SECOND SESSION

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The group of financial and monetary experts I chaired a few weeks ago in Wolfsberg agreed that it is even theoretically impossible —let alone practically possible—, to improve the monetary set-up of the world separately from the complex problems in the field of debt, trade and development. We agreed that right now there is no chance for a big worldwide or a smaller monetary conference to achieve anything if not at the same time—and maybe even earlier—the problems of debt related to trade and development have been brought into a framework where they do become soluble. Thus, we concluded that we should not in the first place make any monetary proposals. Instead we felt that we should put before the InterAction Council five different sets of proposals (see the text of the report following this speech).

Starting with proposals regarding the debt crisis and debt management; secondly, the crisis of development and development aid; thirdly —for the third time I'll use the word crisis— the world free-trade crisis; fourthly, the necessity to overcome the devastating lack of coordination of fiscal, monetary and economic policies of sovereign nations; and fifthly —rather reluctantly— did we make a few proposals regarding the monetary constellation and disorder of today. We are advancing a few guidelines in order to get from disorder to a system. We did agree that what we have right now is not a world monetary system; at best, it is a constellation, maybe even less, a floating constellation—floating in many senses of the word.

The principle of this report was not to give you any new analysis. There are so many analyses around the world and thus we refrained from that. While there are here and there one or two sentences describing the problem, we normally have assumed that the hoped-for readers do know the problems. The problems need no further analysis or explanation. Instead, we did concentrate on practical proposals and sometimes you will find a proposal just in one sentence about which you could write a book of 120 pages. We concentrated on practical proposals which are not detrimental to the hoped-for evolution of the world's economy in the medium- and the long-term.

We also let ourselves be guided by the principle of shortness. We understand that Heads of State and Heads of Government as much as ourselves do not wish to read long papers and never do —whether they wish it or not, as they do not have the time. I think, the Council will have to abbreviate its conclusions from our discussions even further.

I would like to mention a fourth principle which was of overwhelming importance to us. We had at our disposal, given the background of the members of the group, the knowledge of all the proposals and papers which float around the world right now. Nothing of importance did escape us. What we concluded represents proposals put together to former leaders from various regions of the world, put together by personalities coming from industrialized countries as well as planned economies, coming from OPEC countries as well as from developing countries, coming from developing countries who are in heavy debt, but also from least developed countries who don't really suffer from debt but suffer from other very grave problems at the same time.

By consensus, we arrived at the conclusion that no solution is really worthwhile to be considered if it does not ask something from everybody. Or to put it in short: every group of countries, every category has to suffer somewhat, has to sacrifice something in order to let us all gain and let the world as a whole gain. This principle is not explicitly put on top of the paper or at the bottom in the last line, but it is necessary to be understood: we do not believe that the world is going to make economic progress in this mess if those who advise governments and governments themselves do not understand that there is no way to get out of the mess neither in trade or development nor in debt management situation nor in the monetary situation if governments do not understand that they have to sacrifice something.

It is very difficult to ask this from governments because almost all of them are in domestic trouble vis-a-vis their opposition and their electorate and do not wish to appear as sacrificing some of their so-called national interests or their holy cows. This is the real difficulty: that governments are much more occupied with their domestic pressure now than they have been until the first oil price explosion in 1972 or 1973. And since 1979-1980 this domestic pressure has grown, whether it is growing famine in country A or growing unemployment in county B or whether it is the attempt to paper all this over by growing inflation in country C.

As regards the substance of the report, there is a short introduction of one page, in which one group of institutions is being praised. I think one should not always criticize institutions altogether: one becomes an outcast if one voices criticisms only. It is very easy to have four has-beens criticize the rest of the world. So one group of institutions gets praised, namely that cooperation among central banks and the skillful responses of the Bank for International Settlements (BIS) and the International Monetary Fund (IMF) have succeeded thus far in containing the debt crisis. Then it goes on that the restoration of broad prosperity on a sustainable basis will require responsible and concerted action of all.

All the groups of countries, all the countries in different regions, any of them have to sacrifice something. The introduction stresses that economic policy should be guided not just by short-term concerns. This is the natural thing for governments to do —to act or react on short term aspects having in mind the next general elections or whatever the next domestic event may be in their respective countries. But that they instead should also concern themselves about the long-term implications, about the long-term consequences of their short-term economic policies.

