

Gold, The International Monetary Fund and the Third World

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The aim of the Third World in reforming the IMF should be to make it a factor that promotes its autonomy rather than its continued dependence, argues Leelananda de Silva, a Senior Assistant Secretary of the Ministry of Planning and Economic Affairs from 1970 to 1977 and now Third World Forum representative of the International Foundation for Development Alternatives based in Geneva. He emphasises in this paper that the IMF has to be more concerned with Third World priorities such as the provision of basic needs and increased economic co-operation within Third World countries and to this end the Third World should *make use* of the IMF gold stock worth US \$ 24 billion at present prices. Rather than agree to its gradual erosion, the Third World should *make use* of the IMF gold stock (1) to create a basic needs facility to provide funds to countries prepared to channel funds for the relief of absolute poverty, and (2) to provide 100 percent gold cover to a new currency unit to promote economic transactions within the Third World.

There is an important school of thought which ascribes the shortcomings of the IMF to the rejection of the Keynes proposals at Bretton Woods. The acceptance of the Keynes proposals would doubtless have improved the prospects of the debtor countries and introduced a greater symmetry in the adjustment process. But that would not have made the IMF a more appropriate institution for the present concerns of the Third World. In seeking a new orientation within the IMF the Third World should not demand a return to Keynes and the enlargement of the credit lines within the present system of rules. What it needs is a qualitative improvement of the IMF system which only would enable the Third World to be an increasingly autonomous rather than an increasingly dependent factor in the World economy. The IMF might do no worse than to examine Third World concerns and priorities and assess its own capacity and scope for greater flexibility in meeting those needs.

Basic needs are now accorded very high priority among the objectives of development efforts, both at national and international level. This would continue to be so for the rest of this century as the elimination of absolute poverty provides the most urgent and practical area for co-operative action of both North and South. The implications for donor countries and international agencies in the adoption of a basic needs strategy have been the subject of considerable study. It is in this

context somewhat surprising that inadequate attention has so far been focussed on the future impact of IMF policies on the provision of basic human needs in Third World countries.

Third World Priorities

It needs in fact to be argued that the concern should even be broader, encompassing not only basic needs but the direction of IMF policies in relation to concepts such as greater self-reliance, technology issues and greater trade within the Third World. Collective self-reliance is an accepted axiom of international policy and the extent to which the IMF is even implicitly committed to this principle needs analysis. It is possible that such an analysis would indicate that the present policies of the IMF work in a contrary direction. Criticism of the IMF and its policy prescriptions is not uncommon. IMF policies are attributed as a cause in the rise and fall of governments, civil commotion and such other traumatic experiences with the possible exception of natural calamities. There is no doubt that IMF policies call for less state intervention in national economies and therefore for less public expenditures, less taxes on the investing classes and generally, for the free and unregulated operation of market forces. Price "distortions" are anathema to the IMF and welfare expenditures, e.g. food subsidies, are not the most favoured instruments of government policy in the IMF rule book. Mr. Witteveen as Managing Director

of the Fund made the point that "the Fund avoids taking a view on the appropriate distribution of the burden of adjustment as between various sections of society.¹ Though as a statement of the formal position it is true, the IMF's proposals for remedial action leave little choice for governments in determining the incidence of their impact.

A distinction has to be drawn between the social welfare expenditures of governments and those that are directed towards the alleviation of absolute poverty. The consequences of a cutback in welfare expenditure conditioned on IMF credits need not necessarily be to the detriment of basic human needs. But a proper question at a time when there is general acceptance of the validity of a basic human needs strategy is whether there is no positive obligation on the part of IMF to ensure that basic human needs are not adversely affected as a result of the implementation of its recommendations. The IMF would have to be more concerned with the structure of growth rates rather than with their mere magnitude.

The IMF conditionality has been a critical factor in the Organization's relationships with member-countries. There are those who argue against stipulation of any conditions as impinging on the sovereignty of nation-states. There are others who see no objection to conditionality clauses provided they are the right ones from their own particular angle. The provision of basic human needs as a central objective of development would probably qualify for incorporation as an "appropriate" conditionality clause from most points of view. It could therefore be for the IMF to monitor the impact of its prescriptions on the achievement of basic human needs.

