the intervention currencies, within 2¼ per cent of either side of parity. However, recognising that there could be extenuating circumstances which may prevent a country from selecting the appropriate exchange rate consistent with equilibrium in the medium term it was agreed that countries should be allowed to float in particular situations, subject to IMF authorization, surveillance, and review.

There will be a strong presumption against the use of controls on current and capital account transactions and countries will not be allowed to "use controls over capital transactions for the purpose of maintaining inappropriate exchange rates, or more generally, of avoiding appropriate adjustment action" .... "Wherever possible, developing countries will be

exempted from controls imposed by other countries, particularly from import controls and controls over outward long term investment".

Countries will be expected to co operate in adopting measures, such as the harmonization of monetary policies, to limit and, where necessary, finance and offset disruptive capital flows.

(b) <u>Issues outstanding</u>

The main outstanding issues relating to the adjustment process are the use of objective indicators to trigger off adjustment consultation and assessment within the IMF, the types of pressures to be used against countries with large and persistent imbalances, rules for floating and multi-currency intervention.

(ii) <u>International liquidity and the Composition and Importance of reserve assets</u>

It has been agreed that the Executive Board of the IMF would continue to make decisions regarding the appropriate volume of international liquidity.

The SDR will become the principal reserve asset, and the role of gold and reserve currencies will be reduced. The SDR will also be the numeraire in terms of which par values will be expressed. The amount of SDRs allocated and the timing of the allocations will be in accordance with international liquidity needs.

(b) <u>Issues Outstanding</u>

The main outstanding issues are the establishment of appropriate procedures for the determination of global reserve needs and for decision-making on the SDR, methods for reducing the constraints on the use of the SDR so as to encourage its use, and appropriate arrangements for gold in the light of the decision to reduce its use and importance as a primary reserve asset.

The two critical issues on which an increasing role for SDR hinges are its valuation and the determination of its yield. A decision on the valuation of the SDR would have to be guided by two main points:-

(i) the effective yield on the SDR should be sufficiently high to make it attractive to acquire;

(ii) the effective yield should not be so high as to make countries reluctant to use it when in deficit.

/.....

Three proposals have been under consideration

(a) "that the value of the SDR in transactions against currencies should be maintained equal to the average of a group of currencies and that the SDR should carry an average market interest rate;"

(b) "that the value of the SDR in transactions against currencies should be maintained equal to an average of a group of strong currencies and that the SDR should carry an interest rate lower than an average market interest rate;"

(c) "that the value of the SDR in transactions against currencies should be maintained by the balance of revaluations and devaluations of currencies in general and that the SDR should carry a low or zero rate of interest;"

As an interim measure it has been decided to use the "standard basket" approach until a more lasting situation can be agreed upon. Under this approach the transactions value of the SDR would be equal to that of a basket of currencies calculated on the basis of the prevailing spot rates of the currencies included and their amounts in the "basket" would be determined by the IMF.

The suggestions for the relaxation of constraints on the use of the SDR include:-

1) the abolition of the existing limits on acceptance obligations and the reconstitution obligation.

2) some relaxation of the requirement of need for the use of the SDR.

3) modification of the provision on opting out of decisions to allocate SDRs.

4) the authority for countries to engage in SDR transactions without being required to do so by the Fund.

5) the authority for SDRs to be used in payments into or from the General Account of the Fund for all types of operations and transactions now conducted in gold or currencies.

6) the authorization for the Fund to expand the list of institutions authorised to hold and use SDRs and to permit additional types of operations and transactions in SDRs.

Three proposals have been submitted with respect to gold. One proposal would enable monetary authorities, including the Fund, to undertake

official price of gold would be abolished and monetary authorities would be free to undertake transactions in gold with each other at the market price and also to sell gold in the market. A third proposal extends the second suggestion to include the purchase of gold in the market.

(iii) Convertibility, Consolidation and the Management of Currency Reserves

(a) Issues on which agreement have been reached

Agreement on the need for consolidation has been reached. All countries maintaining par values will settle in reserve assets official balances of their currencies presented to them for conversion. The aggregate volume of official currency holding will be kept under international surveillance and management so as to relate the growth of international liquidity with the growth of international transactions.

However, while the need for co-operation in the management of reserve currencies has been recognised no decision has been reached on the method for achieving this objective.

(b) Issues outstanding

The two main suggestions regarding the mechanism for the consolidation of existing balances are, that such balances should be settled on a bilateral basis, and/or that such balances should be centralized in the form of SDRs through a facility in the Fund on the basis of terms to be negotiated. Future balances could be exchanged for SDRs through a substitution facility established in the Fund under appropriate rules. A decision regarding the allocation to currency issuers of profits or losses arising from the operation of the facility would have to be made.

