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Policy Development and Review Department

Currency Convertibility and the Fund:
Review and Prognosis 1/

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Abstract

This paper reviews experience with currency convertibility on both the current and capital accounts, with particular attention to the Fund's concepts and policy implications. After discussing the basic concepts of convertibility, the paper reviews the experience with convertibility in three groups of Fund members--industrial countries, developing countries, and transition countries. The paper also discusses some policy options designed to encourage acceptance of convertibility by Fund members that have not yet done so.

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1/ Even more than in the usual case, the author wishes to emphasize that the views contained therein are his own and do not necessarily reflect those of the IMF, the Board, or the staff. Any opinions and remaining errors are therefore the sole responsibility of the author, who would like to thank without implication Charles Adams, Hans-Michael Flickenschild, Aerdts Houben, and R. Barry Johnston for their comments on an earlier version of this paper, and Hassan Al-Atrash, Eduard Brau, Craig Beaumont, Gerard Belanger, Owen Evans, Ross B. Leckow, Ake Lonnberg, and S. Kal Wajid for a second round of comments.

Currency Convertibility and the Fund:
Review and Prognosis

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Summary

This paper reviews experience with currency convertibility on both the current and capital accounts in Fund member countries, paying particular attention to the Fund's concepts and policy implications. A basic concept of convertibility--the jurisdictional concept of Article VIII, Sections 2, 3, and 4--is that of the absence of restrictions on payments and transfers for "current international transactions" (that is, all current account transactions and a few capital transactions). By contrast, the Fund's Articles of Agreement allow members to maintain controls on international capital movements, provided that they do not restrict payments for current transactions or unduly delay transfers of funds in settling commitments. The paper notes that, for convertibility to be meaningful, it must be accompanied by liberalization of trade in goods and services--an area over which the World Trade Organization has jurisdiction.

The study observes that the 23 industrial countries no longer maintain exchange or capital restrictions. Of the 158 nonindustrial member countries of the Fund (developing countries and transition countries), well over one half have accepted the obligations of Article VIII, Sections 2, 3, and 4. Most of these, plus some others, no longer maintain restrictions on current international transactions, and an increasing number also have eliminated capital restrictions. Many nonindustrial countries liberalized exchange and capital controls in the context of comprehensive liberalization programs, supported in many instances by Fund resources. The 25 transition countries have given high priority to removing restrictions on current international transactions, and 12 of them have promptly accepted the obligations of Article VIII. In most transition countries, the liberalization of capital controls has been given lesser priority while basic reforms have been consolidated.

The paper highlights the unfinished business in the nonindustrial countries concerning the speed for achieving current account convertibility, the termination of multiple currency practices, and the introduction of capital convertibility. Although the Articles of Agreement do not specify a time limit for accepting the obligations of Article VIII, Sections 2, 3, and 4, Fund staff has made members increasingly aware of the benefits of early current account convertibility and provided useful advice on achieving and retaining such convertibility. There is also a trend toward eliminating multiple currency practices and the exchange and trade restrictions that give rise to parallel markets. With regard to capital account convertibility, much can continue to be accomplished within the present regulatory framework; alternatively, the Fund membership could consider amending the Articles to expand Fund jurisdiction over capital controls. The paper suggests that in these three areas, improvements in periodic reporting to the Fund could further promote the achievement of current and capital account convertibility.

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I. Introduction

The Articles of Agreement of the IMF define the basic code of conduct for Fund members in two broad areas of policy: achievement of current account convertibility, and choice of exchange rate regime and policy.

Regarding convertibility, one of the purposes of the Fund is "to assist in the establishment of a multilateral system of payments in respect of current transactions between members and in the elimination of foreign exchange restrictions which hamper the growth of world trade" (Article I(iv)). By contrast, the Fund's Articles allow members to maintain controls on international capital movements at their own discretion, subject to some provisions (Article VI, Section 3). 1/

Exchange rate policy is also central to the Fund's purposes. One of these purposes is "to promote exchange stability, to maintain orderly exchange arrangements among members, and to avoid competitive exchange depreciation" (Article I (iii)). Correspondingly, each member is obliged inter alia to "avoid manipulating exchange rates or the international monetary system in order to prevent effective balance of payments adjustment or to gain an unfair competitive advantage over other members" (Article IV, Section 1(iii)). However, since the Second Amendment, the Articles recognize the "right of members to have exchange arrangements of their choice consistent with the purposes of the Fund..." (Article IV, Section 2(c)).

This paper focuses on the experience with, and the policies designed to encourage currency convertibility on both the current and capital accounts (full convertibility). The point of departure is the recognition of the interdependence between currency convertibility, exchange rate policy, and domestic demand (monetary and fiscal) policies. Broadly speaking, it is widely recognized that a country cannot simultaneously achieve convertibility, a fixed exchange rate, and monetary policy independence. 2/ Thus, when most European Union countries accepted participating in the Exchange Rate Mechanism (ERM), which implied maintaining a fixed exchange rate among themselves, and at the same time adopted full convertibility, they did so on the assumption that they would be able to keep appropriately coordinated domestic demand policies (basically a single monetary policy, leading eventually to a common currency, and moderate fiscal policies). However, floating or some other

1/ Article VI, Section 3 states that "Members may exercise such controls as are necessary to regulate international capital movements, but no member may exercise these controls in a manner which will restrict payments for current transactions or which will unduly delay transfer of funds in settlement of commitments, except as provided in Article VII, Section 3(b) and in Article XIV, Section 2."

2/ To some extent this also applies to fiscal policy and even to wage policies.

form of exchange rate flexibility became necessary, in the absence of exchange restrictions, when domestic demand policies and economic developments failed to provide adequate coordination for maintaining the agreed exchange rate parities; this was exemplified by the exit of Italy and the United Kingdom from the ERM and devaluations in Portugal and Spain in September 1992, as well as by the subsequent widening of the ERM bands around the established parities. 1/

As noted, under the Second Amendment members are no longer obliged to maintain fixed parities and, therefore, implicitly a clear preference would seem to have been given to the goal of avoiding exchange restrictions (particularly on current transactions) over the fixing of the exchange rate. As a result, convertibility--always an important goal in the Fund's purposes--is particularly relevant under the Second Amendment. In order of preference, when dealing with balance of payments problems, countries are urged to make use first and foremost of domestic demand policies, and failing this, to make appropriate exchange rate adjustments; the maintenance or reintroduction of exchange restrictions is not viewed as an acceptable option. 2/ This preference for some adjustment policies (market-based policies) over others, is based on efficiency considerations and provides the basis for the Fund's principles on conditionality. The Fund is called to finance balance of payments adjustment only if carried out through the appropriate methods, that is, by curbing domestic demand and improving supply policies and, failing this, by depreciating the exchange rate, but not through exchange restrictions (Guitián, 1981).

The rest of this paper is arranged as follows. Section II discusses the basic concepts of convertibility, with particular attention to the Fund's concepts and policy implications. Section III briefly reviews experience with convertibility in three groups of Fund members--industrial countries, developing countries, and transition countries. The last section discusses some policy options designed to encourage early acceptance of convertibility by Fund members that have not yet done so.

1/ However, floating may also be undertaken voluntarily to allow for some degree of monetary independence under sound domestic policies. This is for instance the case of Singapore and Switzerland, which have generally benefitted from having appreciating currencies and very low inflation rates under tight domestic demand policies.

2/ Another recent example of policy interdependence is provided by Mexico. Given its firm commitment to full convertibility, maintenance of a fixed rate with respect to the U.S. dollar required renouncing to have an independent monetary policy (as would happen, for instance, under a currency board system of the type established in Argentina). In the absence of a total domestic policy commitment, the only other alternative is to have a floating exchange rate system such as is presently the case.

II. Basic Concepts

Currency convertibility is the ability of residents and nonresidents to exchange domestic currency for foreign currency and to use foreign currency in real or financial transactions. This implies the absence of restrictions on the making or receipt of payments for international transactions and on the exchange of local for foreign currency for those purposes. There are, however, many degrees of convertibility depending on the restrictions imposed by the government on the exchange of currency. A basic distinction can be made for these purposes between the current and capital account transactions. For the Fund's purposes, current account convertibility refers to the absence of any restrictions on the making of payments and transfers for "current international transactions" (that is, all current account transactions and a few capital transactions). 1/ Full convertibility of a currency means that there are no payments (or receipts) restrictions either on the current or the capital account.

1. Current account convertibility

The basic concept of convertibility in the Fund's Articles of Agreement--the jurisdictional concept--is that of current account convertibility (Gold, 1971). 2/ Capital account convertibility is not mandated in the Articles except in some specific cases of transactions which are closely related to the current account, such as amortization of loans or depreciation of direct investments. 3/ Therefore, except in those specific cases, a Fund member may restrict inward or outward movements of capital

1/ From a more general economic point of view, current account convertibility also comprises the absence of restrictions on the receipts and inward transfers for current international transactions. The Fund's Articles do not specifically refer to receipts and inward transfers, perhaps because it is assumed that governments would not in any case be interested in imposing restrictions of this kind.

2/ For a more recent exposition of various Fund currency convertibility concepts, see Guitián (1993a). He notes among others, the distinction between "hard" and "soft" current account convertibility. Hard convertibility was that which applied to members under the Bretton Woods regime of fixed parties, that is, convertibility at a fixed exchange rate. By contrast, soft convertibility refers to convertibility at the going market exchange rate, a possibility open by the abandonment of fixed parities in the Second Amendment.

3/ The definition of payments for current transactions contained in the Articles of Agreement includes some items which belong to the financial (capital) account in the Fund's methodology on the balance of payments. Specifically, the making of "payments of moderate amounts for amortization or for depreciation of direct investments" is included as part of current transactions (Article XXX (d), (3)).

capital without the need for Fund approval. 1/ However, the Fund may provide advice on capital controls--because they can affect the balance of payments and exchange rates--in the context of exercising its general surveillance over exchange rates or in the context of economic programs supported with the use of Fund resources.

The general obligations of Fund members with regard to the avoidance of restrictions on payments and transfers for current international transactions; discriminatory currency arrangements and multiple currency practices; and the rules regarding the convertibility of foreign-held balances, are set out in Article VIII, Sections 2, 3, and 4, respectively. A member availing itself of the transitional arrangements under Article XIV, Section 2, may, however, "maintain and adapt to changing circumstances the restrictions on the making of payments and transfers for current international transactions that were in effect on the date on which it became a member." Members' obligations regarding controls on capital transfers, which cannot be exercised in a manner "which will restrict payments for current transactions or which will unduly delay transfers of funds in settlement of commitments," are contained in Article VI, Section 3. The general thrust of these provisions is to provide for the elimination of restrictions on payments and transfers for current international transactions (current account convertibility), and to ensure that any controls on capital transfers will not restrict payments for current transactions or unduly delay transfers of funds in settlement of commitments. Restrictions on payments and transfers for current international transactions can take various forms such as prohibitions on import payments, taxes on import payments and on the transfer of profits and dividends, advance import deposit requirements, absolute limits on the availability of foreign exchange for invisible payments (such as for travel, study, and medical allowances) and rationing procedures for allocating foreign exchange to imports of goods and services.

In addition, members, subject to certain exceptions, are prohibited from engaging in discriminatory currency arrangements and/or multiple currency practices (Article VIII, Section 3). In a discussion in February 1985, the Executive Board was divided on the staff's view that the Fund's jurisdiction over multiple currency practices encompassed all such practices including the ones related solely to capital transactions. 2/ While most

1/ Indeed, Article VI, Section 1, of the Articles of Agreement provides that the Fund may request a member using its general resources to impose controls to prevent that those resources are used to meet large or sustained outflows of capital.

2/ The staff's case for arguing that multiple currency practices related solely to capital transactions are included in the proscription of Article VIII, Section 3, rests in part on the fact that the language in Section 3 (unlike that in Section 2) does not refer to current transactions. In addition, there is often a problem of distinguishing multiple currency practices arising from current and/or capital account restrictions.

Directors viewed multiple currency practices and capital controls as costly in terms of resource allocation and difficult to administer, others viewed them as important additional emergency tools when faced with large, destabilizing capital flows.

First, although capital account restrictions are generally allowed by the Articles, it does not necessarily follow that the particular restrictions involved in multiple currency practices applicable solely to capital transactions are also allowed. Second, if as suggested by the staff the Articles are interpreted as giving the Fund jurisdiction over all multiple currency practices, including those applicable solely to the capital account, a strange set of policy priorities could result with regard to restrictions applicable to the capital account. Such interpretation would imply that quantitative exchange restrictions on capital movements would be allowed under the Articles, whereas cost restrictions and composite exchange restrictions (a combination of quantitative and cost restrictions) would not, even though quantitative restrictions often are considered to be the more discriminatory and inefficient. ^{1/} Against this argument, however, it should be noted that the reason for taking a particularly dim view on multiple rates is that foreign exchange is probably one of the most homogeneous goods imaginable and that it should be traded at one price only. For good reason, the Bretton Woods system wanted to get away from multiple rates. Third, because quantitative exchange restrictions often lead to cost restrictions, thereby becoming composite restrictions, it is unclear whether there is any effective scope for members to maintain any capital restrictions as authorized under Article VI.3. One possible answer is that this general authorization to keep capital restrictions covers cases in which quantitative restrictions lead to cost restrictions for certain transactions which are considered strictly illegal by the member, although it is well known that the existence of the latter is frequently an economic consequence of the quantitative restrictions.

It is indeed generally understood in Fund practice that, from a jurisdictional point of view, whether a dual exchange rate system gives rise to a multiple currency practice depends on whether official action by the member or its fiscal agency gives rise to a spread in rates of more than 2 percent between the member's currency and another currency. ^{2/} However, from the economic point of view, a dual exchange rate system involving an official rate and a parallel market rate, whether the parallel market is

^{1/} This assumes, of course, that the existing quantitative restrictions are binding, that is, that they effectively constrain the volume of flows that can take place. Otherwise, non-binding quantitative restrictions could turn out to be less distortionary than tax restrictions. For an analysis of the different forms of exchange restrictions see IMF (1950, Chapter Two).

^{2/} To the extent that a parallel rate arises out of restrictions on current account payments, this would already be proscribed under the Fund's jurisdiction. This would not be the case if it were the result of solely capital account restrictions.

officially sanctioned or not, results in a distortion of costs and of the allocation of foreign exchange to competitive uses. 1/ Moreover, ultimately, the existence of a parallel rate is a consequence of government restrictions on some international transactions. 2/ For these reasons, the jurisdictional distinction between official and unofficial dual exchange rate systems has been de-emphasized in practice. At a minimum, the Fund has proceeded to request members to provide periodic information on such practices. 3/

Members' obligations under Article VIII refer exclusively to financial transactions (that is, payments and transfers for current international transactions, and the purchase and sale of foreign exchange) not to the underlying real transactions (trade) which give rise to them. Jurisdiction in the trade area is vested in the World Trade Organization (WTO), one of the three institutions contemplated in the original Bretton Woods conference but which did not get established until 1995. 4/ Given the potentially close substitution between exchange and trade restrictions, however, a combined examination of both aspects is necessary to ascertain the overall direction of change in the restrictive nature of regulations on the current account of the external sector. "Thus, convertibility--a financial concept--should be accompanied by liberalization of trade and other international transactions, implying that the benefits of full convertibility are derived from both 'financial' and 'commodity' convertibility" (Gilman, 1990, p. 33).

1/ For an overview of parallel currency markets in developing countries, see Agénor (1992).

2/ However, some parallel exchange markets may arise not from government exchange restrictions but from other prohibitions which affect indirectly the exchange market. For instance, money laundering on illegal drug trafficking may result in a parallel rate. The authorities could hardly be made responsible for these kinds of multiple rates (in fact, in most cases, such multiple rates would not be observable to the authorities except as a result of special police inquiries). For this reason, it would be necessary to examine the situation on a case-by-case basis.

3/ The staff already monitors exchange rates in parallel markets in the course of Article IV consultations, use of Fund resources, and other contacts with the authorities. However, there is to date no general compilation and reporting of parallel rates. (The only general source of information on parallel or black market rates is a private New York firm, which is used in Table 2 of this paper. But no one can vouch for the accuracy of this source.) Admittedly, requiring official reporting of black market exchange rates can be a sensitive matter in some cases, as it might be misinterpreted by market participants as official recognition of the illegal markets.