Since the comparatively recent expression of universal concern on environmental issues, agencies like the IBRD tend to build into their projects safeguard elements to prevent abuses of the environment. Similarly, the provision of basic human needs in the Third World could be ensured only if progress in that direction is not retarded at frequent intervals due to constant changes in economic policy. Basic human needs have to be looked upon as a first claim on the resources of

both the national and the international community. The IMF has an overriding obligation in view of its tremendous political and financial leverage, particularly in those countries which could do very much more to provide for the basic needs of their peoples, if their efforts at economic growth were tempered with a greater concern for the re-distributive aspects of that growth.

The IMF remit (and also that of GATT) is such that its primary concern is with the external sector of Third World economies—exports and imports, consumption of imported and exportable goods, the level of external debt, private foreign investment and commercial bank credit, and the general health of the balance of payments. The IMF concern in domestic economic management is essentially geared to improvements in these and related directions based on an appropriate range of indicators. Financial probity and paying one's way in the world are supreme objectives of the IMF mandate. It is this excessive concern with rates of economic growth and balance in foreign exchanges, and its relative unconcern with the worst aspects of poverty within the Third World that makes one question the IMF's interest in basic human needs. The external sector of most Third World economies is still of the 'enclave' type, more closely integrated with the international economy rather than with its own domestic economy. An important task for the external sector of these economies is to strengthen their backward linkages rather than the IMF's implied emphasis on forward linkages. An export-oriented strategy is not necessarily detrimental to Basic Human Needs strategies in poor countries provided the benefit of value accruals remains within these countries and mechanisms are established for the wider distribution of such values—through greater labour intensity, more appropriate forms of technology and so on. The IMF's concern with greater access to markets for increased exports of Third World countries could be reconciled with such strategies if the IMF were to provide more opportunities for trade within the Third World. The Compensatory Financing Facility is too limited in scope to provide for some of these

structural changes in export regimes required in the foreign trade of Third World countries, and the IMF could think in terms of new facilities to promote such changes within the overall IMF objectives of trade creation. Economic Cooperation among Developing Countries (ECDC) is not a concept for UNCTAD only, and its realization depends on financial institutions like the IMF.

The foregoing considerations assume even increased validity in the light of the IMF's growing emergence as an international central bank.² Its task is no longer confined to the supervision of a fixed exchange rate regime. It is concerned with international economic management and the "firm surveillance" of economies of member countries and the onus is now cast on these countries for regular consultations. Over and above the traditional credit tranches the IMF has now an array of instruments for recycling of financial surpluses, swap arrangements like the General Agreements to Borrow, and informal consultative systems with a network of the most powerful banking institutions in the world. It is therefore right and proper that the IMF moves also in the direction of working with the Third World countries in their own particular concerns on issues like increased intra-trade within the Third World, the creation of jobs for the massive unemployed labour forces and so on. The Trust Fund of the IMF is a step in the right direction, but it is too restricted in its scope. It is the contention of this paper that the IMF uses its gold stock as an initial step in the direction of the achievement of these new objectives.

The IMF Gold Stock

The arrangements with regard to the present role of gold in the international monetary system are derived from agreements reached by the Interim Committee of the Board of Governors of the IMF. At its meeting in Jamaica in January 1976, various aspects of the implementation of the arrangements were worked out in detail. The effective outcome of these decisions was to abolish the official price of gold and the obligation of Fund members to use gold as part of their quota sub-

scription. Under the agreements, one-third of the Fund's gold stock would be disposed of, of which one-half would be 'restituted' to IMF members in accordance with their quotas, and one-half sold for the benefit of the Third World countries. The reasons for these decisions, and the rationale for phasing out gold as a central reserve asset of the international monetary system need not concern us here, except to the extent of their direct effects on the economic well-being of the Third World countries. In the context of the arrangements made for the phasing out of gold as an international reserve asset, it was agreed that the poor countries should receive some part of the benefits that might be generated by the abolition of the official price of gold. The gold stock of the IMF amounted to 150 million ounces and at the official price of 35 SDR per ounce (US \$ 42) the stock was valued at US \$ 6.7 billion. At the then prevailing market price of US \$ 140 per ounce, the gold stock was 3.3 times the value determined at the official price, and the total stock could be valued at US \$ 22 billion.