We also wish to stress the necessary sustaining and reinforcing of international institutions, some of which we have mentioned already, IMF, for instance, the World Bank, GATT and others. We think that they are of overriding importance. We also hint to the fact that there is an enormous economic waste not only in developed countries but also in developing countries. The enormous expenditures on the military side of the budget in the developed world and in the developing world is one of the real reasons for the fiscal difficulties in which many of our states find themselves right now. We also found it necessary in the introduction to call the dangers from a depletion of natural resources and ecological deterioration to the attention of this Council and the world. In the end, we state the obvious, namely that the ultimate aims of economic activity have to be the enhancement of welfare and the respect of human rights for the benefit of the individual.

The first chapter of the report on debt and debt management is divided into four paragraphs. Each paragraph deals with another group of addressees. We address the debtor countries and tell them that debtor countries should seek early advice from the IMF and that they should pursue realistic adjustment programmes agreed with the IMF. We find it unthinkable to renounce this important role of the IMF. We also stress that debtor countries should create favorable conditions in order to let the flight capital return to the respective countries. The percentage at which the flight of capital, out of Latin America for instance, led to this debt crisis is enormous. Many of the so-called credits are in fact nothing else but a way to finance the flight of capital from Latin America to North America, to London, to Frankfurt, to Switzerland and other places. It is necessary that the debtor countries understand this and then that they undertake legislation and other measures in order to let the flight capital get back which, in itself, would alleviate them from a great part of the interest which otherwise they have to transfer.

We also call on the developing and debtor countries to undertake measures to attract more private investment on their national soil —private investment from abroad— and to remove the bureaucratic or the political restrictions which are in place right now. That is the best way to attract capital from the outside. That is the best way for technological transfer. We also think that it is intolerable for the government or the central bank of a debtor country that they do not know what maximum debt service payments they will have to make in the course of the next ten months, given the floating rates of interest. It is necessary for them that at least over one year they can calculate what they have to pay.

The essential role of the IMF, nowadays, we think, is the role of negotiating adjustment programmes with the several debtor countries. We do feel that there has to be conditionality whether it is popular or not because otherwise fresh money will not flow. Otherwise you might only get official aid but no fresh money from private banks.

I would like to mention that we concerned ourselves with the question whether or not under the auspices of the IMF we need to try to put together a "General Agreement to Lend" which would comprise the rules which I have sketched. A "General Agreement to Borrow" does already exist between central banks.

As regards the commercial lender banks —whether in Tokyo or Frankfurt or Zurich or London or New York or wherever— they have to provide fresh money to the debtor countries. It is not easy for them to do so because most of them are already over-exposed to a very dangerous degree. I have made private calculations as regards the five biggest banks in New York City, or as regards the three biggest German banks in Frankfurt. If you take these banks on the one hand and take on the other hand the five biggest Latin American debtor countries you will find that these five biggest banks in New York or the three biggest German banks are exposed —to the five biggest debtors in Latin America only— to an order of between 130 per cent up to 230 per cent of their own capital. This is only a comparison between their own capital and five debtor countries; there are many more debtor countries than just Argentina, Chile, Brazil, Mexico and Venezuela which are the only ones I have taken into account. This shows that the debt crisis is not just a crisis for the debtor countries but a crisis to the world. If one of these big banks breaks down the rest will and nothing will work afterwards. I want to stress this as the common insight of our group. I want to stress this in order that you understand that to urge the provision of fresh money by these banks is quite something. It would of course enlarge their exposure and not, diminish it. But it is necessary that they provide fresh credit, it is unavoidable. But, of course, they do need good faith in order to do so, and in order to let a bank in New York, in good faith, to lend fresh money to a Latin American country, for instance, you need to show that bank that there is an agreement between that country and the IMF by which the country undertakes to adjust and that there is sensible prospect under that agreement that the country will be able to serve under the agreed conditions its debt and that there are sufficient mechanisms that will cap the interest payment or the payment as a whole which the country has to transfer.