4/ Before the creation of the WTO, the post-war world had organized multilateral trade liberalization through the General Agreement on Trade and Tariffs (GATT). With the creation of the WTO, other agreements, mainly in the areas of services transactions and the right of establishment, have been added to the GATT.

Among the obstacles to "commodity" convertibility--trade restrictions--are cumbersome import and export licensing systems, quantitative restrictions on trade in goods and services, import deposit requirements, prohibitive tariffs and trade discrimination in any form. Clearly, to be economically meaningful, current account convertibility needs to be accompanied by substantial elimination of at least nontariff barriers to imports (Williamson, 1991).

Exchange and trade restrictions must be viewed as a whole--and not in separate compartments--to be able to evaluate the overall restrictiveness of a country's external controls. A country that no longer maintains restrictions on payments and transfers for current international transactions, may nevertheless maintain severe trade restrictions. Conversely, a country that still maintains some exchange restrictions 1/ may have a largely liberal external system, first because the remaining exchange restrictions may be minor in scope and substance and second because it may have minimal trade restrictions. Although both financial and commodity convertibility are necessary to derive the benefits of free international transactions, it is often argued that financial convertibility should come first because the results that can be accomplished through financial restrictions can also be accomplished through trade restrictions but in a manner that provides greater transparency and that permits the use of more market-based instruments, such as tariffs, rather than quantitative restrictions.

The application of restrictions on payments and transfers for current international transactions constitutes under virtually any conditions an inefficient way of maintaining a sustainable balance of payments or protecting specific local industries, because these restrictions tend to be ineffective in the aggregate, while they induce microeconomic distortions, and because of their general lack of transparency compared to trade restrictions. However, there are two reasons for which governments often proceed cautiously in removing exchange restrictions on current account invisibles. First, unlike in the case of merchandise trade, it is difficult to control or tax the underlying real transactions on invisibles, so in this area governments focus instead on the financial transactions to which they give rise. Second, governments often control financial transactions on current invisibles because such transactions are viewed as a potential vehicle for capital outflows. In practice, however, the second problem can be solved by authorizing reasonable minimum allowances for such transactions as traveling, education, and medical services abroad, and by providing for additional allowances, upon request, subject to presentation of adequate documentary evidence.

1/ A member could maintain restrictions on payments and transfers for current international transactions either as allowed under Article XIV, or with Fund approval under Article VIII, or without the necessary Fund approval.

The need to proceed quickly with both current account convertibility and trade liberalization in eastern Europe has been presented as the only way "to subject domestic producers to competition from abroad and, in the process, to 'import' a system of economic pricing" (Polak, 1991, p. 22). In a similar context, various modifications of the current account approach to convertibility have been considered in the literature. One such modification would exclude tourism from the current account and would lump it together with capital transactions; official foreign exchange would be provided for all merchandise trade and other current account transactions, with the exception of tourism, which, together with all capital transactions, would be conducted in a tolerated parallel exchange rate market (Williamson, 1991). Another modification would liberalize, in addition to current account transactions, inward foreign direct investment, which can help attract associated managerial resources and transfers of technology (Greene and Isard, 1991).

Be that as it may, certain conditions for the successful implementation of current account convertibility (or its related concepts) are considered necessary. These include an appropriate exchange rate, substantial international liquidity (reserves), sound macroeconomic policies, and the ability of the economy to respond to market prices (Gilman, 1990; and Greene and Isard, 1991). All these conditions need not be present, however, in any given case. For instance, the external effect of expansionary macroeconomic policies leading to inflation may be handled through an appropriately flexible exchange rate, without the need to recur to exchange and trade restrictions. Moreover, if the domestic demand disturbance is only temporary, it may be appropriate to use up reserves to avoid both exchange rate depreciation and exchange and trade restrictions.

2. Capital account convertibility

Capital account convertibility remains a more controversial goal, and one that has often been relegated to a lower category of desirability. ^{1/} It is certainly not required under the Articles of Agreement, and it is generally regarded as premature for transition economies (Polak, 1991; Williamson, 1991; and Greene and Isard, 1991), as well as for many developing countries. Among the main arguments against capital account convertibility (especially at an early stage) are the possibility of destabilizing (speculative) capital flows during the transition period, and

^{1/} For recent surveys of the academic literature on the desirability of capital controls in developing countries, see Dooley (1995a, and 1995b).

the possible loss of capital needed to finance economic development. 1/ However, the inefficiencies generally created by capital controls, as well as the practical difficulties and resource costs in implementing those controls, should be recognized (Mathieson and Rojas-Suárez, 1992, 1993; and Guitián, 1992b and 1993b).

In contrast to the cautious views on capital account convertibility for developing and transition economies, the industrial countries firmly, albeit gradually, moved forward to establish full capital convertibility even as trade barriers increased during the 1980s and early 1990s. Soon after its establishment in 1961 the OECD adopted the Code of Liberalization of Capital Movements (in addition to the Code of Liberalization of Current Invisible Operations). The Capital Movements Code committed OECD member countries to eliminate any restrictions listed therein, although it left reasonable scope for countries to move toward the ultimate objective in different ways and at varying speeds. Since 1989, the Code has covered all capital movements, including money-market and other short-term financial activities, as well as banking and financial services (Fischer and Reisen, 1992, p. 5; and OECD, 1992). More important, capital account liberalization received final impetus within the European Union as a result of the second Capital Markets Liberalization Directive (1988), which committed the EU members to the removal of all remaining capital controls, not only among the EU countries but with nonresidents of the rest of the world as well. This resulted in the establishment of an end-1992 deadline for the removal of capital controls by EU members, except for a few which were given a limited extension. 2/

As in the case of current account convertibility, the achievement and sustainability of capital convertibility is predicated on a number of conditions, some of which are the same as those necessary for current account convertibility. These conditions include macroeconomic stability, fiscal consolidation, noninflationary finance of any remaining public sector deficits, right monetary-fiscal policy mix and last, but not least, the

1/ It should be noted that, unlike in the case of the current account, these are theoretical arguments in favor of capital controls which may remain valid even in the long run. Another, more sophisticated argument, is based on the possibility of existence of multiple equilibria, with controls acting to steer the economy away from the less desirable equilibria supported by the markets. See Dooley (1995b). However, the theoretical possibility of second-best capital controls does not necessarily justify the imposition of such controls, since it may be empirically difficult to identify the market failures giving rise to them and the types of controls needed to overcome them.

2/ The recognition of the impulse generated by official commitments to eliminate capital controls does not belittle the fact that those commitments themselves followed the pressures of the markets (through multinational corporations, international banks, and offshore financial centers) to remove capital controls.

development of the domestic financial sector in a free market context. The latter includes the establishment of free interest rates, the reduction of differences between domestic and external financial conditions, the limitation of taxes on income, wealth and transactions, strengthening the safety and soundness of financial institutions through improved banking supervision and recapitalization, and building of primary and secondary securities markets for monetary policy implementation and financial stability (Fischer and Reisen, 1992; and Mathieson and Rojas-Suárez, 1993). Not all these conditions are necessary in any particular case. Moreover, the introduction of capital convertibility may, under some circumstances, promote the attainment of the very conditions needed to maintain it.

The concerted liberalization of capital flows in the EU is an example of the EMS going ahead of the Bretton Woods system, with which it is often compared. This raises "a question about the continuing appropriateness of the distinction in the Articles of Agreement between current and capital transactions, a distinction conceptually and operationally awkward." (Guitián, 1992a, p. 31.) In regard to capital controls, "the time has come for updating the code of conduct so as to bring it into conformity with economic logic, which argues against restrictions regardless of the nature of the transaction, and with the current prospective world economic environment, where capital movements have established both a permanent and prominent presence. ... [In sum] extending the code of conduct to cover all international transactions would be most appropriate for the establishment of true universality." (Guitián, 1992a, pp. 44-45).

Based on the notion of the need for capital controls under some circumstances, Article VI, Section 1, of the Articles of Agreement provides that the Fund may request a member using its general resources to impose controls to prevent these resources from being used to meet large or sustained outflows of capital. However, before recommending to the member the imposition of capital controls, the Fund has generally preferred to advise the member to adjust its macroeconomic policy framework so as to discourage capital outflows, e.g., by lifting domestic controls on interest rates and by tightening monetary policy to reduce inflation and increase interest rates. Indeed, in the absence of a sound macroeconomic framework, the Fund would not be in a position to allow the member to use Fund resources. This may explain why the Fund, true to its main objectives, has never used this provision of the Articles.

Foreign exchange repatriation and surrender requirements maintained by many developing countries are closely associated with capital outflow controls. Proceeds from exports of goods and services and from external borrowing must be repatriated if a total capital outflow control is desired because the alternative, that is, depositing or investing abroad, would violate capital outflow controls. ^{1/} In addition to repatriation,

^{1/} It should be noted that even under strict capital controls, enterprises may be allowed to hold some amounts of foreign exchange abroad.

surrender requirements (the mandatory sale of foreign currency, in exchange for domestic currency, to banks or to the central bank) may perform the function of ensuring the availability of foreign exchange to cover not only public sector needs but also those of importers of goods and services. ^{1/} A repatriation requirement, then, is often an important component in a regime that includes capital controls, whereas a surrender requirement is, in addition, a restriction on the domestic holding of foreign currency assets by residents (a restriction on "internal" convertibility).

3. Sequencing issues

The timing of convertibility poses two issues. The first is to know when is a good time for currency liberalization measures in relation to the liberalization of the rest of the economy. The second is the internal sequencing of convertibility measures. As in other economic policy areas, opinions on sequencing vary on both these issues (Galbis, 1994). Current account convertibility has acquired urgency, as noted earlier, in view of the need of formerly planned economies to introduce a set of rational prices. With regard to capital convertibility, "experience suggests that capital market integration will continue in spite of controls and that economic policy in emerging markets will have to adapt to changes in international interest rates. Capital control programs will become less effective over time and, eventually, the emerging country will have to choose between more flexible exchange rates or domestic interest rates that are determined in international capital markets." (Dooley, 1995b, p. 7).

On the internal sequencing of convertibility cum trade liberalization, a typical recommendation for the liberalization process would be as follows:

- (1) Remove current account restrictions and some selected capital restrictions
 - (1.a) Remove exchange restrictions on current international transactions and on trade finance and inward foreign direct investment;
 - (1.b) Remove quantitative trade restrictions;
 - (1.c) Reduce tariffs and standardize them at a relatively low level.
- (2) Remove remaining capital account restrictions
 - (2.a) Remove remaining restrictions on foreign direct investment and trade finance, and lift restrictions on portfolio investment;

^{1/} The surrender requirements are a restriction on the direct use of foreign exchange by exporters of goods and services and by borrowers, but may also be used in some cases to ration foreign exchange distribution to importers at the officially determined exchange rate.

- (2.b) Remove remaining controls on capital outflows;
- (2.c) Remove remaining controls on capital inflows. 1/

Stage one may lead to a dual exchange rate system: an official rate for current account, trade finance, and foreign direct investment transactions, and a parallel rate for the rest of the capital transactions. If the remaining capital controls could be well designed (effective) and if the market was backed by sound monetary and fiscal policies, a parallel exchange market need not arise, at least not in an organized way. This would be especially true if the official exchange rate was floating or adjustable in some form that took into account market developments.

Depending on individual circumstances of members, however, the above sequencing need not be the preferred one. Some countries may benefit from early capital account liberalization even if not completely able to remove all current account restrictions at once. 2/ Also, the introduction of capital convertibility need not wait until all the preconditions are right but may be introduced simultaneously with current account convertibility (Gutián, 1992b and 1993b). There are also examples of members that have successfully introduced capital convertibility in a big-bang fashion (United Kingdom) and others which did it more gradually (Japan).

III. Experience with Convertibility

The experience with convertibility is varied across members, but as a first approximation, a distinction can be made for the purposes of this paper between industrial countries, developing countries, and transition countries of eastern Europe and the former Soviet Union. In general, industrial countries have progressed further than the others in achieving both current and capital account convertibility. 3/

1/ The need to retain some capital inflow controls to the end of the process--mainly on short-term financial inflows--is predicated on the prediction that liberalizing countries would be swamped with capital inflows, rather than suffer outflows, if they maintained appropriate macroeconomic policies.

2/ The sequencing of capital account liberalization will also depend on the domestic institutional capacity, for instance, whether it is possible promptly to develop indirect monetary policy instruments.

3/ For a brief historical overview of countries' acceptance of the obligations of Article VIII, Sections 2, 3, and 4 of the Fund's Articles, see the Appendix to this paper. The information presented in this paper reflects the position of members as of end-1995 (as reflected in Tables 1 and 3). Since then Hungary and Mongolia have accepted Article VIII obligations.

By contrast, with exceptions, the introduction and maintenance of convertibility in developing countries has been uneven and hesitant, even in the case of some members that have for long formally adhered to the obligations of Article VIII. In fact, there is some blurring between Article VIII and Article XIV members. Some of the Article VIII developing members continue to apply exchange restrictions on current transactions from time to time--some explicitly approved by the Fund and others without due approval--as a result of various circumstances. 1/ By contrast, a number of members that have not formally accepted the obligations of Article VIII, Sections 2, 3, and 4, no longer maintain any exchange restrictions. This blurring is reinforced when account is taken of trade policies, as a few of the Article VIII members maintain extensive quantitative trade and other current account restrictions and high and discriminatory tariffs that reduce the efficacy of exchange liberalization. Moreover, most developing countries still have to achieve capital account convertibility. As a result of remaining restrictions, many developing members (including members that have accepted the obligations of Article VIII as well as members that have not) appear to continue to have parallel exchange markets with exchange rate quotations that differ significantly from the official exchange rate. 2/

The transition countries of central and eastern Europe and the former Soviet Union, have generally advanced rapidly toward current account convertibility as part of the overall reform process. By contrast, some of them consider capital convertibility as an objective for the longer term, once the transition toward a market economy has already taken hold.

1. Industrial countries

All 23 members defined as industrial countries by the IMF have accepted the obligations of Article VIII, Sections 2, 3, and 4 (Table 1); 3/ and they actually maintain no exchange restrictions on current international transactions. They deal with current account adjustment problems by adjusting domestic demand policies and/or the exchange rate.

1/ An internal review in March 1992 found that 20 Article VIII members with current access to Fund resources had unapproved exchange restrictions and/or bilateral payments agreements. Another 16 Article VIII members had approved restrictions.

2/ Parallel exchange markets generally arise from exchange and trade restrictions including, especially, exchange restrictions on capital account. To the extent that these parallel rates are officially sanctioned and result from current account exchange restrictions, they fall under the jurisdiction of the Fund.

3/ The definitions of country classifications for analytical purposes are routinely presented in the statistical appendix to the World Economic Outlook publications of the Fund.