The IMF gold stock, however, is only a fraction of the total international monetary reserves held in gold. As of May 1975, the official gold holdings of the various member countries of the IMF at the official price of 35 SDR per ounce were worth US \$ 44 billion. This enormous accumulation of gold benefited immediately from the abolition of the official price and the re-evaluation which subsequently occurred in terms of market prices. Not all member countries of the IMF had significant gold reserves on their own account and the inequity of these arrangements for the Third World should be seen in this light. The Group of Ten, plus Switzerland, had over US \$ 37 billion of gold valued at the official price, while all the remaining nations in the IMF owned US \$ 7 billion worth. The latter group, in view of the convertibility of the currencies of the Group of Ten, plus Switzerland, held nearly 90 percent of their international monetary reserves in the form of convertible currencies (i.e. mainly the currencies of the Group of Ten, plus Switzerland). The figures are, while the Group of Ten, plus Switzerland, held US \$ 70

billion in foreign exchange, all the remaining countries had an almost equal amount, i.e. US \$ 68 billion in foreign exchange. This contrasts with the US \$ 7 billion held in gold. These figures prove that the gold price boom really benefitted those who had the gold while those who held foreign exchange in convertible currencies were abruptly told that their claims for gold at 35 SDR per ounce were no longer to be honoured. No wonder that the former Secretary of the Treasury of the U.S.A., Mr. Henry H. Fowler expressed his grave apprehension in no uncertain manner: "To assent to any arrangement that would work a grievous inequity on those central banks who hold our dollars resulting from US balance of payment deficits rather than present them to the Federal Reserve window in exchange for gold is not worthy of a great nation. This is particularly true when the United States would itself stand to reap the greatest monetary profit from this inequitable arrangement since its gold reserves are the largest."³

The international monetary system is probably the toughest nut for the Third World to crack in the NIEO negotiations. The Group of Ten calls the tune and the Group of 24 obtains a few crumbs to keep their economies alive. On 30 August 1975, the Group of 24 representing the Third World issued its own communique calling for "policies designed to ensure the gradual reduction of the role of gold in the international monetary system and the strengthening of the role of the SDR". Ministers also affirmed that no arrangements with regard to gold would be acceptable to the Third World unless they met the above principles and also unless,

"(a) they were designed to raise substantially the flow of financial resources to the developing countries without imposing a loss on any individual developing country;

"(b) they did not accentuate the already inequitable distribution of international liquidity."

"In this context, Ministers agreed that there was a need to expedite the study of a gold substitution account".

The Group of 24 Communique of three years later, issued on 22 September 1978, makes no mention of gold or the gold substitute account though the problems associated with

the phasing out of gold could still be central to the development process. The reasons for ignoring the issue—probably the concession to create 12 billion SDRs over three years—are not self-evident from the Communique.⁴

The Third World in recognition of their acquiescence with the 1975/1976 arrangements leading to the Second Amendment of the IMF Articles was allowed the profits from the sale of one-sixth (25 million ounces) of the IMF gold stock, disbursed through the Trust Fund administered by the IMF over a period of four years. In May 1978, the Fund passed the mid-point in its four years gold sales program and during the period of two years since these sales started 12.5 million ounces were sold for the benefit of Third World countries. The profits totalled US \$ 1,306 billion. Of this amount \$ 362.6 million were distributed directly to 104 eligible Third World member countries, and the balance amount of a little more than US \$ 1 billion was distributed through the Trust Fund on concessional terms to 43 of the poorest IMF members (the number of eligible members over the second two year period of the gold sales program number 59).⁵ It would be pertinent at this point to inquire into the actual movement of the market price of gold since the above decisions were taken, as even greater disadvantages continue to accumulate for the Third World.