Regarding the management of currency reserves the main proposals are:-

(i) that countries whose currencies are held in official reserves should be able to require other countries to limit or convert into other reserve assets further increases in other countries' holdings of their currencies;

(ii) that after prior consultation with the Fund countries should periodically choose the composition of their currency reserves;

(iii) that countries should not switch around their reserves in such a manner that they increase their holdings of a currency held outside the country of issue except within limits agreed with the Fund.

The ......

(iv) The Transfer of Real Resources from Developed to Developing Countries

(a) Issues on which agreement has been reached

Unlike the other aspects of reform there appears to be as yet no agreement on this subject. The first outline of reform states that ..... "the reformed monetary system will contain arrangements to promote an increasing flow of real resources from the developed to developing countries," and that if these arrangements were to include a link between development assistance and SDR allocation it could take certain forms.

(b) Outstanding issues

There are two main types of link proposed. Both proposals emphasize that the total volume of SDR allocation would be determined exclusively on the basis of global liquidity needs. One version of the link would distribute directly to developing countries a larger proportion of SDR allocations than they would receive on the basis of their share in Fund quotas, with the distribution favouring the least developed countries. Another verison would distribute directly to international and regional development finance institutions a predetermined share of SDR allocations. Those institutions in turn would channel the link resources to developing countries on the basis of development need and in such a manner as to be relatively favourable to the least developed countries.

7. A CARIBBEAN APPROACH TO THE ISSUES

(i) The adjustment process

As explained earlier, the Commonwealth Caribbean countries had in the past adjusted their exchange rates automatically with changes in the pound sterling, without adequate examination of the effects on their own economies. More recently Guyana and Jamaica have broken this relationship and have introduced changes independently of the movements in pound sterling.

While movements in reserves could be interpreted as a reflection of underlying economic factors, such movements may be due to temporary or cyclical factors and may not require responsive adjustment action. Therefore, it would be in the interest of the Caribbean countries to support a proposal which would include other indicators but which would place the main reliance on an assessment of the country's economy by the IMF.

Whether adjustment action is domestic or external has been left to

would have to consider the response of institutional factors to the specific type of change contemplated. However, because of the existence of CARICOM, both domestic and external policies would have to be carefully harmonized to avoid disruptive effects on the economies of individual member countries. This does not mean that there should not be periodic changes in the external adjustment mechanism (the exchange rate) or in domestic monetary and fiscal policies to reflect different rates of changes in internal prices and costs, particularly in the absence of complete factor mobility.

The Caribbean countries should have no difficulty supporting the system of fixed but adjustable exchange rates based on par values. Such stability in exchange rate relationship should facilitate trade and capital movements within the region while enabling periodic adjustments to reflect changes in internal costs and prices.

Proposals for both financial and non-financial pressures to be applied to countries with persistent payment imbalances should be acceptable to the Commonwealth Caribbean countries. Proposals for financial pressures range from penalty rates of interest on net creditor or net debtor positions in the Fund to loss of the right to convert further increases of currency balances into primary reserve assets and to deposit such increases with the Fund at progressively increasing negative interest rates. Proposals for non-financial pressures include publication of a Fund report on the position of the country and trade and other restrictions against countries with persistent large surpluses.

In view of the disruptive effects of floating exchange rates on the economies of the Commonwealth Caribbean countries it is in their interest to support the principle of the establishment of a code of conduct and rules for floating until the system of stable but adjustable parities is re-established.

(ii) International liquidity and the composition and importance of reserve assets

The Commonwealth Caribbean countries should be in agreement with the decision to make the SDR the principal reserve asset and to reduce the role of gold and the reserve currencies and to make the SDR the numeraire in terms of which par values will be expressed.

The issue involving the valuation of the SDR is not clear cut. The Caribbean countries have been net users of SDRs and should be hesitant to support a proposal for a relatively high effective yield on the SDR. At the same time they should recognise that the effective yield should be sufficiently high to make it attractive for other countries to acquire SDRs. The proposal that the value of the SDR be maintained by the balance of revaluations and devaluations

/ .../

of currencies in general and that the SDR carry a low or zero rate of interest should be attractive to the Commonwealth Caribbean countries because the value of SDRs would then tend to be stable and the cost to them of the use of SDRs would be relatively low. The second best alternative from their viewpoint would be the proposal that the value of the SDR be maintained equal to the average group of strong currencies and that the interest rate on the SDR be lower than the average market interest rate. On the assumption of an appreciation of 2 per cent in the average value of the group of strong currencies, a minimal interest rate of 3 per cent would give an effective yield of 5 per cent to the SDR which would be lower than market rates but sufficiently high to make it attractive for other countries to acquire.

With respect to gold, the Caribbean countries should not support any proposal involving an increase in the price of gold. Such a measure will not be an equitable or lasting solution to the provision of international liquidity as it would hinder the development of the SDR as the principal reserve asset. The Caribbean countries should therefore support the proposal enabling monetary authorities, including the Fund, to buy and sell gold to each other at the official price, and sell but not buy gold in the market at the market price.