Table 1. Members That Have Accepted the Obligations of Article VIII, Sections 2, 3, and 4 of the Articles of Agreement, By Year of Acceptance (as of end-1995) 1/

Year	Countries (In parentheses, length of stay under Article XIV status, in years)
1946	El Salvador (--) Mexico (1) Panama (--) United States (1)
1947	Guatemala (2)
1948-49	--
1950	Honduras (5)
1951	--
1952	Canada (7)
1953	Dominican Republic (8) Haiti (--)
1954-60	--
1961	Belgium (16) France (16) Germany (9) Ireland (4) Italy (14) Luxembourg (16) Netherlands (16) Peru (16) Saudi Arabia (4) Sweden (10) United Kingdom (16)
1962	Austria (14)
1963	Jamaica (--) Kuwait (1)
1964	Japan (12) Nicaragua (18)
1965	Australia (18) Costa Rica (19)
1966	Guyana (--)

Table 1 (continued). Members That Have Accepted the Obligations
of Article VIII, Sections 2, 3, and 4 of the Articles
of Agreement, By Year of Acceptance (as of end-1995) 1/

Year	Countries (In parentheses, length of stay under Article XIV status, in years)
1967	Bolivia (22) Denmark (21) Norway (22)
1968	Argentina (12) Malaysia (10) Singapore (2)
1969	--
1970	Ecuador (25)
1971	--
1972	Fiji (1)
1973	The Bahamas (--) Bahrain (1) Qatar (1) South Africa (28)
1974	Oman (3) United Arab Emirates (2)
1975	Papua New Guinea (--)
1976	Venezuela (30)
1977	Chile (32)
1978	Seychelles (1) Suriname (--)
1979	Dominica (1) Finland (31) Solomon Islands (1)
1980	Djibouti (2) St. Lucia (1) Uruguay (34)
1981	St. Vincent (2)

Table 1. (continued). Members That Have Accepted the Obligations of Article VIII, Sections 2, 3, and 4 of the Articles of Agreement, By Year of Acceptance (as of end-1995) 1/

Year	Countries (In parentheses, length of stay under Article XIV status, in years)
1982	New Zealand (21) Vanuatu (1)
1983	Antigua and Barbuda (1) Belize (1) Iceland (38)
1984	St. Kitts and Nevis (--)
1985	--
1986	Kiribati (--) Spain (28)
1987	--
1988	Indonesia (21) Korea (33) Portugal (27)
1989	Swaziland (20)
1990	Thailand (41) Turkey (43)
1991	Cyprus (30) Tonga (6)
1992	Greece (47) Republic of the Marshall Islands (--) San Marino (--) Switzerland (--)
1993	Barbados (23) Gambia, The (26) Israel (39) Lebanon (46) Mauritius (25) Micronesia (--) Morocco (35) Trinidad and Tobago (30) Tunisia (35)

Table 1 (concluded). Members That Have Accepted the Obligations of Article VIII, Sections 2, 3, and 4 of the Articles of Agreement, By Year of Acceptance (as of end-1995) 1/

Year	Countries (In parentheses, length of stay under Article XIV status, in years)
1994	Bangladesh (22) Estonia (2) Ghana (37) Grenada (19) India (49) Kenya (30) Latvia (2) Lithuania (2) Malta (26) Nepal (33) Pakistan (44) Paraguay (49) Sri Lanka (44) Uganda (31) Western Samoa (23)
1995 <u>2/</u>	Botswana (27) Brunei Darussalam (--) Croatia (50) <u>3/</u> Czech Republic (5) <u>4/</u> Guinea (32) Jordan (43) Kyrgyz Republic (3) Malawi (30) Moldova (3) Philippines (50) Poland (9) Sierra Leone (33) Slovak Republic (5) <u>4/</u> Slovenia (50) <u>3/</u> Zimbabwe (15)

Source: IMF, internal records.

1/ 113 members out of 181 members of the Fund. See also footnote 2.

2/ Through end-1995. Hungary became the 114 member that accepted Article VIII in January 1996, and Mongolia became number 115 in February 1996.

3/ Croatia and Slovenia succeeded to the membership of the Socialist Federal Republic of Yugoslavia (original member, 1945) as of December 14, 1992.

4/ The Czech Republic and the Slovak Republic succeeded to the membership of Czechoslovakia (member since 1990) on January 1, 1993.

The situation with regard to trade restrictions is somewhat different. A retrogression in this area took place in the 1980s as a result of protectionist policies in a number of countries (Kelly, Kirmani, et al., 1988, chapter I). Thus, although tariffs remained at historically low levels, nontariff barriers generally intensified; the share of trade covered by such measures increased in the United States and the EU during the 1980s. 1/ As a result of the delay in the Uruguay Round multilateral negotiations, trade liberalization in industrial countries proceeded largely in the context of regional trade arrangements (Kelly, McGuirk, et al., 1992, Chapter III). This situation has changed significantly, however, with the conclusion of the Uruguay Round negotiations in late 1994 and with the establishment of the World Trade Organization in January 1995.

Exchange controls on capital transactions (both inflows and outflows) have been removed in all industrial countries, although in some of them this occurred only recently. 2/ Canada, Switzerland and the United States had long provided a liberal regulatory framework for capital transactions, although there were temporary exceptions. A significant shift toward industrial country liberalization was initiated with the rapid removal of controls by the United Kingdom (1979), Australia (1983), and New Zealand (1984), and the completion of gradual liberalization by Japan (1980) and Germany (1981). 3/ A final impetus toward liberalization was provided by the ratification of the Single European Act (1987) and the Second Capital Markets Liberalization Directive (1988) and by the latest OECD Code of Liberalization of Capital Movements (1989). 4/ The following EU members promptly accepted capital convertibility: Netherlands (1986), Denmark (1988), France (1989), Belgium, Italy, and Luxembourg (1990). Several members of the European Free Trade Association (EFTA) followed suit: Sweden (1989), Austria, Finland, and Norway (1990). 5/ The remaining EU members concluded liberalization in accordance with more distant EU deadlines: Ireland, Portugal, and Spain (1992), Greece (1994) and Iceland (1995) 6/

1/ See IMF, 1992, pp. 31-32; and IMF, 1993a, p. 73.

2/ For an overview of experience with capital account liberalization in industrial countries see Quirk, Cortés, et al (1995, pp. 11-12), and Quirk, Evans, et al (1995, Chapter III).

3/ For a detailed account of the experience of the United Kingdom and New Zealand, see Mathieson and Rojas-Suárez (1993, pp. 22-23).

4/ For a review of the OECD and EU codes of conduct, see Quirk, Evans, et al (1995, Chapter V).

5/ Flickenschild, Gilman, et al (1992, pp. 27-29).

6/ Some controls on certain short-term capital flows were reinforced in Ireland and Portugal, and reintroduced in Spain, in the aftermath of the European exchange rate market instability that began in September 1992. However, these countries lifted all capital restrictions by the year-end 1992 deadline agreed with the EU. (See IMF, 1993b, pp. 17-18, and IMF, 1993c, Chapter V).

In accordance with the removal of capital controls, all industrial countries have now removed repatriation and surrender requirements for foreign exchange. This contrasts with the situation at end-1986 when these requirements were still in force in 10 industrial countries (Quirk, Hacche, et al., 1988, p.7).

One of the visible results of the removal of exchange restrictions on both current account and capital transactions in industrial countries has been the complete disappearance of parallel markets for foreign exchange, with the official and parallel rates rapidly tending to converge in the period 1987-95 in those few countries that were still eliminating remaining capital restrictions. (Table 2.) 1/

Consistent with the liberalization of capital movements, all industrial countries now use indirect monetary policy instruments and allow interest rates to be determined by market forces. This is a necessary complement to the liberalization of capital controls to ensure that interest rate differentials are freely interacting with exchange rate risk to prevent destabilizing capital movements.

The liberalization of capital controls in industrial countries has been as much the result of market pressures (associated with technological and financial innovations) as of policy design. In an increasingly integrated and interdependent world, the national authorities not only recognized the efficiency benefits of free capital movements but also found it increasingly costly and difficult to implement any remaining restrictions (Mathieson and Rojas-Suárez, 1993). In particular, strong pressure arose in countries with capital controls to liberalize them, so as to avoid losing market share to offshore financial centers and to countries with less restrictions. Thus, beginning in the 1970s, the world saw an unprecedented increase in the volume of both gross and net capital flows, an increasing integration between offshore (international) and domestic financial markets, and a rise in the proportion of private capital flows. This happened despite the fact

1/ For lack of an alternative, Table 2 uses "parallel" market data from a private source (ICA), whose accuracy cannot be checked directly. (See further commentary on the ICA source at the end of that table). More important, it must be emphasized that neither the "parallel" rates nor the calculated premiums over the Fund's IFS rates contained therein, have any standing in relation to the determination of whether there is or not a "multiple" rate in a given country from the Fund's jurisdictional point of view. The data in Table 2 are used here only to convey a general impression of possible market trends. In the case of countries which no longer have any parallel exchange markets, the "parallel" rates quoted in the ICA source are interbank exchange rates, which can exhibit small differences with regard to the daily average ("official") rates, just as some bureau or other agency's market rates can show small differences from the bank rates.

Table 2. Official and "Parallel" Exchange Rates
in Article VIII Countries, 1987-1995 ^{1/}
(End-of-period U.S. dollar rates)

	1987	1988	1989	1990	1991	1992	1993	1994	July 1995
<u>Argentina</u>									
Official rate	0.00038	0.00134	0.17950	0.55850	0.99850	0.99050	0.99850	0.99950	1.00000
Parallel rate	0.00055	0.00200	0.36500	0.79500	1.11000	1.10000	1.10	1.01	1.00
Premium	44.7	49.3	103.3	42.3	11.2	11.1	10.2	1.1	--
<u>Australia</u>									
Official rate ^{2/}	0.7225	0.8555	0.7927	0.7733	0.7598	0.6886	0.6771	0.7768	0.7389
Parallel rate ^{2/}	0.71	0.84	0.79	0.77	0.76	0.68	0.671	0.774	0.730
Premium	1.8	1.8	0.3	0.4	--	1.3	0.9	0.4	1.2
<u>Austria</u>									
Official rate	11.250	12.565	11.815	10.677	10.689	11.354	12.143	11.095	9.719
Parallel rate	11.55	12.60	12.20	10.70	10.90	11.40	12.18	11.10	9.78
Premium	2.7	0.3	3.3	0.2	0.2	0.4	0.3	--	0.6
<u>The Bahamas</u>									
Official rate ^{3/}	1.0000	1.0000	1.0000	1.0000	1.0000	1.0000	1.0000	1.0000	1.0000
Parallel rate	1.09	1.12	1.15	1.11	1.15	1.10	1.10	1.05	1.03
Premium	9.0	12.0	15.0	11.0	15.0	10.0	10.0	5.0	3.0
<u>Bahrain</u>									
Official rate ^{4/}	2.6596	2.6596	2.6596	2.6596	2.6596	2.6596	2.6596	2.6596	2.6596
Parallel rate ^{4/}	2.57	2.59	2.62	2.58	2.63	2.58	2.60	2.58	2.61
Premium	3.5	2.7	1.5	3.1	1.1	3.1	2.3	3.0	1.9
<u>Bangladesh</u>									
Official rate	31.200	32.270	32.270	35.790	38.580	39.000	39.850	40.250	40.100
Parallel rate	97.00	135.00	100.00	95.00	110.00	83.00	58.00	58.50	51.15
Premium	210.9	318.3	209.9	165.4	185.1	112.8	45.5	45.3	27.6
<u>Barbados</u>									
Official rate	2.0113	2.0113	2.0113	2.0113	2.0113	2.0113	2.0113	2.0113	2.0113
Parallel rate	2.08	2.33	2.30	2.20	2.32	2.30	2.10	2.06	2.02
Premium	3.4	15.8	14.4	9.4	15.3	14.4	4.4	2.4	0.4
<u>Belgium</u>									
Official rate ^{5/}	33.153	37.345	35.760	30.983	31.270	33.180	36.110	31.838	28.400
Parallel rate	34.40	37.70	36.25	31.10	32.10	33.35	36.25	32.00	28.85
Premium	3.8	1.0	1.4	0.4	2.7	0.5	0.4	0.5	1.6
<u>Belize</u>									
Official rate	2.0000	2.0000	2.0000	2.0000	2.0000	2.0000	2.000	2.000	2.000
Parallel rate	3.33	2.50	2.47	2.50	2.30	2.38	3.05	2.15	2.08
Premium	66.5	25.0	23.5	25.0	15.0	19.0	52.5	7.5	4.0
<u>Bolivia</u>									
Official rate	2.2100	2.4700	2.9800	3.4000	3.7450	4.0950	4.4750	4.6950	4.8150
Parallel rate	2.35	2.95	3.00	3.45	3.95	4.11	4.50	4.70	4.88
Premium	6.3	19.4	0.7	1.5	5.5	0.4	0.6	0.1	1.3
<u>Botswana</u>									
Official rate ^{6/}	0.6387	0.5166	0.5341	0.5344	0.4825	0.4431	0.3899	0.3680	0.3619
Parallel rate ^{6/}	0.48	0.43	0.49	0.50	0.42	0.38	0.337	0.321	0.3599
Premium	33.1	20.1	9.0	6.9	14.9	16.6	15.7	14.6	0.6

Table 2 (continued). Official and "Parallel" Exchange Rates
in Article VIII Countries 1/
(End-of-period U.S. dollar rates)

	1987	1988	1989	1990	1991	1992	1993	1994	July 1995
<u>Brunei Darussalam</u>									
Official rate	1.9985	1.9462	1.8944	1.7445	1.6305	1.6449	1.6080	1.4607	...
Parallel rate	2.09	2.09	1.97	1.78	1.69	1.68	1.66	1.52	1.42
Premium	4.5	7.4	4.0	2.0	3.6	2.1	3.2	4.1	...
<u>Canada</u>									
Official rate	1.2998	1.1927	1.1578	1.1603	1.1556	1.2711	1.3240	1.4028	1.3697
Parallel rate	1.31	1.21	1.18	1.18	1.16	1.29	1.33	1.41	1.37
Premium	0.8	1.5	1.9	1.7	0.4	1.5	0.5	0.5	--
<u>Chile</u>									
Official rate	238.14	247.20	297.37	337.09	374.51	382.12	428.47	402.92	381.04
Parallel rate	285.00	350.00	355.00	400.00	405.00	402.00	440.00	440.00	418.00
Premium	19.7	41.6	19.4	18.7	8.1	5.2	2.7	9.2	9.7
<u>Costa Rica</u>									
Official rate	69.25	79.50	84.35	103.55	135.43	137.43	151.44	165.07	181.96
Parallel rate	91.00	110.00	98.00	120.00	147.00	143.00	157.00	165.00	184.00
Premium	31.4	38.4	16.2	15.9	8.5	4.1	3.7	--	1.1
<u>Croatia</u>									
Official rate	...	...	...	...	...	...	6.562	5.629	5.007
Parallel rate	...	...	...	...	...	...	8.500	10.00	8.69
pREMIUM	...	...	...	...	...	...	29.5	77.7	73.6
<u>Cyprus</u>									
Official rate 7/	2.2785	2.1445	2.0885	2.3010	2.2777	2.0702	1.9238	2.0998	2.2918
Parallel rate 7/	2.18	2.09	1.99	2.20	2.10	2.05	1.90	2.00	2.220
Premium	4.5	2.6	4.9	4.6	8.5	1.0	1.3	5.0	3.2
<u>Czech Republic</u>									
Official rate 8/	...	...	...	...	...	...	29.955	28.049	25.963
Parallel rate 8/	28.60	45.75	43.00	45.00	34.00	38.00	38.00	28.90	27.85
Premium	...	...	...	...	...	...	26.9	3.0	7.3
<u>Denmark</u>									
Official rate	6.097	6.874	6.608	5.776	5.914	6.256	6.773	6.083	5.372
Parallel rate	6.30	7.00	6.85	5.80	6.10	6.30	6.80	6.12	5.40
Premium	3.3	1.8	3.7	0.4	3.1	0.7	0.4	0.6	0.5
<u>Djibouti</u>									
Official rate	177.72	177.72	177.72	177.72	177.72	177.72	177.72	177.72	177.72
Parallel rate	208.00	202.00	210.00	198.00	198.00	210.00	212.00	212.00	198.00
Premium	17.0	13.7	18.2	11.4	11.4	18.2	19.3	19.3	11.4
<u>Dominican Republic</u>									
Official rate	4.960	6.340	6.340	11.350	12.660	12.575	12.767	13.064	13.798
Parallel rate	5.25	7.20	10.50	17.15	14.30	13.00	12.90	13.90	14.10
Premium	5.8	13.6	65.6	51.1	13.0	3.4	1.0	6.4	2.2
<u>(ECCB Dollar) 9/</u>									
Official rate	2.7000	2.7000	2.7000	2.7000	2.7000	2.7000	2.7000	2.7000	2.7000
Parallel rate	3.25	3.23	3.00	2.85	2.90	2.96	2.85	2.83	2.72
Premium	20.4	20.0	11.1	5.6	7.4	9.6	5.6	4.8	0.7

Table 2 (continued). Official and "Parallel" Exchange Rates
in Article VIII Countries, 1987-1995 1/
(End-of-period U.S. dollar rates)