In the later course of 1984, no bank could vis-a-vis its shareholders or the banking regulatory authorities claim to be in good faith about the expatriate transfer of interest from Latin America into their accounts in London or wherever it is, as the figures of the money to be transferred are rocketing into the sky. They have to be defined. We all agreed that there has to be a cap, a ceiling on interest rates, which, on the other hand, means sacrifices by the lender banks. Some of them may be able to sustain such sacrifices immediately, some of them may need a couple of years to write off what had been expected so far and what was in their books so far. Of course, it does need sacrifices by the creditor countries because the creditor countries will not get the expected amount of taxation from these banks. These are quite large sums which will be lost for the national treasury.

We list five proposals concerning commercial banks. Firstly, short-term debts ought to be consolidated to medium-term bonds under fixed interest rates. We say this in one line and a half, but to do it is an enormous exercise and there will be many, many vested interests who will not wish this to happen. Secondly, to reschedule over a multi-year period rather than the present practice of shortest-term rescheduling of debts, which means that some countries are coming up for rescheduling already a second time. Some, you can perceive, will come up for a third time. We want to replace this system by a multi-year rescheduling instead of shortest-term rescheduling.

The suggestion to restrict debt service payments to an agreed maximum percentage of a debtor country's export earnings may be controversial. There are countries who do export, take Brazil for instance. If Brazil would take all of her export earnings, what she gains from exporting coffee and whatever else, even a hundred per cent of the export earnings in hard currency would not be sufficient to service in a regular way her debt. Brazil just cannot do it. Brazil cannot use 90 per cent because she needs some goods and commodities from the rest of the world. She cannot use 80 per cent: if she doesn't buy anything in the world who would buy from Brazil? I would predict that this suggestion will create the greatest difficulties. It has to be done on a general principle basis, individually, country to country.

The proposal to capitalise interest is a little short in the report. We should have used an additional half sentence saying that beyond the fixed interest rate, beyond an interest rate which one has agreed upon between the country and the IMF, if interests go higher, then they ought to be capitalized. This will be done in a different way again from country to country or from a group of countries to a group of countries. But we agreed, both the industrialized countries experts and the developing countries experts, that there ought to be a partial capitalization of interest that otherwise would he due to be paid now and may come due in the oncoming future, and cannot be paid.

In the fourth instance, we deal with the creditor countries. We praised the Paris Club who has served the world quite well in its crisis management. But we also do mention, in the first place, the enormous pain for the debtor countries which has been created by the high-rise world interest rates. We urged OPEC and other central banks, but especially OPEC's central banks and OPEC governments, to consolidate their deposits —in private banks in New York or London or wherever— into medium-term bonds. There is money on call right now. This is very dangerous. We have seen it in Chicago, a fortnight ago. It ought to be transformed into medium-term bonds, which is not easy for those who have deposited the money, because in many cases it is their reserve of first resort and not of last resort. They wish to be able to draw from their accounts immediately. It is not easy for OPEC, for instance, to transfer short-term deposits into medium-term bonds. But also they have to sacrifice something. We also find that in some countries, - we did not mention the United States but this is the one we really have in mind - banking legislation ought to be harmonized or liberalized, as you call it, particularly with regard to the required ratio between capital and credit outlay.

Concerning development, there is nothing really new in our report and it is a condensed version of what all of us know and many of us have said time and again. We stress the necessity to cut into the excess of population growth in many areas. We stress what the developed countries have to do. New is that we say the IDA replenishment should be concluded rapidly and at the level which the World Bank has proposed even if not all countries will live up to their previously held share, that means even if the United States of America do not participate. The rest should go ahead. This is something which governments have not said so far, and don' like. Any government hides right now behind the United States and says "if the United States do not live up to their previous ratio of engagement, why should we?" —in Germany or in Belgium or in Canada or wherever it is.

I would like to mention that the United States of America is not mentioned here but the other big world power is not named here either. I wish to bring to the attention of this Council that the Soviet Union is not participating in all these schemes which I think is a mistake. Parallel to what we proposed to you about the World Bank, the IMF and the IDA we also wish to see a substantial increase in the World Bank capital while developing countries on the other hand are addressed in a way that is not necessary for me to explain here.

The chapter on trade and protectionism is almost totally covering the same ground that is being covered by the separate reports before the Council on trade and on the least developed countries.