The open market price of gold has moved continuously upwards and at the time of writing one ounce is quoted at over US \$ 240. This contrasts with the average sale price of the IMF gold sales programme in the first two years of US \$ 150. It is to be expected that the second phase would bring in profits for Trust Fund loan disbursements of well over the figure of US \$ 1 billion of phase I. In the meantime, in addition to the massive profits generated by the rich countries on their own national monetary authority gold holdings, nearly 10 million of the 12.5 million ounces sold by the IMF at the former official price would also have accrued to these countries and an equal quantity is expected to pass on to their hands over the next two years. At present market prices, and over the full four years, the

national gain of these few countries would be nearly US \$ 4 billion by the transfer of one-sixth of the IMF gold stock in accordance with quotas of member countries. The beneficiaries of even the gold sales program of the IMF are not the Third World countries but the rich member countries of the IMF. Prof. Fritz Machlup, an eminent American monetary economist, in 1975 itself commented thus on the grave injustice of these arrangements:

"The gold holdings of the 14 most-developed countries amount to US \$ 36 billion at the present official valuation. Hence, the gain accruing to these 14 countries, would be about US \$ 83 billion calculated on the basis of last week's market price of gold of US \$ 140 per ounce. To the \$ 83 billion we may have to add the value of these countries' share in the 25 million ounces of gold to be restituted. . . . Hence, counting only the share going to the industrial countries about US \$ 3 billion, we may put the increment in the gold holdings of these 14 countries at US \$ 86 billion. If the same market price of US \$ 140 can be attained for the other 25 million ounces to be sold by the Fund 'for the benefit of developing countries' the cash proceeds would be of US \$ 3.5 billion and the profit less than US \$ 2.5 billion. %This sum allotted to developing countries compares with the gain of US \$ 86 billion going to the 14 individual countries. These 14 countries would pocket, therefore, more than 34 times the profit distributed to the developing countries—".

Contrary to the above forecast, the reality has been even worse for the Third World. The present price of gold at US \$ 240 an ounce would indicate that the 14 highly developed countries are more than 50 times better off rather than 34 times. Countries like Italy have raised loans with gold as collateral valued at the inflated market prices and France values its gold at the market price. No longer is the benefit of the gold price increase a notional one.

It is not the purpose of this paper to assess the attempts made so far, and of their success or failure to phase out gold as a principal reserve asset. What is conclusive from the foregoing analysis is that the abolition of the official price of gold and the arrangements made to phase out gold have resulted in a major distribution of gains in favour of the rich countries, and in particular, a handful of them. It is imperative that the Third World and the IMF evaluate once again the present arrangements and offer a set of more equitable proposals for the disposal of the 100 million ounces of gold

which would remain with the IMF in 1980 after the disposal of one-third of the gold stock. At present market prices, this residual gold stock could be worth US \$ 24 billion. We are not concerned in this context with the proposals for a gold substitution account for conversion of officially held gold of IMF member-countries into SDRs. However, it should not be forgotten that the Third World countries should have a share in the capital gains of that situation too.⁶ But the proposition that the IMF gold stock should be solely utilised in the interest of and for the exclusive benefit of the Third World and in particular, the lower-income countries has greater validity than ever before.

Recent developments strengthen the moral as well as the political and economic claims of the Third World to be sole beneficiary of the residual 100 million ounces of gold with the IMF. The Third World should consider this stock as an asset which must be utilised to achieve some of its primary demands within the framework of a New International Economic Order (NIEO). The circumstances in which this gold stock has so far been utilised have led to an erosion of its potential strength. Rather than run it down by ad hoc disbursements based on ill-defined formulae, the Third World must consider its sustenance and continuation as an instrument for the greater control of the international economic environment.

Proposals for Action

It has been pointed out that, "as far as gold is concerned, the consensus reached by the IMF Interim Committee in August 1975 and confirmed in Jamaica in January 1976, provides a highly ingenious and acceptable compromise between very different and legitimate, national and international concerns and objectives."⁷