	1987	1988	1989	1990	1991	1992	1993	1994	July 1995
<u>Ecuador</u>									
Official rate	221.50	432.51	648.42	878.20	1270.58	1844.30	2043.8	2269.00	2578.00
Parallel rate	290.00	595.00	750.00	1110.00	1520.00	1935.00	2050.00	2400.00	2695.00
Premium	30.9	37.6	15.7	26.4	19.6	4.9	0.3	5.8	4.5
<u>El Salvador</u>									
Official rate	5.0000	5.0000	5.0000	8.0300	8.0800	9.1700	8.670	8.750	8.755
Parallel rate	10.00	14.75	9.25	9.95	8.69	10.35	10.20	10.65	9.70
Premium	100.0	195.0	85.0	23.9	7.5	12.9	17.6	21.7	10.8
<u>Estonia</u>									
Official rate	...	...	...	...	...	12.912	13.878	12.390	11.051
Parallel rate	...	...	...	...	...	...	17.00	15.40	14.35
Premium	...	...	...	...	...	...	22.5	24.3	29.9
<u>Fiji</u>									
Official rate	1.4405	1.4049	1.4939	1.4592	1.4728	1.5645	1.5408	1.4090	1.3847
Parallel rate <u>10/</u>	0.58	0.63	0.67	0.66	0.68	0.64	0.641	0.702	0.719
Premium	19.7	13.0	--	3.8	-0.2	-0.1	1.3	1.1	0.4
<u>Finland</u>									
Official rate	3.9460	4.1690	4.0590	3.6340	4.1330	5.2450	5.7845	4.7432	4.1924
Parallel rate	4.01	4.20	4.17	3.65	4.20	5.27	5.83	4.79	4.23
Premium	1.6	0.7	2.7	0.4	1.6	0.5	0.8	1.0	0.9
<u>France</u>									
Official rate	5.3400	6.0590	5.7880	5.1290	5.1800	5.5065	5.8955	5.3460	4.7670
Parallel rate	5.55	6.15	6.10	5.14	5.25	5.52	5.92	5.39	4.84
Premium	3.9	1.5	5.4	2.1	1.4	0.2	0.4	0.8	1.5
<u>Gambia, The</u>									
Official rate	6.439	6.659	8.315	7.495	8.957	9.217	9.535	9.579	9.550
Parallel rate <u>11/</u>	0.12	0.11	0.14	0.13	0.12	0.11	0.108	0.108	0.090
Premium	29.4	36.5	-14.1	2.6	-7.0	-1.4	-2.9	-3.3	16.3
<u>Germany</u>									
Official rate	1.5815	1.7803	1.6978	1.4940	1.5160	1.6140	1.7263	1.5488	1.3805
Parallel rate	1.64	1.79	1.72	1.50	1.57	1.62	1.74	1.57	1.39
Premium	3.7	0.5	1.3	0.4	3.6	0.4	0.8	1.4	0.7
<u>Ghana</u>									
Official rate	176.06	229.89	303.03	344.83	390.63	520.83	819.67	1052.63	...
Parallel rate	227.00	310.00	355.00	370.00	389.00	580.00	805.00	1040.00	1214.00
Premium	28.9	34.8	17.2	7.3	-0.4	11.4	-1.8	-1.2	...
<u>Greece</u>									
Official rate	125.93	148.10	157.79	157.63	175.28	214.58	249.22	240.10	223.95
Parallel rate	138.60	160.00	170.00	162.00	180.00	217.00	250.00	241.00	226.00
Premium	10.0	8.0	7.7	2.8	2.7	1.1	0.3	0.4	0.9
<u>Guatemala</u>									
Official rate <u>12/</u>	2.5000	2.7050	3.4000	5.0146	5.0434	5.2743	5.8152	5.6485	5.7777
Parallel rate	3.32	3.45	3.72	6.90	5.45	5.50	6.25	6.16	5.56
Premium	32.8	27.5	9.4	37.6	8.1	4.3	7.5	9.1	-3.8

Table 2 (continued). Official and "Parallel" Exchange Rates
in Article VIII Countries, 1987-1995 1/
(End-of-period U.S. dollar rates)

	1987	1988	1989	1990	1991	1992	1993	1994	July 1995
<u>Guinea</u>									
Official rate	...	550.0	620.0	680.0	803.0	922.4	972.4	981.0	995.1
Parallel rate	490.00	585.00	585.00	765.00	825.00	995.00	1180.00	1025.00	1015.00
Premium	...	6.4	-5.6	12.5	2.7	7.9	21.3	4.5	2.0
<u>Guyana</u>									
Official rate	10.0	10.0	33.0	45.0	122.0	126.0	130.80	142.50	142.50
Parallel rate	51.00	53.00	62.0	105.0	168.0	172.00	148.00	160.00	150.00
Premium	410.0	430.0	87.9	133.3	37.7	36.5	13.1	12.3	5.3
<u>Haiti</u>									
Official rate	5.00	5.00	5.00	5.00	8.240	10.953	12.805	12.947	15.017
Parallel rate	11.00	12.55	16.75	20.00	12.90	19.50	30.25	40.00	27.00
Premium	120.0	151.0	235.0	300.0	56.6	78.0	136.2	208.9	79.8
<u>Honduras</u>									
Official rate	2.0000	2.0000	2.0000	2.0000	5.4000	5.8300	7.2600	9.4001	9.5035
Parallel rate	2.85	3.70	4.40	6.85	6.25	6.10	7.60	9.40	9.35
Premium	42.5	85.0	120.0	242.5	15.7	4.6	4.7	--	-1.6
<u>Iceland</u>									
Official rate	35.660	46.220	61.170	55.390	55.620	63.920	72.730	68.300	62.780
Parallel rate	35.00	48.50	62.00	57.00	59.00	66.00	77.25	69.50	63.00
Premium	-1.9	4.9	1.4	2.9	6.1	3.3	6.2	1.8	0.4
<u>India</u>									
Official rate	12.877	14.949	17.035	18.073	25.834	26.200	31.380	31.380	31.400
Parallel rate	14.55	17.00	19.00	19.80	28.00	32.30	31.45	31.60	35.00
Premium	13.0	13.7	11.5	9.6	8.4	23.3	0.2	0.7	11.5
<u>Indonesia</u>									
Official rate	1650.0	1731.0	1797.0	1901.0	1992.0	2062.0	2110.0	2200.0	2256.0
Parallel rate	1900.00	2000.00	1850.00	1950.00	2000.00	2400.00	2155.00	2225.00	2240.00
Premium	15.2	15.5	2.9	2.6	0.4	16.4	2.1	1.1	-0.7
<u>Ireland</u>									
Official rate <u>13/</u>	1.6755	1.5075	1.5563	1.7755	1.7498	1.6294	1.4108	1.5471	1.6492
Parallel rate <u>13/</u>	1.60	1.49	1.55	1.75	1.71	1.63	1.400	1.539	1.639
Premium	4.7	1.2	0.4	1.5	2.3	--	0.8	0.5	0.6
<u>Israel</u>									
Official rate	1.5386	1.6850	1.9630	2.0480	2.2830	2.7640	2.9860	3.0180	2.9890
Parallel rate	1.70	1.98	1.99	2.12	2.30	2.75	2.99	3.04	2.99
Premium	10.5	17.5	1.4	3.5	0.7	-0.5	0.1	0.7	--
<u>Italy</u>									
Official rate	1169.3	1305.8	1270.5	1130.2	1151.1	1470.9	1704.0	1629.7	1584.5
Parallel rate	1217.00	1320.00	1315.00	1187.00	1195.00	1480.00	1717.00	1630.00	1596.00
Premium	4.1	1.1	3.5	5.0	3.8	0.6	0.8	--	0.7
<u>Jamaica</u>									
Official rate	5.500	5.480	6.480	8.038	21.493	22.185	32.475	33.202	34.118
Parallel rate	6.50	6.70	8.30	10.20	23.00	24.75	33.00	34.25	35.00
Premium	18.2	22.3	28.1	26.9	7.0	11.6	1.6	3.2	2.6

Table 2 (continued). Official and "Parallel" Exchange Rates
in Article VIII Countries, 1987-1995 1/
(End-of-period U.S. dollar rates)

	1987	1988	1989	1990	1991	1992	1993	1994	July 1995
<u>Japan</u>									
Official rate	123.50	125.85	143.45	134.40	125.20	124.75	111.85	99.74	88.43
Parallel rate	128.70	126.25	144.00	136.00	127.00	125.25	112.00	99.90	88.50
Premium	4.2	0.3	0.4	1.2	1.4	0.4	0.1	0.2	--
<u>Jordan</u>									
Official rate <u>14/</u>	3.0395	2.0964	1.5432	1.5038	1.4815	1.4472	1.4205	1.4265	1.4327
Parallel rate <u>14/</u>	2.77	1.90	1.47	1.35	1.42	1.37	1.42	1.42	1.43
Premium	9.7	10.3	5.0	11.4	4.3	5.6	--	0.5	0.2
<u>Kenya</u>									
Official rate	16.515	18.599	21.601	24.084	28.074	36.216	68.163	44.839	55.833
Parallel rate	20.0	21.00	22.50	25.50	30.50	75.00	90.00	49.00	55.85
Premium	21.1	5.4	4.2	5.9	8.6	7.1	32.0	9.3	--
<u>Korea</u>									
Official rate	792.30	684.10	679.60	716.40	760.80	788.40	808.10	788.70	756.50
Parallel rate	890.00	750.00	680.00	725.00	762.00	820.00	830.00	792.00	800.0
Premium	12.3	9.6	0.1	1.2	0.2	4.0	2.7	0.4	5.8
<u>Kuwait</u>									
Official rate <u>15/</u>	3.7051	3.5384	3.4250	...	3.5178	3.3036	3.3510	3.3320	3.3328
Parallel rate <u>15/</u>	3.61	3.40	3.34	...	3.42	3.22	3.27	3.32	3.32
Premium	2.6	4.1	2.5	...	2.9	2.6	2.5	0.4	0.4
<u>Kyrgyz Republic</u>									
Official rate	...	...	...	...	...	...	...	...	...
Parallel rate	...	...	...	...	...	...	8.00	11.50	...
Premium	...	...	...	...	...	...	...	...	...
<u>Latvia</u>									
Official rate	...	...	...	...	...	0.835	0.595	0.548	0.515
Parallel rate	...	...	...	...	...	...	0.62	0.59	...
Premium	...	...	...	...	...	...	4.2	7.7	...
<u>Lebanon</u>									
Official rate	455.0	530.0	505.0	842.0	879.0	1838.0	1711.0	1647.0	1616.5
Parallel rate	690.00	590.00	555.00	900.00	880.00	2000.00	1740.00	1655.00	2100.00
Premium	51.6	11.3	9.9	6.9	0.1	8.8	1.7	0.5	29.9
<u>Lithuania</u>									
Official rate	...	...	...	...	...	3.790	3.900	4.000	4.000
Parallel rate	...	...	...	...	...	...	5.00	4.60	4.50
Premium	...	...	...	...	...	...	28.2	15.0	12.5
<u>Luxembourg</u>									
Official rate	33.153	37.345	35.760	30.983	31.270	33.180	36.110	31.838	28.400
Parallel rate	34.40	38.80	37.70	31.50	33.00	34.45	36.55	32.30	28.87
Premium	3.8	3.9	5.4	1.7	5.5	3.8	1.2	1.5	1.7
<u>Malawi</u>									
Official rate	2.0538	2.5355	2.6788	2.6469	2.6638	4.3958	4.4944	15.2986	15.2749
Parallel rate <u>16/</u>	0.43	0.31	0.28	0.33	0.26	0.17	0.169	0.060	0.060
Premium	13.2	27.2	33.3	14.5	44.4	33.8	31.7	8.9	9.1

Table 2 (continued). Official and "Parallel" Exchange Rates
in Article VIII Countries, 1987-1995 1/
(End-of-period U.S. dollar rates)

	1987	1988	1989	1990	1991	1992	1993	1994	July 1995
<u>Malaysia</u>									
Official rate	2.4928	2.7153	2.7033	2.7015	2.7240	2.6120	2.7015	2.5600	2.4575
Parallel rate	2.59	2.78	2.69	2.70	2.74	2.60	2.68	2.57	2.49
Premium	3.9	2.4	-0.4	-0.1	0.6	-0.5	-0.8	0.4	1.3
<u>Malta</u>									
Official rate <u>17/</u>	3.2081	3.0107	2.9686	3.3249	3.2724	2.6725	2.5309	2.7166	2.9105
Parallel rate <u>17/</u>	3.00	2.94	2.87	3.25	3.10	2.65	2.50	2.70	2.8596
Premium	6.9	2.4	3.4	2.3	5.6	0.8	1.2	0.6	1.8
<u>Mauritius</u>									
Official rate	12.175	13.834	14.996	14.322	14.794	16.998	18.656	17.863	16.958
Parallel rate	13.00	14.20	16.20	15.45	16.35	17.80	18.70	18.10	17.85
Premium	6.8	2.6	8.0	7.9	10.5	4.7	0.2	1.3	5.3
<u>Mexico</u>									
Official rate	2209.7	2281.0	2641.0	2945.4	3071.0	3115.4	3.1059	5.3250	6.0882
Parallel rate	2857.00	2630.00	2935.00	3145.00	3125.00	3180.00	3.15	5.38	6.18
Premium	29.3	15.3	11.1	6.8	17.6	2.1	1.4	1.0	1.5
<u>Moldova</u>									
Official rate	...	...	...	...	...	0.4145	3.6400	4.2700	4.5337
Parallel rate	...	...	...	...	...	...	...	4.30	...
Premium	...	...	...	...	...	...	...	0.7	...
<u>Morocco</u>									
Official rate	7.800	8.211	8.122	8.043	8.150	9.049	9.651	8.960	8.284
Parallel rate	8.20	8.55	9.50	9.10	9.00	9.10	9.68	9.15	8.25
Premium	5.1	4.1	17.0	13.1	10.4	0.6	0.3	2.1	-0.4
<u>Nepal</u>									
Official rate	21.600	25.200	28.600	30.400	42.700	43.200	49.240	49.880	51.010
Parallel rate	24.45	40.50	42.00	35.25	56.00	65.00	64.00	67.00	60.00
Premium	13.2	60.7	46.9	16.0	31.1	50.5	30.0	34.3	17.6
<u>Netherlands</u>									
Official rate	1.7775	1.9995	1.9155	1.6900	1.7104	1.8141	1.9409	1.7351	1.5448
Parallel rate	1.84	2.02	2.00	1.70	1.75	1.82	1.95	1.74	1.56
Premium	3.5	1.0	4.4	0.6	2.3	0.3	0.5	0.3	1.0
<u>New Zealand</u>									
Official rate <u>18/</u>	0.6575	0.6283	0.5972	0.5878	0.5411	0.5143	0.5588	0.6425	0.6740
Parallel rate <u>18/</u>	0.67	0.63	0.59	0.56	0.54	0.51	0.558	0.639	0.668
Premium	-1.9	-0.3	1.2	5.0	0.2	0.8	0.1	0.5	0.1
<u>Nicaragua</u>									
Official rate <u>19/</u>	14.00	184.00	7.63	600.00	5.00	5.0	6.35	7.11	...
Parallel rate <u>19a/</u> [20000]	[3000]	[3000]	[40000]	[3000000]	6.95	6.35	7.25	7.25	7.62
Premium	...	...	...	...	39.0	27.0	14.2	2.0	...
<u>Norway</u>									
Official rate	6.2325	6.5700	6.6150	5.9075	5.9730	6.9245	7.5180	6.7620	6.1230
Parallel rate	6.35	6.60	6.78	5.95	6.05	6.95	7.52	6.79	6.21
Premium	1.9	0.5	2.5	0.7	1.3	0.4	--	0.4	1.4

Table 2 (continued). Official and "Parallel" Exchange Rates
in Article VIII Countries, 1987-1995 1/
(End-of-period U.S. dollar rates)