Let me turn to policy coordination. It is a nice headline for a very ugly fact. The headline does not mention the country which really has been addressed here. The country that is really being addressed is the United States of America and especially their budget. On a very personal basis, I would like to say a few words. Since I was a grown-up man, over thirty years, I have been a close friend and will remain so of the United States of America. There are many things which I deeply respect, some which I envy. I have a great love for the United States. On the other hand, it is necessary that one does have the courage not only to criticize them, but to tell them what they do to the rest of the world. If you listen to the speeches of the President or the two would-be Presidents, Mr. Mondale and Mr. Hart, you do not find that any of them, as far as they deal with monetary economic and fiscal policies, do understand that the high budgetary deficits have created, number one, an enormously high level of interest rates and that this enormous level of interest rates was necessary in order to suck into the United States money and capital from the rest of the world. The United States right now is the greatest net importer of capital. The richest economy is the greatest user of foreign savings. The high interest rates have also aggravated the burdens of the debtor countries, of course. The high interest rates have also led to a situation in Europe and elsewhere in the world in developed countries where you make much higher profits if you invest the money that you have earned as a corporation or as an individual, if you invest that money in the American money market or in American Treasury bonds rather than invest it into real capital in your own firm or your own country. This is one of the main reasons of the still much too high unemployment figures in the industrial part of the world. This, I do not understand and it is a very difficult question for America. They do not wish to understand. Some of them don't. Others don't wish to. It is a very difficult question of tact and diplomacy, whether and, if yes, how could this Council effectively bring home that message to the United States in a campaign year when anything which we say will be used by some against the opposition and by some against the incumbent Administration. But we did feel that this is one of the most outstanding single cause of a number of troubles all over the world.

Under the heading of policy coordination, we speak of the necessity to coordinate fiscal and monetary policies. We also say very clearly that the present deficit and also the trade deficit of the United States is in the short run beneficiary to many other countries —for instance Germany right now exports much more to the United States than early on because the dollar rate is unfavorable to American industry and favorable to European industry —, and there is an enormous demand pull in the United States - if you have big deficits, you create a demand pull and the demand pull also pulls into the United States goods from other countries. But we equally say very clearly that this present beneficial effect has severe risks and disadvantages because, in any event, it is not sustainable in the longer run. The United States will have to curtail their budgetary deficit and if they don't do it we might even see higher interest rates and we might see "the ever present danger of a loss of confidence in the dollar", which might precipitate a depreciation that would oblige the Federal Reserve Board to raise interest rates further, risking renewed deep recession. It is all said in a way that is not insulting and in an expertise language. This is what one really means under the heading of policy coordination: the United States' fiscal policy and therefore its interest rates and exchange rates are out of coordination with the rest of the world.

In the end, we say a few things on international monetary reform. We re-state what the InterAction Council has already stated, namely that the present monetary arrangements have not proven satisfactory. But we also said that a return to the Bretton Woods system is impossible, precluded by the fundamental changes in the world economy over the last fifteen years. We were aware of all the proposals, discussions that do exist in the world right now on monetary reform. However, we felt that there is as yet no sign of a new consensus emerging, even not a new consensus among the major economic powers of the world. We therefore thought it was wise to just flag several issues, namely the need for greater stability of exchange rates between the dollar, yen and ECU. If another German had been present except myself, he even would have urged to replace ECU by Deutschmark but I would have preferred ECU. We also feel it is necessary that new and additional special drawing rights (SDRs) in the IMF should be allocated regularly every year over a period of several years. I personally do not like this paragraph but this was the consensus and I think it could be made agreeable to the rest of the world if one precludes by creating SDRs to finance inflationary policies in debtor countries or in recipient countries. Finally, we propose to strengthen the IMF by introducing arrangements which would make possible an increased borrowing by the IMF from a number of governments, from central banks who are in a situation to help others. We also say - and I repeat what I conveyed to you already - that currently, there does not seem to exist a chance for a constructive outcome of an international monetary conference. A greater degree of stability of exchange rates is clearly desirable and again, in a very diplomatic language, the report says why, because it helps to bring about greater economic discipline in governments who have to orient their monetary and fiscal policies towards the balance of payment situation and therefore stable interest rates.

I have deleted many details but would like to tell you also that the group that was convened at Wolfsberg wished to delete details. We even felt that this paper is much too long and much too specialized for the understanding of an average Foreign Secretary of any of our countries or Labor Secretary. I would of course not speak about our successors. They are wise as we have been, but we tried to be short and to delete the details, to forego any historic analysis.