Three years later the ingenuity of the authors of the Agreement is open to doubt by the Third World. There is now talk of "the gold revival" and "not so heavily disguised, it is now slipping in through the back door. Many central banks are revaluing their gold reserves and a few are actively buying and selling the stuff. Most significant of all, when the European Monetary System (EMS)

is eventually born, it will have a gilded spoon in its mouth".⁸ The IMF is presumed to dislike these new trends but they are the political and economic reality. The European Currency Unit (ECU) will be backed up by gold and the apparent acceptance of the French position in revaluing gold for this purpose at nearly market prices would mean the remonetization of gold... The 1975 IMF Gold Agreement was a compromise reconciling US and French positions and the Third World did not come out of it satisfactorily. New French moves and the major gains that have accrued to the rich nations demand an urgent re-appraisal and a new design for gold. For the Third World, benefits from demonetization of gold have been restricted to relatively small disbursements (US \$ 1 billion in two years) from the Trust Fund. Even in the basis of principles accepted in 1975, the Third World countries, particularly those with an income of SDR 300 per capita in 1973 had an entitlement to nearly half the IMF gold stock. There is overwhelming justification to use not half but the entire IMF gold stock for the benefit of Third World countries in view of recent developments. This question is a matter for international monetary diplomacy but its political feasibility need not be that remote if there is some equity in the bargaining process. Though amendments might be required to the IMF Articles, there is no direct cost to the rich nations in an exercise of this nature, and there could in fact be considerable gains if once again the 'ingenuity' of reformers is matched by an equal commitment to international economic stability in the medium term.

The IMF residual gold stock of 100 million ounces is worth, at current market price, US \$ 240 billion. This paper proposes that the gold stock be used for two major purposes:

1. The establishment of a new credit facility in the IMF with access to it for the low-income countries that presently have access to the Trust Fund. Half of the gold stock could be used for this purpose. Basic human needs conditionality would have to be met for access to this facility.
2. The creation of a new Currency Unit backed 100 percent by gold, which would be available for payment within the Third World only. The initial

disbursement would be to the low-income countries, eligible according to Trust Fund criteria.

A New IMF Credit Facility

Basic human needs in the Third World is a central issue in development over the next decade but present IMF policies are not exactly conducive to its achievements. There is a positive correlation between economic growth and basic needs, but it is necessary to establish closer linkages between investment for growth and investment for the relief of poverty. The distinction between investment and recurrent expenditures is blurred when the objective is growth in, for example, the informal sector.

The strains of the foreign exchange of countries pursuing a basic human needs strategy have to be relieved by access to credits without conditionality, and in low-income countries which are presently averse to a basic human needs strategy, access to credit conditioned on such purpose would promote its acceptance. For the Third World as a whole, and for the specific provision of basic human needs, the IMF could have exemption clauses on the existing facilities related to indicators it works on (public expenditure targets could exempt those items directed at the most poor and food subsidies could be considered an acceptable measure for those living in absolute poverty and so on).

It is proposed that the Basic Human needs facility could be US \$ 12 billion or half of the value of the gold stock. It could be started with less, but increased very rapidly to its maximum limit. If US \$ 12 billion, this would probably mean a nearly 100 percent increase over present levels of access to IMF credits for the low-income countries. These arrangements raise a major question: How would the gold stock be converted into some acceptable form of currency to provide these credits? This could be done in several ways, among which are the following: (1) negotiating with the rich nations, 'swap' facilities between their currencies and gold, (2) the sale of gold when market prices are really favourable, unlike the present gold sales program (3) borrowing from the commercial banks with gold as collateral. In the latter case an interest subsidy account might have

to be considered dependent on the extent of concessionality of the required lending. There are features in this proposed arrangement which make it somewhat identical to the Trust Fund. The major differences would be in its magnitude, and the generation of resources other than through gold sales. The impact within a 10-year development strategy would be that much greater.

A Third World Currency Unit

Third World countries have little control over the world trade and payments system. Special Drawing Rights are issued in a manner that three-fourths go to the rich countries. In the last three years the Third World position has steadily declined as the rich nations financed their deficits by inflationary issues of their national currencies. The European Currency is to be created, backed by gold, adding further to international liquidity.

The Third World for reasons we shall not analyse here would wish to increase their trade among themselves, and greater access to Third World countries into each others' markets, might relieve emerging problems for the industrialized countries. A Third World currency to promote trade within the Third World has been proposed elsewhere.⁹ The proposal is to create a little over US \$ 2.5 billion of New Currency Units as a proportion of the total value of the trade in manufactures within the Third World. The use of the currency was to be restricted to purchases of manufactures. The proposal now presented contains features that should make it more attractive as an international currency, which was a substantial obstacle in the earlier proposal.