	1987	1988	1989	1990	1991	1992	1993	1994	July 1995
<u>Oman</u>									
Official rate	0.3845	0.3845	0.3845	0.3845	0.3845	0.3845	0.3845	0.3845	0.3845
Parallel rate <u>20/</u>	2.49	2.54	2.56	2.52	2.52	2.51	2.53	2.53	2.560
Premium	4.4	2.4	1.6	3.2	3.2	3.6	2.8	2.8	1.6
<u>Pakistan</u>									
Official rate	17.450	18.650	21.420	21.900	24.720	25.700	30.120	30.800	31.190
Parallel rate	20.70	20.50	21.50	25.00	25.10	29.10	30.90	31.00	33.00
Premium	18.6	9.9	0.4	14.2	1.5	13.2	2.6	0.6	5.8
<u>Papua New Guinea</u>									
Official rate <u>21/</u>	1.1384	1.2100	1.1633	1.0493	1.0498	1.0127	1.0190	0.8485	0.7410
Parallel rate <u>21/</u>	1.09	1.09	1.10	1.04	0.92	0.86	0.877	0.794	0.727
Premium	4.4	11.0	5.8	0.9	14.1	17.8	16.2	6.9	19.3
<u>Paraguay</u>									
Official rate	550.0	550.0	1218.0	1258.0	1380.0	1630.0	1880.0	1940.0	1970.0
Parallel rate	1111.00	1250.0	1590.00	1600.00	1470.00	1825.00	2000.00	2250.00	2215.00
Premium	102.0	127.3	30.5	27.2	6.5	12.0	6.4	16.0	12.4
<u>Peru</u>									
Official rate <u>22/</u>	33	500	5261	516.9	960.0	1630.0	2.160	2.180	2.220
Parallel rate <u>22/</u>	125	1700.00	15000.00	600.0	1060.0	1820.0	2.24	2.21	2.28
Premium	278.8	240.0	185.1	16.1	10.4	11.7	3.7	1.4	2.7
<u>Philippines</u>									
Official rate	20.800	21.335	22.440	28.000	26.650	25.096	27.699	24.418	25.585
Parallel rate	22.50	22.00	23.23	30.00	27.50	25.70	28.00	24.55	28.00
Premium	8.2	3.1	3.5	7.1	3.2	2.4	1.1	0.5	9.4
<u>Poland</u>									
Official rate	0.0316	0.0503	0.6500	0.9500	1.0957	1.5767	2.1344	2.4372	2.3685
Parallel rate	0.1300	0.3200	1.025	1.0350	1.2750	2.3100	2.1500	2.4500	2.41
Premium	311.4	536.2	57.7	8.9	16.4	46.5	0.7	0.5	1.8
<u>Portugal</u>									
Official rate	129.87	146.37	149.84	133.60	134.18	146.76	176.81	159.09	144.35
Parallel rate	151.00	165.00	157.00	138.00	142.00	147.50	178.00	160.75	150.00
Premium	16.3	12.7	4.8	3.3	5.8	0.5	0.7	1.0	3.9
<u>Qatar</u>									
Official rate	3.6400	3.6400	3.6400	3.6400	3.6400	3.6400	3.6400	3.6400	3.6400
Parallel rate	3.74	3.79	3.70	3.79	3.71	3.70	3.75	3.70	3.65
Premium	2.7	4.1	1.6	4.1	1.9	1.6	3.0	1.6	0.3
<u>Saudi Arabia</u>									
Official rate	3.7450	3.7450	3.7450	3.7450	3.7450	3.7450	3.7450	3.7450	3.7450
Parallel rate	3.84	3.84	3.81	3.85	3.84	3.83	3.78	3.79	3.75
Premium	2.5	2.5	1.7	2.8	2.5	2.2	0.9	1.2	0.1
<u>Seychelles</u>									
Official rate	5.1435	5.3966	5.4672	5.1188	5.0627	5.2545	5.2579	4.9695	4.6530
Parallel rate	5.75	5.65	6.00	5.80	5.30	5.33	5.48	5.70	5.44
Premium	11.8	4.7	9.7	13.3	4.7	1.4	4.2	14.7	16.9

Table 2 (continued). Official and "Parallel" Exchange Rates
in Article VIII Countries, 1987-1995 1/
(End-of-period U.S. dollar rates)

	1987	1988	1989	1990	1991	1992	1993	1994	July 1995
<u>Sierra Leone</u>									
Official rate	23.04	39.06	65.36	188.68	434.78	526.32	577.63	613.01	783.02
Parallel rate <u>23/</u>	0.020	0.0017	0.0025	0.002	0.0016	0.001	675.00	612.00	735.00
Premium	117.0	1406.0	512.0	165.0	43.8	90.0	16.9	-0.1	-6.1
<u>Singapore</u>									
Official rate	1.9985	1.9462	1.8944	1.7445	1.6305	1.6449	1.6080	1.4607	1.3945
Parallel rate	2.09	1.98	1.90	1.78	1.68	1.65	1.61	1.46	1.40
Premium	4.5	1.7	0.2	2.0	3.0	1.4	0.1	--	0.4
<u>Slovak Republic</u>									
Official rate	...	...	...	...	...	...	33.202	31.277	29.194
Parallel rate	...	...	...	...	...	...	50.00	37.50	31.45
Premium	...	...	...	...	...	...	50.6	19.9	7.7
<u>Slovenia</u>									
Official rate	...	...	...	...	56.69	98.70	131.84	126.46	112.85
Parallel rate	...	...	...	...	...	99.00	150.00	165.00	153.00
Premium	...	...	...	...	...	0.3	13.8	30.5	35.6
<u>Solomon Islands</u>									
Official rate	1.9743	2.1182	2.3969	2.6137	2.7949	3.0998	3.2478	3.3289	...
Parallel rate <u>24/</u>	...	...	...	...	...	...	0.27	0.303	0.294
Premium	...	...	...	...	...	...	14.0	-0.9	...
<u>South Africa</u>									
Official rate <u>25/</u>	0.51815	0.42057	0.39432	0.39024	0.36456	0.32755	0.29433	0.28221	0.27401
Parallel rate <u>25/</u>	0.44	0.40	0.39	0.38	0.36	0.32	0.287	0.280	0.26667
Premium	17.8	5.1	1.1	2.7	1.3	5.3	2.6	0.8	2.8
<u>Spain</u>									
Official rate	109.00	113.45	109.72	96.91	96.69	114.62	142.21	131.74	118.59
Parallel rate	115.00	116.00	120.00	99.00	100.00	116.00	143.50	132.70	119.50
Premium	5.5	2.2	9.4	2.2	3.4	1.2	0.7	0.7	0.8
<u>Sri Lanka</u>									
Official rate	30.763	33.033	40.000	40.240	42.580	46.000	49.562	49.980	50.968
Parallel rate	31.50	45.00	48.00	50.00	43.00	52.00	53.25	50.10	51.00
Premium	2.4	36.2	20.0	24.3	1.0	13.0	7.4	0.2	0.1
<u>Suriname</u>									
Official rate	1.7850	1.7850	1.7850	1.7850	1.7850	1.7850	1.7850	409.50	471.00
Parallel rate	12.50	8.55	15.20	16.55	16.00	16.30	85.00	365.00	515.00
Premium	600.3	379.0	751.5	827.2	796.4	813.2	4661.9	-10.9	9.3
<u>Swaziland</u>									
Official rate <u>26/</u>	0.51815	0.42057	0.39432	0.39024	0.36456	0.32754	0.29433	0.28221	0.27628
Parallel rate <u>26/</u>	0.44	0.36	0.35	0.37	0.34	0.27	0.253	0.250	0.260
Premium	17.8	16.8	12.7	5.5	7.2	21.3	16.3	12.9	6.3
<u>Sweden</u>									
Official rate	5.8480	6.1570	6.2270	5.6980	5.5295	7.0430	8.3035	7.4615	7.0590
Parallel rate	5.95	6.16	6.40	5.73	5.70	7.07	8.42	7.49	7.07
Premium	1.7	--	2.8	0.6	3.1	0.4	1.4	0.4	0.2

Table 2 (continued). Official and "Parallel" Exchange Rates
in Article VIII Countries, 1987-1995 1/
(End-of-period U.S. dollar rates)

	1987	1988	1989	1990	1991	1992	1993	1994	July 1995
<u>Switzerland</u>									
Official rate	1.2780	1.5040	1.5465	1.2955	1.3555	1.4560	1.4795	1.3115	1.1461
Parallel rate	1.35	1.52	1.54	1.29	1.36	1.46	1.48	1.32	1.16
Premium	5.6	1.1	-0.4	-0.4	0.3	0.3	--	0.6	1.2
<u>Thailand</u>									
Official rate	25.070	25.240	25.690	25.290	25.280	25.520	25.540	25.090	24.750
Parallel rate	25.90	25.50	27.00	25.80	25.40	25.75	26.50	25.20	24.80
Premium	3.3	1.0	5.1	2.0	0.5	0.9	3.8	0.4	0.2
<u>Tonga</u>									
Official rate	1.3841	1.1703	1.2585	1.2958	1.3317	1.3902	1.3793	1.2584	1.2649
Parallel rate 27/	0.69	0.55	0.70	0.70	0.69	0.59	0.573	0.641	0.715
Premium	4.7	55.4	13.5	10.2	8.8	21.9	26.5	24.0	10.6
<u>Trinidad and Tobago</u>									
Official rate	3.6000	4.2500	4.2500	4.2500	4.2500	4.2500	5.8141	5.9332	5.8800
Parallel rate	5.00	6.69	6.65	5.95	5.52	4.87	6.15	5.90	6.00
Premium	38.9	57.4	56.5	23.5	29.9	14.6	5.8	-0.6	2.0
<u>Tunisia</u>									
Official rate	0.7779	0.8985	0.9046	0.8368	0.8645	0.9507	1.0466	0.9912	0.9126
Parallel rate	0.79	1.01	0.94	0.90	0.93	0.99	1.05	1.00	0.96
Premium	1.6	12.4	3.9	7.6	15.7	4.1	0.3	0.9	5.2
<u>Turkey</u>									
Official rate	1020.9	1814.8	2313.7	2930.1	5079.9	8564.4	14472.5	38726.0	44993.0
Parallel rate	1100.00	1980.00	2350.00	3000.00	5275.00	8825.0	14700.00	38850.00	45500.00
Premium	7.7	9.1	1.6	2.4	3.8	3.0	1.6	0.3	1.1
<u>Uganda</u>									
Official rate	60.0	165.0	370.0	540.0	915.0	1217.2	1130.2	926.8	977.0
Parallel rate	280.00	595.00	618.00	755.00	1000.00	1425.00	1520.00	1035.00	1065.00
Premium	366.7	260.6	67.0	39.8	9.3	17.1	34.5	11.7	9.0
<u>United Arab Emirates</u>									
Official rate	3.6710	3.6710	3.6710	3.6710	3.6710	3.6710	3.6710	3.6710	3.6710
Parallel rate	3.74	3.85	3.71	3.80	3.80	3.73	3.76	3.72	3.68
Premium	1.9	4.9	1.1	3.5	3.5	1.6	2.4	1.3	0.2
<u>United Kingdom</u>									
Official rate 28/	1.8715	1.8095	1.6055	1.9280	1.8707	1.5120	1.4812	1.5625	1.6025
Parallel rate 28/	1.82	1.80	1.60	1.91	1.86	1.51	1.48	1.56	1.59
Premium	2.8	0.5	0.3	0.9	0.6	0.1	0.1	0.1	0.8
<u>Uruguay</u>									
Official rate	281.0	451.0	805.0	1594.0	2489.0	3480.0	4.4180	5.6150	6.4350
Parallel rate	320.00	500.00	900.00	1925.00	2630.00	4545.00	5.65	5.80	6.48
Premium	13.9	10.9	11.8	20.8	5.7	30.6	27.9	3.3	0.7
<u>Vanuatu</u>									
Official rate	100.56	105.05	110.70	109.25	110.79	119.00	120.80	112.08	112.37
Parallel rate	105.00	126.50	125.00	140.00	144.00	171.00	185.00	162.00	140.00
Premium	4.4	20.4	12.9	28.1	30.0	43.7	53.1	44.5	24.6

Table 2 (continued). Official and "Parallel" Exchange Rates
in Article VIII Countries, 1987-1995 ^{1/}
(End-of-period U.S. dollar rates)

	1987	1988	1989	1990	1991	1992	1993	1994	July 1995
<u>Venezuela</u>									
Official rate	14.500	14.500	43.079	50.380	61.554	79.450	105.640	170.000	170.000
Parallel rate	38.50	42.00	48.70	53.00	65.00	83.40	110.00	182.00	200.00
Premium	165.5	189.7	13.0	5.2	5.6	5.0	4.1	7.1	17.6
<u>Western Samoa</u>									
Official rate ^{29/}	0.4973	0.4655	0.4367	0.4286	0.4084	0.3910	0.3835	0.4079	0.4078
Parallel rate ^{29/}	0.37	0.39	0.41	0.39	0.38	0.31	0.304	0.302	0.3280
Premium	34.4	19.4	6.5	9.9	7.5	26.1	26.2	35.1	24.3
<u>Zimbabwe</u>									
Official rate ^{30/}	0.6013	0.5147	0.4405	0.3793	0.1980	0.1824	0.1442	0.1192	0.1159
Parallel rate ^{30/}	0.40	0.35	0.25	0.33	0.15	0.14	0.118	0.110	0.1140
Premium	50.3	47.1	76.2	14.9	32.0	30.3	22.2	8.4	1.7

Sources: IMF, International Financial Statistics; and Free or Black Market Rates of Payments and/or Transfers Abroad, monthly sheet, International Currency Analysis, Inc. (New York).

For lack of an alternative, this table uses "parallel" market data from a private source (ICA), whose accuracy cannot be checked directly. However, as an indirect test of the representativeness of these data, the author checked the countries for which the data indicated the existence of "significant" parallel premiums (10 percent and up) or quasi-significant premiums (2 percent to 10 percent) at the end of 1993 and 1994, against the exchange restrictions reported for those countries in the Fund's publication Exchange Arrangements and Exchange Restrictions (Annual Report, 1994, and 1995). In virtually all cases, countries with significant and quasi-significant premiums were those with reported remaining restrictions on current and/or capital account. As of end-1994, there were only a handful of countries (including two of the Baltics--Estonia, and Latvia) for which a significant premium was reported, yet they did not reportedly have any exchange restrictions either on the current or the capital account. In such cases, it would seem that the "parallel" rate may have been misreported. Or perhaps there were trade and other restrictions accounting for them. Such discrepancies would warrant further study on a case-by-case basis. In any case, the Fund does not rely on the ICA data or on any other data than those provided by the authorities of a member country when it involves the determination of the existence or not of multiple rates in the Fund's jurisdictional sense. (See further commentaries in footnote 1, p. 19.)

^{1/} List of member countries under Article VIII as of end-December 1995. Marshall Islands, Micronesia, Panama, and the United States are excluded from the table as they use the U.S. dollar. Also excluded are Kiribati which uses the Australian dollar, and San Marino which uses the Italian lira. See also footnote 9 below.

^{2/} In U.S. dollars per Australian dollar.

^{3/} In addition to the principal official rate there is also a secondary rate which is more depreciated (1.2250).

^{4/} U.S. dollars per dinar.

^{5/} Until 1989 there was a secondary rate in addition to the principal rate, but the deviation of the two rates was small.

^{6/} U.S. dollars per pula.

^{7/} U.S. dollars per pound.

^{8/} Rates for Czechoslovakia before separation of Czech Republic and Slovak Republic.

^{9/} The ECCB dollar is the common currency of the following six Article VIII members: Antigua and Barbuda, Dominica, Grenada, St. Kitts and Nevis, St. Lucia, and St. Vincent.

^{10/} U.S. dollars per Fijian dollar.

^{11/} U.S. dollars per Gambian dalasi.

^{12/} There is also a secondary market rate (1.00); and a tertiary rate applied through 1988 (2.71).

^{13/} U.S. dollars per pound.

^{14/} U.S. dollars per dinar.

^{15/} U.S. dollars per dinar.

^{16/} U.S. dollars per Kwacha.

^{17/} U.S. dollars per lira.

^{18/} U.S. dollars per New Zealand dollar.

^{19/} Gold cordobas per billion U.S. dollars through 1987, per million U.S. dollars in 1988, per thousand U.S. dollars in 1989-90, and per U.S. dollar thereafter.

^{19a/} Currency unit is not well specified.

^{20/} U.S. dollars per Omani rial.

^{21/} U.S. dollars per kina.

^{22/} New soles per million U.S. dollars through December 1989 and new soles per thousand U.S. dollars thereafter.

^{23/} U.S. dollars per Sierra Leone leone through 1992; thereafter Sierra Leone leones per U.S. dollar.