(iii) <u>Convertibility, Consolidation and the Management of Currency Reserves</u>

Most of the reserves of the Commonwealth Caribbean countries are held in sterling (one of the reserve currencies). The exact proportion varies from country to country but the requirement under the sterling area agreement ranges from 50-per cent. These countries derive a relatively good return on such reserves and any arrangement involving consolidation of sterling for a lower yielding asset would reduce their incomes derived from foreign exchange investments. In view of the conflicting objectives of a lower than market yield for the SDR on the one hand and a maximum yield on foreign exchange investments on the other, the Caribbean countries should put forward a proposal enabling developing countries to hold a certain proportion of their official reserves in reserve currencies. This would not necessarily imply a continuation of the present system of holding reserves in sterling because if the sterling guarantee is rescinded, the yield from sterling investments might be less attractive because of the exchange risk.

Allowing for this modification, the Commonwealth Caribbean countries could support the suggestion requiring the consolidation of existing balances in the form of SDRs through a facility in the Fund. Additional balances could then be exchanged for SDRs through the [illegible]

With respect to the management of currency reserves the proposal that after prior consultation with the Fund countries should periodically choose the composition of their currency reserves should enable the Caribbean countries some flexibility in the management of their reserves.

(iv) <u>The Transfer of Real Resources from Developed to Developing Countries</u>

There are currently three proposals for the transfer of real resources from developed and some oil exporting developing countries to developing countries, all of which would benefit the Commonwealth Caribbean countries. The first proposal would establish a link between SDR allocation and development finance. The interests of the Commonwealth Caribbean countries would be best served by supporting the proposal for a direct allocation of SDRs to developing countries in larger amounts than their corresponding share in Fund quotas. This would enable the countries to have somewhat more control over the disbursement of the funds than would be possible under the second version of the link whereby allocations would be made directly to development finance institutions for on-lending to developing countries. However, this issue involves the whole set of procedures concerning the establishment of quotas and the decision-making process regarding the allocation and cancellation of SDRs. It is hoped that these issues would be reviewed and resolved by the Council of Governors of the Fund who will be expected to continue the work of the Committee of Twenty.

The second proposal would establish a facility in the Fund for the purpose of providing resources to developing countries for a longer period than presently existing under the present system of stand-by arrangements. These resources would be used to support a comprehensive stabilization programme covering a span of three or more years and would be associated with comprehensive policy measures for the correction of balance of payments imbalances. This type of assistance would enable Commonwealth Caribbean countries with structural problems to undertake reforms under the aegis of a longer-term programme with resources which would carry a relatively low rate of interest.

The third proposal is for the establishment of a temporary supplementary credit facility (the oil facility under the Witteveen Plan) in the IMF to aid member countries in their payment problems arising from the steep increase in oil prices. The new lending operation is to be financed from the Fund's existing currency holdings and from funds borrowed from oil-exporting countries and other countries which have not been seriously affected by the oil crisis. Member countries will be

permitted to borrow from this source to finance a portion of their deficit arising from higher oil prices and the amount obtainable will be related to the size of their reserves and to their Fund quotas. The funds will be made available for up to seven years with a three-year grace period before the commencement of repayment.

All of the Commonwealth Caribbean countries with the exception of Trinidad and Tobago would be adversely affected by the increase in oil prices. It is estimated that to maintain the 1973 level of oil imports in 1974, the additional costs would require an increase in the use of foreign exchange reserves varying from U.S$13 million for Barbados to U.S.$100 million for Jamaica. In the longer-run price and other adjustments in the goods and services accounts of the individual countries would mitigate the effect on reserves of the increase in the price of petroleum and petroleum products but in the short run the non-oil producing countries of the Commonwealth Caribbean would have to utilize the IMF oil facility if serious economic dislocations are to be averted. For Trinidad, the problem would be to reduce the inflationary effects arising from the inflow of foreign exchange from oil revenues. The question of whether the existing exchange rate is appropriate under the changed conditions should also be examined.

Other arrangements for co-operation - the international payment arrangements and special oil facility for members of the area to be provided by Trinidad - between the Commonwealth Caribbean countries are presently being pursued but these are outside the scope of the issues of international monetary reform.

BANK OF JAMAICA
3rd May, 1974.

B I B L I O G R A P H Y

I. M. F: ANNUAL REPORTS 1965 - 1973

: REFORM OF THE INTERNATIONAL MONETARY SYSTEM -
A Report by the Executive Directors to the Board of Governors (I. M. F. Washington, D.C. 1972).

: Executive Board Papers (Unpublished)

: Survey - 8th October, 1973 (Annual Meetings Issue)

"THE INTERNATIONAL MONETARY SYSTEM: A SYMPOSIUM".

Journal of International Economics Volume II, No. IV
September 1972

(North - Holland Publishing Company, Amsterdam 1972).