Half of the gold stock of the IMF, valued at US \$ 12 billion could provide the gold backing for the new currency in 10 years time (or a suitable medium term time span) by which it is expected the new unit would have emerged as an acceptable currency in international tender. With 100 percent gold backing the new currency issue would be restricted to US \$ 12 billion. It would be issued to the low-income countries (as defined for Trust Fund purposes) in the first instance. To that extent there would be an initial transfer of resources to those countries. Thereafter the currency could

be available for use by any Third World country and its validity need not be restricted to manufactures, though, certain commodities could be excluded. As one of the major objectives of a new currency is to promote trade within the Third World, the transactions to which it is applied should be carefully worked out. To illustrate, payments for shipping services may be a relevant item, thereby assisting in the increase of merchant shipping capacity within the Third World. The more industrialized countries within the Third World should find the currency an attractive instrument to increase their trade specifically in the context of underutilized industrial capacity.

The IMF would be the issuing authority for the currency. This alone would ensure its ready acceptance and it should be in a position to earn interest like any other reserve currency. It need not be a requirement that it should be used only by central banks, like SDRs and the proposed ECU, in the different context of the Third World, with its mainly non-convertible currencies and exchange restrictions.

The IMF would have its reservations on the use of gold to create a new currency. But gold has particular attraction as a midwife at the birth of new currencies. However, the use of gold would be for a limited duration of ten years. It would also not be a freely convertible currency, being a currency for use only

within the Third World. The IMF has not actively opposed the ECU and this would therefore constitute an appropriate precedent. The objectives to be achieved from the new currency are consistent with IMF principles and policies for the expansion of international trade. The IMF has been too closely associated in its operations with the interests of the rich nations and their banking sector, particularly in recent years. The implementation of a proposal of the nature outlined above would probably improve its image in the Third World as a truly international organization and offset any inherent bias in the existing system.

It must be stressed, in conclusion, that the proposals made above are tentative and in outline, and their implications have to be worked out in more detail. But the main thrust of the contention should be in no doubt. There is an IMF gold stock of US \$ 24 billion lying idle and which could be used in the 1980s to benefit the Third World. Even if conventional mechanisms are used, resources could be raised from the banking system, with gold as collateral, for transfer to poorer countries through existing institutions like the World Bank, Regional Banks and IFAD. The way the gold stock is administered at present leads only to a mere trickle of such resources reaching the poor countries. The Third World should set its targets higher and exploit the latent potential in the IMF gold stock within a more comprehensive programme.

NOTES

1. *IMF Survey*, 22 May 1978.
2. See a very good article by Anthony Scaperlanda on "The IMF: An Emerging Central Bank", *Kyklos* (Vol. 31-1978:4), pp. 679-690.
3. *The IMF Gold Agreement: Hearing before the Subcommittee on International Economics of the Joint Economic Committee—Congress of the United States* (US Government Printing Office Washington, 1976). I have relied on this document for the figures contained in this section and for extracts from statements of Mr. Fowler and Prof. Machlup. This document is essential reading for evidence of the extent to which Third World interests were overlooked in the 1975/1976 monetary negotiations.
4. See issues of *IMF Survey* for Communiqués of the Group of 24.
5. See issues of the *IMF Survey* for progress of gold sales program and Trust Fund operations.
6. See Angelos Th. Angelopoulos, *For a New Policy of International Development* (New York: Praeger, 1977) for recent proposals for use of gold held by central banks, rather than IMF gold holdings. Angelopoulos has been a consistent advocate over a long period of utilising the increased value of monetary gold held by national banks in the interests of the Third World. He disagrees with the present Policy of IMF gold sales and suggests that "the Third World countries should demand a halt to these sales, to safeguard their interests."
7. See Duncan Ndegwa and Robert Triffin, *The International Monetary Order in Reshaping the International Order (RIO): A Report to the Club of Rome* (1976).
8. "The Gold Revival", *The Economist* (13 January, 1979).
9. Frances and Michael Stewart, *Trade between Developing Countries: Proposal for a New Currency* (UNCTAD, Mimeo).