^{24/} U.S. dollars per SI dollar

Table 2 (concluded). Official and "Parallel" Exchange Rates
in Article VIII Countries, 1987-1995 ^{1/}
(End-of-period U.S. dollar rates)

<u>25/</u>	U.S. dollars per rand.
<u>26/</u>	U.S. dollars per lilangeni.
<u>27/</u>	U.S. dollars per Tonga Isi pa'anga.
<u>28/</u>	U.S. dollars per pound.
<u>29/</u>	U.S. dollars per tala.
<u>30/</u>	U.S. dollars per Zimbabwe dollar.

that the debt crisis of the early 1980s sharply, albeit temporarily, curtailed access by many indebted developing countries to international capital markets. These trends resulted in a substantial intensification of global competition for funds in an increasingly integrated world capital market, from which progressive developing and transition economies can no longer risk to be detached. 1/

2. Developing countries

This section discusses first the situation of developing countries which have accepted the obligations of Article VIII, Sections 2, 3, and 4 and then explores the situation in the rest.

a. Article VIII members

As of end-1995, well over half of the non-industrial Fund members (90 out of 158) had accepted the obligations of Article VIII, Sections 2, 3 and 4. 2/ This means that they have henceforth committed themselves not to maintain or reintroduce, without explicit approval by the Fund, any restrictions on the making of payments and transfers for current international transactions, multiple currency practices, and discriminatory currency arrangements. 3/

Despite the transitional nature of the arrangements under Article XIV, Section 2, most IMF members had been reluctant historically to accept formally the obligations of Article VIII, Sections 2, 3, and 4. They did so at the rate of less than two members a year since the inception of the IMF. However, the pace of acceptance dramatically accelerated in the past three years, when 39 non-industrial members accepted these obligations. 4/ Two related factors appear to have caused this acceleration. First, the increased experience with successful liberalized systems in developing countries. And second, the IMF staff's adoption in early 1993 of a reinforced strategy to encourage members toward the acceptance of the obligations of Article VIII, especially those that already had a system virtually or totally free of restrictions. A key aspect of this strategy has been to sharpen the focus of Article IV consultation discussions on the

1/ The risks and systemic consequences of the new global financial market, as well as the potential benefits, are discussed in Goldstein, Mathieson and Lane (1991).

2/ The reader is referred back to Table 1. This count of 90 Article VIII developing members includes 10 transition countries, which are more specifically discussed in the next subsection.

3/ As noted earlier, the Fund's jurisdictional definition of current transactions includes some transactions which are ordinarily included in the statistics on the financial (capital) account.

4/ See Table 1 for a list of countries. For an overview of recent developments on current account convertibility, see Quirk, Cortés, et al (1995), Chapter II.

issue of Article VIII restrictions. In particular, countries with no remaining exchange restrictions were advised by the staff that they gained nothing from delaying acceptance of the obligations of Article VIII, because any reintroduction of restrictions by them would be subject to Fund approval under Article VIII. 1/ At the same time, countries that still keep restrictions are encouraged under existing guidelines to suggest a time frame for eliminating both Article XIV and Article VIII restrictions, and accepting the obligations of Article VIII.

Article VIII status does not automatically guarantee that the members concerned do not have any remaining exchange restrictions, some under temporary Fund approval and some without due approval, or that they do not have parallel exchange rate markets, which, in some circumstances, de facto cover some current account transactions. 2/ Moreover, the external debt difficulties of many developing countries in the 1980s often manifested themselves in payments arrears that arose because of exchange restrictions imposed by the authorities, which means that, at least in this sense, the obligations of Article VIII were not always complied with. These various difficulties imply that some developing countries that have accepted the obligations of Article VIII, Sections 2, 3, and 4, have de facto from time to time, but especially in the 1980s, fallen short of maintaining complete current account convertibility.

In addition to exchange restrictions on some current account transactions, a few Article VIII members still maintain restrictive trade systems, which have not been significantly liberalized for decades. In a few cases, these restrictive trade systems have been intensified and substituted for the current restrictions on payments and transfers for current international transactions that have been abandoned. Nevertheless, in the majority of Article VIII developing countries, the tendency in the last decade has been toward the removal of the quantitative trade restrictions and the substantial liberalization of tariffs. Most of these countries underwent successful exchange and trade liberalization on a unilateral basis.

With regard to the capital account, the situation of Article VIII developing members is also varied but promising. Many of the developing members that have liberalized the exchange and trade system have also recently liberalized the capital account. The result in these cases has been the end of the segmentation of the exchange markets for current and capital transactions, which was often enforced partly through repatriation and surrender requirements. Unfortunately, however, no comprehensive study

1/ Most of the members that accepted the obligations of Article VIII, Sections 2, 3, and 4 in the last three years were either those that already had no restrictions or transition countries that had moved quickly to eliminate restrictions.

2/ For evidence on parallel markets the reader is referred back to Table 2. See further discussion below.

of capital account liberalization in developing countries is yet available. 1/ The most recent review indicates that whereas prior to the mid-1980s liberalization of capital account transactions was almost always undertaken from a relatively strong balance of payments position, more recently a number of developing countries adopted full convertibility despite some adverse initial conditions, which could include current account deficits, capital flight, large external debt, limited gross reserve holdings and domestic macroeconomic imbalances. 2/ In virtually all cases the removal of capital controls was followed by substantial net capital inflows, to such an extent that net inflows rather than outflows became a challenging policy problem. 3/ In many of these developing countries, capital account liberalization was accompanied by the introduction or maintenance of a market-determined exchange rate system. 4/ 5/ 6/

Available data for the period 1987-1995, show that about 67 of the 90 Article VIII non-industrial members had parallel exchange rates that differed by more than 10 percent from the official rate at least in one year (Table 2). 7/ However, there was a marked tendency in most countries throughout this period for the parallel market premiums to fall to low single digit levels, reflecting the drive to eliminate remaining exchange

1/ For the most recent reviews of capital account convertibility in developing countries see Quirk, Cortés et al (1995), Chapter III, and Quirk, Evans et al (1995), Chapter IV.

2/ The review in Quirk, Evans et al (1995), Chapter IV, was based on case studies of selected countries which had adopted full convertibility (with the year of adoption in brackets): Argentina (1991), Costa Rica (1992), El Salvador (1992), Estonia (1993-94), The Gambia (1992), Guyana (1991), Indonesia (1970), Jamaica (1991), Latvia (1992), Lithuania (1992), Malaysia (1973), Mauritius (1994), Peru (1991), Singapore (1978), Trinidad and Tobago (1993), and Venezuela (1989). The countries were chosen to provide a representative sample across the various regions.

3/ The possibility of large capital inflows in the liberalization process was already anticipated in the early literature on liberalization in developing countries. See McKinnon (1973), who suggested the need for a temporary retention of some capital inflow controls.

4/ However, in some cases as in Argentina (1991), capital account liberalization was introduced simultaneously with a fixed exchange rate. In Argentina this took place in the context of the introduction of a currency board system.

5/ For an overview of the early experience of developing countries with floating exchange rate systems, see Quirk, Christensen, et al (1987), and Galbis (1993).

6/ The early and unsuccessful experiences of Argentina, Chile and Uruguay in the late 1970s, as well as the successful experience of Mexico in the late 1980s, are discussed in Mathieson and Rojas-Suárez (1993, pp. 23-29).

7/ This comprised 61 countries with separate currencies as well as 6 member countries of the currency union operating under the Eastern Caribbean Central Bank.

restrictions, particularly on invisibles and capital transactions. By July 1995, significant premiums (over 10 percent) remained in only 17 of these countries, and in many cases these also exhibited a significant tendency to fall. 1/ In most countries, the earlier large parallel rate premiums had reflected mainly the continued existence of capital controls, but also, in a few cases, the practical inability of importers of goods and services to satisfy their demand for foreign exchange at the established official exchange rate, or to pay for imports of banned items. In such cases, under lax domestic demand policies and with a relatively sticky official exchange rate, there was an unsatisfied excess demand for funds in the official market, which put pressure on the rate in the parallel market.

The first priority for Article VIII members would be to continue reforms conducive to the removal of remaining restrictions (approved or unapproved by the Fund) on current account convertibility. 2/ To be effective in opening up these economies, this would have to continue to be matched by parallel progress in removing quantitative trade restrictions and simplifying and standardizing trade tariffs. Thus, Article VIII members would have to be especially careful not to conduct exchange rate and domestic demand policies in a manner inconsistent with the maintenance of a liberal exchange and trade system. The generally favorable experience with exchange and trade liberalization in developing countries should encourage others to follow a similar path. 3/ Unilateral liberalization has proven useful to the countries undertaking it even though they did not always face reciprocal conditions in transactions with other countries.

b. Article XIV members

As of end-1995, there were 68 members operating under the transitional arrangements of Article XIV, Section 2 (Table 3). 4/ Some 46 of these

1/ As noted in Table 2, the parallel rate premiums were related in virtually all cases to underlying exchange restrictions on current and/or capital account. A few anomalous cases could be investigated further.

2/ However, as argued in Section II.3, depending on individual circumstances of members, they may benefit from an early capital account liberalization, even if not completely able to remove all current account restrictions at once.

3/ A Fund study found that "countries with above-average growth have had relatively fewer trade restrictions and...lower black market premiums" (IMF, 1993a, p. 51).

4/ This includes some new members which had not yet notified the Fund of their decision regarding their status with regard to Article VIII or XIV. Most of the new Fund members are central and eastern European countries and the Baltics, Russia and other countries of the former Soviet Union, on which a separate subsection follows.

Table 3. Members that Have Not Accepted the Obligations
of Article VIII, Sections 2,3, and 4 of the
Articles of Agreement, in Chronological Order of Fund Membership
(as of end-1995) 1/

Year (In parentheses length of stay under Article XIV status, in years)	Member
1945 (50)	China <u>2/</u> Colombia <u>2/</u> Egypt <u>2/</u> Ethiopia <u>2/</u> Iraq <u>2/</u> Iran, Islamic Republic of (Iran) <u>2/</u>
1946 (49)	Brazil <u>2/</u>
1947 (48)	Syrian Arab Republic
1952 (43)	Myanmar (Burma)
1955 (40)	Afghanistan
1956 (39)	Vietnam (Viet Nam)
1957 (38)	Sudan
1958 (37)	Libya
1961 (34)	Nigeria Lao People's Democratic Republic
1962 (33)	Liberia Togo Senegal Somalia Tanzania
1963 (32)	Cote d'Ivoire Niger Burkina Faso Cameroon Central African Republic Chad Congo Benin Gabon

Table 3 (continued). Members that Have Not Accepted
the Obligations of Article VIII, Sections 2,3, and 4
of the Articles of Agreement, in Chronological Order of Fund Membership
(as of end-1995) 1/

Year	Member
	Mauritania
	Madagascar
	Algeria
	Mali
	Burundi
	Zaire
	Rwanda
1965 (30)	Zambia
1968 (27)	Lesotho
1969 (26)	Equatorial Guinea
	Cambodia
1972 (23)	Romania
1976 (19)	Comoros
1977 (18)	Guinea-Bissau
	Sao Tomé and Príncipe
1978 (17)	Maldives
	Cape Verde
1981 (14)	Bhutan
1982 (13)	Hungary <u>3/</u>
1984 (11)	Mozambique
1989 (6)	Angola
1990 (5)	Yemen, Republic of <u>4/</u>
	Bulgaria
	Namibia
1991 (4)	Mongolia
	Albania

Table 3 (concluded). Members that Have Not Accepted
the Obligations of Article VIII, Sections 2,3, and 4
of the Articles of Agreement, in Chronological Order of Fund Membership
(as of end-1995) 1/

Year	Member
1992 (3)	Georgia Armenia Russian Federation Belarus Kazakhstan Ukraine Azerbaijan Turkmenistan Uzbekistan Macedonia, former Republic of <u>5/</u> Bosnia and Herzegovina <u>5/</u>
1993 (2)	Tajikistan
1994 (1)	Eritrea
1995 (0)	--

Source: IMF, internal records.

1/ This list adds up to 68 members operating under Article XIV out of a total of 181 members of the Fund. This list includes new members which have not yet notified the Fund of their decisions regarding the acceptance of Article VIII or XIV. (See also footnote 3.)

2/ "Original members" (Article II, Section 1).

3/ Hungary became the 114 member that accepted the obligations of Article VIII, Sections 2, 3, and 4 in January 1996. Mongolia became the 115 member in February 1996.

4/ The Republic of Yemen succeeded to the membership of the Yemen Arab Republic and of the People's Democratic Republic of Yemen on May 22, 1990.

5/ The former Republic of Macedonia, and Bosnia and Herzegovina, succeeded to the membership of the Socialist Federal Republic of Yugoslavia as of December 14, 1992.

members had joined the Fund before 1980. The de facto situation of these countries with regard to exchange restrictions was, however, varied. 1/ Some 19 of these members did no longer actually maintain any restrictions under the transitional arrangements of Article XIV, Section 2, or that were subject to approval under Article VIII. For these countries, acceptance of the obligations of Article VIII, Sections 2, 3, and 4, appeared to be a matter of confirming their de facto situation, without any material consequences for the convertibility of their currencies. 2/ They could no longer reintroduce any restrictions without the Fund's approval under Article VIII.

The rest of the members (54 countries) maintained transitional restrictions under Article XIV (the original restrictions that were in effect at the time they joined the Fund and not later removed) and/or restrictions approved or unapproved by the Fund under Article VIII. In many cases, however, the remaining restrictions under Article XIV or under Article VIII were not major. In this case, and especially in those countries that have been long-time members of the Fund, the staff has proceeded in recent years (under an internal guidance note of early 1993) to urge the members to remove the remaining restrictions, so as to prepare themselves promptly to accept the obligations of Article VIII, Sections 2, 3, and 4. Most of the new members of the Fund, and some of the long-time members, have on their own accord accelerated the removal of restrictions.

If the recent success with removing restrictions continues, virtually all countries (temporarily excepting some members with very special difficulties) could eventually be subject to the same standard, with all remaining restrictions being subject to approval by the Fund under Article VIII. For this to be possible, policies leading to more realistic exchange rates and to curbing excess aggregate domestic demand would have to be vigorously pursued. Given the freedom granted under the Second Amendment of the Articles for countries to adopt the exchange rate system of their choice, there seems to be little justification for the continued maintenance in some countries of current account restrictions, which are counter-productive for the member that maintains them and also damaging to the rest of the world. As experience has demonstrated, even the least developed countries can operate free of current account restrictions if macroeconomic policies are calibrated correctly.

Under Article XIV, Section 3, the "Fund may, if it deems such action necessary in exceptional circumstances, make representations to any member

1/ For a recent review of the situation of Article XIV members see Quirk, Cortés et al (1995, Chapter II).

2/ This is true only if the members believe that the Fund will not be more lenient in approving future restrictions under Article VIII for those countries formally operating under Article XIV. The Fund did not make any such distinction in the past.

that conditions are favorable for the withdrawal of any particular restriction, or for the general abandonment of restrictions, inconsistent with the provisions of any other articles of this Agreement." In light of this, the Fund already has the means to prod the members to terminate longstanding Article XIV cases.

Most of the members that have not formally accepted the obligations of Article VIII continue to have parallel exchange rate markets with exchange rate quotations that differ significantly (by more than 10 percent) from the main official exchange rate. As in the case of the few Article VIII developing countries that still have significant parallel exchange markets, the parallel exchange rate premiums of these countries reflect a variety of restrictions, mainly, no doubt, exchange restrictions on the capital account, but also any remaining exchange restrictions on the current account, and in some cases also severe trade restrictions.

In many developing countries, particularly those that still maintain current account exchange and trade restrictions, the opening up of the capital account is viewed as a more problematic and longer-term objective than the opening of the current account. Nevertheless, for those countries that in increasing numbers are choosing outward-oriented policies, the relaxation and eventual removal of capital controls has acquired increasing relevance. Not only it is becoming increasingly difficult to maintain effective capital controls, particularly when current account controls have been removed, but there is also increased awareness that the full benefits of convertibility cannot be reaped unless all exchange restrictions are lifted.

From the early days, there was a certain ambiguity about the reasons for maintaining capital controls. On the one hand, developing countries feared that if they opened the capital account they could lose capital needed for development. On the other hand, theory predicted that because of their potentially higher returns to capital, developing countries that maintained appropriate macroeconomic policies would be awash with capital inflows if they lifted both domestic and external barriers to financial transactions. Experience has amply confirmed the tendency for net capital inflows to become the norm during financial liberalization in cases in which appropriate macroeconomic policies are pursued. ^{1/} In fact, the early and troubled experiences with large net capital inflows of the Southern Cone countries--Argentina, Chile, and Uruguay--of the late 1970s, as well as some recent ones (Mexico in the 1990s) have indicated the need to proceed with caution. In the absence of well coordinated macroeconomic policies and of a domestic environment capable of absorbing productively the foreign inflows, these inflows could complicate the stabilization efforts, lead to real exchange rate appreciation and large current account deficits and an unsustainable level of debt, and originate a financial crash.

^{1/} See, for instance, Schadler et al (1993).

Large net capital inflows have been visible in recent years especially in countries of Asia and Latin America that have freed capital movements as part of a program of general economic reform. 1/ Generally these countries that have received substantial capital inflows in the 1990s have been in a much better position than those in the 1970s to absorb these inflows and to prevent the possible destabilizing effects of excessive inflows (Collyns et al (1992), Chapter V). Part of these inflows may have been the result of external factors in industrial countries that influenced the international allocation of capital (Calvo, Leiderman, and Reinhart, 1992). Nevertheless, in general they tended to reflect economic fundamentals in the developing countries that received them (Schadler, Karcovic, et al (1993) and Ghosh and Ostry (1993)). The policy response of the affected countries to capital inflows has been varied but it has generally involved adjustments in macroeconomic policies, and not the reimposition of capital inflow (or outflow) controls. 2/

Developing countries can particularly benefit from foreign direct investment as well as other forms of foreign investment if they develop and maintain the conditions to attract it. 3/ Besides the removal of restrictions to inflows, political and economic stability is a condition for prospective investors to consider the opportunities open in a developing country. Beyond this, a country can also facilitate these inflows by developing the appropriate legislative and administrative framework to ease the administrative costs and guarantee the repatriation of profits and capital. An adequate tax treatment which does not discriminate against foreign profits and which avoids double taxation is also necessary. 4/

1/ See Collyns et al (1992, Chapter V); Schadler et al (1993); and IMF (1995b) and (1995c).

2/ Even in Mexico during the financial crisis of late 1994 and early 1995 the authorities did not consider the reintroduction of capital controls.

3/ The Fund and the World Bank, mainly through the work of the Development Committee, have emphasized this aspect of development in recent documents. See Development Committee (1993); IMF Survey, May 17, 1993; and Pfeffermann and Madarassy (1992).

4/ The elimination of double taxation cannot be accomplished by an individual country alone. An international consensus is needed to this effect. The OECD with strong support from the United States adopted in 1963 the Model Convention on Income Tax. However, beginning in the 1980s the international consensus under the OECD in this area began to fall apart and was only partly replaced by a more regional approach within the European Community, leading to the conclusion in 1988 of a Multilateral Convention on Mutual Assistance in Tax Matters. See Kuroda (1992).

3. Transition countries

In the external area, the Fund's approach to stabilization and reform in transition countries 1/ has been to push for a substantial measure of current account convertibility and an early unification of the foreign exchange market. 2/ When supported by a liberal trade system, current account convertibility subjects domestic producers to competition from abroad and therefore can assist in the establishment of a rational structure of relative prices. Although capital account convertibility also encourages the integration of the domestic economy with the world economy (in particular world interest rates), its immediate achievement--except as regards trade-related capital flows and foreign direct investment 3/--has not been given priority in most transition countries with Fund-supported programs. 4/ In fact, many of these countries have retained some kind of capital controls, with the application of repatriation and surrender requirements for foreign exchange playing a role in the practical implementation of this policy.

Most transition countries quickly recognized the importance of moving toward complete current account convertibility. Ten of these countries accepted the obligations of Article VIII in 1994-95. 5/ Most of the remaining 15 members also have made substantial progress toward de facto current account convertibility.

In central and eastern Europe, some remaining current account restrictions, applying almost exclusively to invisibles, were retained temporarily in cases in which it was feared that the removal could precipitate capital outflows. Thus, the five countries covered in a 1993

1/ This section reflects experience in 25 countries in central and eastern Europe, the Baltics, Russia, and other states of the former Soviet Union, and Mongolia.

2/ Some countries, notably the Baltics, had already achieved a large degree of convertibility before they engaged in Fund-supported adjustment programs. In such cases, these programs served to promote and support the authorities' intentions.

3/ Allowing the repatriation of earned interest and of dividends on foreign direct investment is already covered under current account convertibility.

4/ Some transition countries (notably the Baltics) did move toward capital account convertibility very early in the reform programs.

5/ These are the three Baltic countries (Estonia, Latvia, and Lithuania), two of the countries spun from the breakout of the former Yugoslavia (Croatia and Slovenia), the two countries of the former Czechoslovakia (the Czech Republic and the Slovak Republic), and Poland, Moldova, and the Kyrgyz Republic (see Table 1). Subsequently to the preparation of this paper, Hungary accepted the obligations of Article VIII in January 1995, and Mongolia in February 1996.

staff study 1/--Bulgaria, Czechoslovakia (before the breakout), Hungary, Poland, and Romania--that pursued extensive market-oriented reforms in 1990-91, acted very quickly to remove restrictions on access to foreign exchange for most payments and transfers for current international transactions; they provided, however, at least initially, very limited access to foreign exchange for travel abroad for tourism. 2/ Bulgaria, Czechoslovakia, and Poland instituted this limited version of current account convertibility in a "big bang" fashion in conjunction with the liberalization of domestic prices; by contrast, Hungary and Romania took about one year from the time of substantial domestic price liberalization to remove licensing and other requirements for most imports. 3/ With appropriate management of the exchange rate and sound macroeconomic policies, the central and eastern European countries that have not already done so, could rapidly accept the obligations of Article VIII. Moreover, they could benefit from further liberalizing inflows of foreign direct investment and trade-related capital flows.

A rapid transition to current account convertibility was also implemented in the three Baltic States, and to a lesser extent in Russia and some other states of the former Soviet Union. 4/ In most of these countries the movement toward current account convertibility was backed by a flexible exchange rate regime 5/ and by attempts to rein in expansionary demand policies. Although it would be too early to draw final conclusions from the experience of these countries, the successful introduction of complete or virtually complete current account convertibility in countries such as these, with virtually no underlying market institutions, with a low starting level of foreign exchange reserves and with practically no preconditions, suggests that the introduction of current account convertibility may have benefits of its own and need not wait until markets are deepened.

1/ Borensztein and Masson (1993).

2/ In January 1994 Bulgaria raised the tourist travel limit to US\$2,000 per person, almost twice the annual income per capita. Also, resident holders of foreign currency deposits may use these balances without restriction.

3/ See Borensztein and Masson (1993), p. 46. In contrast, Albania initially faltered in the transition process and hesitated in permitting greater account convertibility--see Blejer, Mecagni, et al (1992, chapter V)--but in 1992 followed a rapid transition to full convertibility together with other reforms.

4/ For a general overview of major economic developments in these countries, see Citrin and Lahiri, ed. (1995).

5/ However, in Estonia, the authorities introduced a new currency in June 1992--the kroon--under a fixed rate with the deutsche mark backed by the rules of a currency board arrangement. See Bennett (1993). A similar currency board system was established somewhat later by Lithuania. Also, Latvia adopted an unofficial peg to the SDR in February 1994.

By contrast, most of the transition countries have maintained capital controls during the early stages of the reform process, waiting to relax these controls until credibility in the economic program has been established and the financial sector has been developed. A basic argument that has been made against establishing complete capital account convertibility early in the reform process is that unrestricted capital movements could make the reforming economies potentially vulnerable to speculative attacks, which could be particularly damaging when the credibility of the authorities is still to be established. Before achieving any substantial development of domestic financial markets and with continued reliance on direct instruments of monetary control such as credit ceilings and in a few cases regulated interest rates, capital controls were perceived as being needed to prevent destabilizing flows between domestic and foreign financial markets and undesirable reserve and/or exchange rate movements. A related argument has been that in economies with substantial shortages of foreign exchange and where there is a likelihood of substantial capital outflows that can result from portfolio diversification and risk considerations, the authorities may wish to contain the outflows to a level that does not endanger the achievement of reserve, foreign exchange or import targets needed for economic growth. Indeed, despite the maintenance of restrictions on capital outflows "in many transition countries, private capital inflows were initially dwarfed by capital flight." (IMF, 1995a, p. 58).

For the longer run, however, it is recognized that capital controls may create widespread inefficiencies, that there are likely to be administrative problems in controlling capital flows, particularly at times of pressure in exchange markets, and that capital controls should not be a substitute for appropriate domestic financial policies. "As stabilization took hold, capital inflows rose substantially in some countries, both through repatriation of domestic funds and through new foreign financing." (IMF, 1995a, p. 59). As could be expected, the transition countries were more likely to benefit in the early stages from removing controls on inflows of direct investment than other types of inflows. 1/ "Foreign direct investment in all transition countries increased from about \$200 million in 1989 to about \$6 billion in 1993 and then fell somewhat in 1994." (IMF, 1995a, p. 60).

All the transition countries in central and eastern Europe initially introduced repatriation requirements in connection with capital controls, although in some of them the existing capital controls were apparently not strictly enforced. Except for Bulgaria, which has no form of surrender requirement, all these economies also introduced a full surrender

1/ Nevertheless, an argument that has been made for capital inflow controls on direct investment is that restrictions on inflows might be required to prevent the wholesale buying up of domestic assets by nonresidents in the event that the currency is overly depreciated initially.

requirement for enterprises. 1/ In all cases, however, households were allowed to place foreign currency deposits with domestic banks (internal convertibility). Repatriation and surrender requirements were viewed in many cases as mechanisms needed to implement uniform capital controls. While in principle the implementation of capital controls tended to impose distortions with implications for enterprise behavior, temporary surrender requirements in central and eastern Europe appear not to have created serious problems. This in part reflected progressively tighter financial policies in most countries, increasingly flexible interest rates and exchange rates that created incentives to hold domestic financial assets, and the credibility of residents' right to re-acquire foreign exchange for all legitimate current account transactions.

All five transition countries in the above mentioned staff study (Borensztein and Masson, 1993) decided to maintain restrictions on capital account convertibility in the early stages of the reform process. Restrictions included the repatriation and surrender requirements noted above, the unavailability of foreign exchange in the official market for the acquisition of foreign assets by enterprises and households, and restrictions on holdings of foreign assets by enterprises (but not by households). Again, no serious problems appeared to have been encountered with the temporary exchange control systems in these countries. Because of restrictive financial policies, the surrender requirements and other capital controls imposed did not appear to have been tightly binding constraints on enterprise behavior, and there was little evidence to suggest widespread attempts at circumvention. The small and generally shrinking premiums on black markets appeared to indicate an absence of widespread desire to obtain foreign exchange for purposes other than those legally permitted. 2/ Conversely, it was not clear that the lack of effective capital controls in Bulgaria was the source of major problems, although there was initially (1991) some overdepreciation of the floating exchange rate. 3/

The Baltic States, as well as Russia and other states of the former Soviet Union, started from a position of no effectively implemented repatriation or surrender requirements, 4/ and with enterprises holding

1/ Romania initially had a partial surrender requirement at an appreciated exchange rate.

2/ Only in Romania did significant problems seem to have been encountered; these stemmed from a wide dispersion between the reference exchange rate, announced by the central bank, and the floating rates of the exchange bureaus, and from the use of foreign exchange held by enterprises in foreign currency accounts to intervene in the official exchange market.

3/ However, the more fundamental factor underlying the 1991 inflation and depreciation was a large monetary overhang.

4/ Such requirements were on the books, but were difficult to enforce in the absence of tight financial policies and the credibility of the policies for re-acquisition of foreign exchange for legitimate current account transactions.

foreign currency balances of unknown amounts in bank accounts abroad. Early in 1992 the Baltic States abolished repatriation and surrender requirements. However, new, albeit temporary, controls were soon reintroduced. Estonia reintroduced a 100 percent repatriation and surrender requirement with the launching of its new currency--the kroon--in the context of a currency board arrangement in June 1992; this requirement was eliminated in December 1993. Latvia replaced the surrender requirement with taxation of foreign currency earnings, but this taxation was eliminated promptly in 1993. Lithuania reintroduced a surrender requirement of 25 percent on state enterprise export earnings in February 1993, but this was eliminated in mid-1994. The Russian Federation, by a Presidential Decree on the Liberalization of Foreign Economic Activity of November 1991, introduced a 40 percent surrender requirement and a multiple exchange rate system. The exchange system was unified in July 1992 and the exchange surrender requirement was increased to 50 percent beginning in September 1992. The rest of the former Soviet Union countries also maintained capital controls, often supported by partial surrender requirements. A few of them replaced surrender requirements with a tax on export proceeds.

IV. Some Policy Options

This paper has addressed a number of issues that arise in Fund policy and technical advice on convertibility. A basic theme has been the extent to which the Fund's policies and advice on convertibility continue to provide adequate guidance on these matters. In this regard, there is some unfinished business concerning (1) the speed for achieving current account convertibility and the policies to maintain such convertibility thereon, (2) the use of multiple currency practices, and (3) capital account convertibility.

1. Current account convertibility

A minority of Fund members continue to avail themselves of the transitional arrangements under Article XIV; in some cases such arrangements have been maintained for very long periods. The Articles do not specify a time limit on the duration of Article XIV status. In accordance with Article XIV, Section 1, members may at any time notify the Fund that they accept the obligations of Article VIII, Sections 2, 3, and 4, and no longer wish to avail themselves of the transitional provisions of Article XIV. The Fund has long been of the view that before members give notice that they are accepting the obligations of Article VIII, Sections 2, 3, and 4, it would be desirable that, as far as possible, they eliminate measures which would require the approval of the Fund, and that they satisfy themselves that they are not likely to need recourse to such measures in the foreseeable future. This is because the acceptance of the obligations of Article VIII, Sections 2, 3, and 4 should be perceived as a public commitment on the part of the authorities to deal with balance of payments problems in future through appropriate adjustment policies (including

exchange rate action) and financing rather than through recourse to restrictive exchange measures. Moreover, Executive Board discussions have concluded that it would not be prudent to impose a time limit uniformly across members because of their diverse situations. However, it is recognized that it is not efficient to allow members to avail themselves of the transitional arrangements for too long.

In the light of these considerations, in January 1993 the Chairman's summing up at the conclusion of the biennial review of the IMF's surveillance policy called for an acceleration of Article VIII acceptances within the existing framework, that is, in the context of Article IV consultations and use of Fund resources discussions. 1/ In response to this call the staff prepared an internal guidance note, which served to put in practice the recommended policy. 2/ Since the staff began to intensify its efforts in early 1993, the rate of Article VIII acceptances has increased dramatically. 3/ An additional 39 members have accepted Article VIII obligations, bringing the total of Article VIII members to 113 by end-1995. Further to reinforce these policies, and within the same spirit of cooperation, the Fund could consider the following actions:

(i) With regard to restrictions on payments and transfer for current international transactions maintained by Article VIII members, the Fund could regularly compile a list of the countries maintaining restrictions and of the restrictions concerned, indicating in each case whether they have been approved by the Fund and the date upon which such approval will lapse, or they remain unapproved, and therefore constitute a breach of the member's obligations under the Fund's Articles. The compilation of such a list could by itself be counted on to operate as a deterrent against the unjustified use of these restrictions.

(ii) The Fund could continue to urge the members which have not formally accepted the obligations of Article VIII but which no longer maintain any restrictions, quickly to move to Article VIII status. Many of the members that maintain no restrictions under Article XIV also do not impose any restrictions subject to approval under Article VIII, or they maintain restrictions that could be quickly eliminated without adversely affecting the balance of payments, so that they are already meeting the basic conditions for acceptance of the obligations of Article VIII. These countries appear to be maintaining their Article XIV status through inertia. In some cases there may be inadequate recognition of the fact that once a restriction maintained under Article XIV has been eliminated, its reintroduction would be subject to approval under Article VIII. Progress on a case-by-case basis in this area could continue to be reported to the Board

1/ See Quirk, Cortes et al, 1995, page 8.

2/ See Quirk, Cortes et al, 1995, page 9.

3/ Of course, the success of this policy rested mainly with the member countries' recognition of the beneficial effects of eliminating exchange restrictions, with the Fund acting as a catalyst.

in the context of Article IV consultations with each of these members, and in the context of Fund-supported adjustment programs.

(iii) With regard to the rest of the Article XIV members, and while avoiding a rigid general time limit, the Fund could continue in the context of Article IV consultations and use of Fund resources, to discuss with each member an indicative time limit, tailored to the individual situation of the member, for the acceptance of the obligations of Article VIII, Sections 2, 3, and 4. It should be noted that each country maintaining Article XIV restrictions is required under Article XIV, Section 3, to submit to an annual review by the Fund, usually in the context of the Article IV consultations. Further efforts could be made to use these consultations to explore with the authorities the benefits of eliminating the existing restrictions. ^{1/} This would tend to reduce the excessive freedom enjoyed in the past by members to maintain Article XIV status indefinitely. Discussions could focus on the requirements and sequencing for the removal of these restrictions, specially in the case of long-standing Fund members and those that have availed themselves of Fund financial support over an extended period.

Members which retain restrictions under Article XIV often seem reluctant to accept the obligations of Article VIII status because of their difficult balance of payments position and their perception of a continued need to have possible recourse to exchange restrictions for balance of payments reasons. However, often the effect of these micro measures on resolving balance of payments problems is null while the resulting distortions carry large costs. In some cases the restrictiveness in terms of scope and intensity of the measures is limited because they are limited only to those which were in existence at the time the country became a member of the Fund and which were not subsequently eliminated. The exercise of surveillance and conditionality could continue to be used to encourage members to remove restrictions and accept Article VIII status after a reasonable transition period.

In addition, the Fund "may, if it deems such action necessary in exceptional circumstances, make representations to any member that conditions are favorable for the withdrawal of any particular restriction, or for the general abandonment of restrictions" (Article XIV, Section 3). However, the Fund has thus far avoided making use of this provision, preferring instead to encourage and advice members on the removal of restrictions.

^{1/} These consultations could focus on removing the underlying factors for which countries maintain exchange restrictions on current account transactions. Among these factors are the use of exchange controls to enhance fiscal revenues in countries with weak fiscal systems; the use of exchange controls to substitute for direct trade restrictions; and the authorities' desire to continue restrictions on capital transactions.

2. Multiple currency practices

Multiple currency practices have already been effectively abandoned by all the industrial countries and many developing countries, but they remain entrenched in some other developing countries. A few developing countries maintain multiple rates that are officially sanctioned. More important, too many developing countries (including some of those that have accepted the obligations of Article VIII) have parallel exchange rates. From the present jurisdictional point of view only multiple currency practices relating to current account transactions that are officially sanctioned and that are not maintained under Article XIV must be approved by the Fund under Article VIII. Thus, an illegal parallel market which exists in a country will not give rise to a multiple currency practice if the authorities do not relegate transactions to this market. Nevertheless, the Fund generally recognizes the negative effects for economic efficiency of the existence of parallel market rates. Thus, even if they are not officially sanctioned, it is generally recognized that these parallel markets largely arise because of official trade, exchange and capital restrictions. 1/

The distinction between official multiple exchange rate systems and the de facto existence of two or more exchange rates can and should continue to be minimized for the following reasons. First, the economic consequences are the same whether the multiple rates are officially sanctioned or not; they both result in inefficiencies in the allocation of resources; in both cases the parallel market players exploit market restrictions. (In the case of multiple exchange rates that are the indirect result of other restrictions, the parallel market players often reduce the economic damage caused by the restrictions. For this reason, in some countries, these parallel markets, though not officially sanctioned, are tolerated.) Second, perhaps more important, the exchange and trade restrictions that cause the existence of the dual or multiple rates are in any case policy determined, whether the rates are officially sanctioned or not. It follows that the Fund cannot make a strong differentiation between dual or multiple exchange rates that are officially sanctioned and those which are not.

Both cases should be treated as emanating essentially from policies which involve controls and discrimination. In addition, in certain respects it would be more efficient and transparent for members officially to sanction the existing multiple rates than to continue to operate as if they did not exist. For one thing, the declaration of a multiple rate brings the matter directly to the attention of the Fund and of the international community and usually leads to a program for the termination of the

1/ However, as noted earlier, in some cases illegal parallel market transactions may result from other than official actions, for instance, drug money laundering and tax avoidance. This presentation abstracts from these non-official causes. The presentation also abstracts from restrictions that are authorized by the Fund in fulfillment of international obligations such as reasons of security that are contracted under the United Nations.

practice. 1/ Indeed, under some programs supported by Fund arrangements, members with unofficial dual exchange rate systems have introduced an official dual rate system to facilitate the shift to a more liberal exchange and trade regime, and generally with a view toward eventual unification of the rates. In some cases, the slow progress with regard to the elimination of multiple rates not officially sanctioned has partly had to do with the lack of official recognition of the problem on the part of members' authorities, which in turn may have led to insufficient attention by the Fund. Therefore, the Fund more forcefully could encourage members to acknowledge explicitly the existence of dual or multiple exchange rates even when those rates are not officially sanctioned. 2/

An appropriate policy to deal with parallel currency markets cannot consist of intensifying controls and penalties for violation of the restrictions, but of progressively reducing the restrictions which give rise to them. In this regard, the elimination of parallel currency markets should not be viewed as an objective in itself, but as a desirable consequence of the broader goal of liberalizing exchange and trade and capital restrictions. This is the only consistent and efficient way of eliminating parallel exchange rate markets. The Fund could consider the following actions:

(i) Request systematic periodic reporting by members of all the multiple exchange rates prevailing in their respective countries, including parallel market exchange rates as applicable. The staff is already requesting such information in the course of Article IV consultation discussions and use of Fund resources. More specifically, the Fund could maintain an updated and integrated database on multiple exchange rates. The reporting obligation of members would, of course, continue to be independent of the issue of whether the Fund has jurisdiction over multiple currency practices applicable solely to capital transactions, an issue still pending from resolution.

(ii) The Fund could henceforth intensify and make more explicit its examination of the determinants and the consequences of multiple currency practices on a case-by-case basis, with a view to liberalizing the exchange and trade and capital restrictions which cause them.

1/ The Fund must in any case examine whether the dual or multiple rate system arises as a result of exchange restrictions on the current account, in which case it falls directly under Fund jurisdiction within the present regulatory arrangements.

2/ Fund staff already monitors exchange rates in parallel markets. Requiring more official reporting of parallel exchange rates could be a sensitive issue in some countries, as it could be misinterpreted as official recognition of such markets.

3. Capital account convertibility

All industrial countries have by now removed all exchange controls on capital movements, and an increasing number of developing countries have done so or are in the process of doing so. ^{1/} Both technological innovations which increased the difficulty of maintaining effective controls and raised costs of administration of controls, and recognition by the authorities of the advantages of a free capital market, have contributed to this liberalization. The EU members received final impetus to move to full capital convertibility as a result of the ratification of the Single European Act (1987) and the second Capital Markets Liberalization Directive (1988). In a broader regional context, the OECD also sponsored capital account liberalization by its members through the Code of Liberalization of Capital Movements which, since 1989, has covered all capital transactions.

Many developing countries continue to argue for the need to maintain capital controls to prevent adverse external monetary influences and to retain financial resources within the country to finance domestic investment. There is, however, an increasing recognition by these countries that foreign direct investment and also, to a lesser extent, portfolio flows are beneficial to the receiving countries and pose the least threat to instability as long as appropriate macroeconomic policies are pursued. Similarly, trade-related capital movements are valued for their role in promoting trade flows. Where questions arise more frequently is in relation to international financial sector flows. Nevertheless, there are increasing doubts about both the desirability of keeping controls on financial sector flows and the ability of the authorities to implement them. Moreover, it is increasingly being recognized that any capital flow disturbances that may arise can more effectively and efficiently be counteracted by implementing sound domestic demand and exchange rate policies, and by introducing reforms to strengthen the domestic financial system, than by tightening capital controls. Capital outflow controls are often made necessary as a complement of a policy of repressing domestic interest rates--a policy which is no longer considered acceptable--with the consequent incentive to outward capital movements. This problem could be solved by freeing domestic interest rates and increasing the efficiency of the domestic financial system.

As in the case of trade, capital controls can be quantitative or tariff-based and in both cases they may lead to or be part of a policy of dual or multiple exchange rate arrangements. Quantitative capital controls, including some forms of repatriation and surrender requirements, are particularly inefficient and discriminatory, and priority should be given to their elimination. By contrast, certain instruments like taxes on private capital inflows and reserve requirements on bank borrowing abroad could in principle be used efficiently--if temporarily--to overcome certain

^{1/} It is estimated that about 60 countries including the 23 industrial countries have achieved full capital convertibility.

macroeconomic market failures, without changing the direction of capital flows.

In proceeding to deregulate capital controls, the priority would thus be to eliminate first all quantitative restrictions, then eliminate dual or multiple exchange rates, and finally retain or put in place if at all warranted, an acceptable tariff-based or tax treatment arrangement, one that preferably does not discriminate between domestic and foreign transactions. 1/ For instance, if a system of reserve requirement ratios is in place against domestic currency deposits, this system should be extended to cover foreign currency deposits with domestic banks. 2/ Temporary marginal reserve requirement ratios or interest rate equalization taxes could also be used to treat difficult cases of external adjustment such as those created by excessive capital inflows in the liberalizing economy.

There are two possible approaches for increasing Fund involvement in the area of removing capital restrictions (see Quirk, Evans et al (1995), Chapter II).

(i) Within the present regulatory system the Fund could more intensely examine, in the course of its surveillance activities (that is, in Article IV consultations), the capital controls prevailing among the members with a view to liberalizing the system, beginning with the elimination of obstacles to trade-related flows, inflows of foreign direct investment and any quantitative controls. This policy should be closely coordinated with the member's exchange rate policy and with the lifting of interest rate restrictions. Moreover, the Fund could increase the regular and systematic collection and dissemination of information regarding the capital controls maintained by member countries with a view to encouraging their removal. 3/

1/ In addition, the authorities should retain or introduce appropriate prudential regulations to maintain sound financial and capital markets systems in the presence of substantial capital flows. For an analysis of such prudential regulations see Garber (1995).

2/ In this respect, the concept of what is a capital control is subject to interpretation. For instance, a reserve requirement imposed on inflows of foreign currency into domestic banks may by itself be regarded as a capital inflow constraint. However, if the reserve requirements on the domestic and foreign currencies are the same, there is in a substantive sense, a kind of neutrality with regard to capital inflows. The issue of reserve requirements on foreign currency deposits also has broader implications, which are not discussed here, for the operation of domestic monetary control and the international banking system.

3/ The Fund already disseminates information on capital controls through its Annual Report on Exchange Arrangements and Exchange Restrictions, but such information is not comprehensive.

(ii) Alternatively, it has been suggested that the Fund membership could consider an amendment to the Articles, in order to claim an expanded area of Fund jurisdiction over capital controls. For this to be possible, it would be necessary to dispense with the provision of Article VI, Section 3, which authorizes members to impose controls on capital movements, as well as to apply Article VIII, Section 3 to all multiple currency practices including those applicable solely to capital transactions. It would probably also be necessary to dispense with the provision of Article VI, Section 1 that empowers the Fund to request a member using its general resources to impose capital outflow controls in case of a sustained and large capital outflow. The Fund could thus assume within the universal context of its membership the roles that the OECD and the EU have exercised over their members through their codes on liberalization of capital movements.

It should be emphasized that, even if an amendment of the Articles resulted in extending the Fund's jurisdiction to capital controls, the policy in practice would be to encourage rather than force countries to eliminate capital controls, in consonance with the present approach followed with regard to current account convertibility.

Historical Background on the Move to Article VIII Status

Although the idea of moving to current account convertibility was embodied in the Articles of Agreement (Articles VIII and XIV) from the beginning, it took a long time for most countries to implement it. 1/ At end of 1995, 113 members out of a total of 181 members had accepted the obligations of Article VIII, Sections 2, 3, and 4 (Table 1). This included all the 23 industrial countries. Most of the eastern European countries and the countries of the former Soviet Union either have accepted Article VIII obligations or have indicated their intention to move promptly to substantial current account convertibility. In addition to the countries that have formally accepted the obligations under Article VIII, 13 African countries whose currencies are pegged to the French franc de facto have convertible currencies, although their convertibility is limited to the French franc. 2/

The United States and three other countries in the Western Hemisphere-- El Salvador, Mexico, and Panama--were the first to accept, in 1946, the obligations of Article VIII. 3/ These early countries were joined by four others in the years through 1953: Honduras (1950), Canada (1952), the Dominican Republic (1953) and Haiti (1953). By contrast, the early attempt by the United Kingdom to establish current account convertibility in 1947 was unsuccessful.

In light of the adverse United Kingdom experience, the other European countries decided to delay the acceptance of convertibility and, instead, established a central payments and clearing union--the European Payments Union (EPU)--to promote trade among themselves and to encourage the elimination of exchange and trade restrictions. Under the aegis of the EPU, the European countries progressively succeeded in eliminating most quantitative trade restrictions and in achieving de facto current account convertibility (absence of restrictions on the current account) by the time the EPU was terminated in 1958. Even so, the former EPU members, including the United Kingdom, waited until 1961 to accept the obligations of Article VIII. In that year, in addition to nine western European countries, Peru and Saudi Arabia also declared formal current account convertibility. Fifteen more countries, both industrial and developing, accepted the obligations of Article VIII from 1962 to 1968.

1/ For earlier discussions of the history of current account convertibility after the Second World War see Gilman (1993), Greene and Isard (1991, Appendix) and Polak (1991).

2/ Also, Hong Kong, as a nonmetropolitan U.K. territory, moved to Article VIII status with the United Kingdom in 1961.

3/ Switzerland, although not a member of the Fund until 1992, also moved quickly to convertibility after the war.

The remaining countries that have accepted the obligations of Article VIII have done so at their own pace and in a largely unrelated manner, except that the process has been intensified in recent years as a result of new thinking, new developments favorable to liberalization, and efforts undertaken by Fund staff. It is worth noting that whereas some developing countries, particularly in the Western Hemisphere and in the Middle East, accepted the obligations of Article VIII relatively early, most others, together with some industrial countries (New Zealand, Iceland, Spain, Portugal, and Greece), postponed their convertibility until the 1980s and 1990s. Among the developing countries that have accepted convertibility are six of the seven Fund members which form a monetary union under the Eastern Caribbean Central Bank, the six members of the Gulf Cooperation Council in the Middle East, and the four newly industrializing Asian economies--Hong Kong, Korea, Singapore, and Taiwan Province of China--together with Indonesia, Malaysia, and Thailand. Recently, there has been a move by some North African countries to eliminate exchange restrictions and accept the obligations of Article VIII; Morocco and Tunisia have already done so. 1/

In about one third of the cases, convertibility under Article VIII was introduced shortly after the country joined the Fund. This was the case, for instance, in the United States, Mexico, El Salvador, and Panama (1946), Guatemala (1947), Haiti (1953), Jamaica, and Kuwait (1963), The Bahamas, Bahrain, and Qatar (1973), Seychelles, and Suriname (1978), Dominica, and Solomon Islands (1979), Antigua and Barbuda, and Belize (1983), San Marino, and the Republic of the Marshall Islands (1992), Estonia, Latvia, and Lithuania (1994), and the Kyrgyz Republic and Moldova (1995). In most other cases, however, member countries took a long time before accepting the obligations of Article VIII, and continued to operate with restrictions under Article XIV. Thus, despite the original notion that the restrictions under Article XIV were to be maintained only temporarily during a transitional period, in practice they were maintained for a long time by many members. In fact, 68 Fund members are still operating today without having accepted the obligation of Article VIII, 36 of them for over 30 years (Table 3).

1/ Algeria is also close to accepting Article VIII. For an analysis of the process of introduction of current account convertibility in these three countries, see Nsouli, Cornelius, and Georgiou (1992).

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