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EBS/84/2

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January 5, 1984

To: *Members of the Executive Board*

From: The Acting Secretary

Subject: Sierra Leone - Request for Stand-By Arrangement

Attached for consideration by the Executive Directors is a request from Sierra Leone for a stand-by arrangement equivalent to SDR 50.2 million. Draft decisions appear on page 26.

This subject will be brought to the agenda for discussion on a date to be announced.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Enweze, ext. (5)8650.

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

SIERRA LEONE

Request for Stand-By Arrangement

Prepared by the African Department and the Exchange and Trade Relations Department 1/

(In consultation with the Fiscal Affairs, Legal, and Treasurer's Departments)

Approved by Oumar B. Makalou and S. Kanesa-Thasan

January 4, 1983

I. Introduction

In the attached letter dated December 3, 1983, the Government of Sierra Leone requests a stand-by arrangement for a period of 12 months in support of a stabilization program covering the second half of 1983 and the calendar year 1984, in an amount equivalent to SDR 50.2 million, representing 86.7 percent of new quota. Of this amount, SDR 26.08 million would be made available from the Fund's ordinary resources and SDR 24.12 million from borrowed resources. Under the three-year extended arrangement that the Fund approved for Sierra Leone in March 1981 (SDR 186.0 million or 400 percent of former quota), Sierra Leone purchased a total of SDR 33.5 million before the arrangement became inoperative in June 1981, and was subsequently cancelled on April 6, 1982. In February 1983 Sierra Leone purchased an amount of SDR 20.7 million (35.8 percent of new quota) under the compensatory financing facility in respect of an export shortfall for the year ended June 1982.

1/ Discussions that provided the basis for the proposed stand-by arrangement were held in Freetown during the periods February 21-March 2, 1983; June 8-24, 1983; July 27-30, 1983; and November 9-15, 1983; discussions were also held in Washington during the 1983 Annual Meetings, and the negotiations were concluded in Washington during November 28-December 3, 1983. Staff members participating in the missions were Mr. Enweze (head-AFR), Mrs. Mitchell (ETR), Mr. Duran (AFR), Mr. Kakoza (AFR), Mr. Fetherston (FAD), Mr. Sukachevin (ETR), Mr. Dublin (AFR), Mr. Abrams (ETR), Mr. Yao (BUR), Mrs. Selassie (secretary-AFR), Mrs. Buggs (secretary-AFR), and Miss Wood (secretary-AFR); Mr. Calamitsis (AFR) participated in the discussions in February/March. Messrs. Makalou (AFR), Bhatia (AFR), and Kanesa-Thasan (ETR) participated in the concluding negotiations in Washington during November/December. Mr. Sangaré, Executive Director for Sierra Leone, and Mr. Mtei, Alternate Executive Director for Sierra Leone, participated in parts of the June and the November discussions, respectively, in Freetown.

As of November 30, 1983, Fund holdings of leones subject to repurchase amounted to SDR 45.0 million (77.8 percent of new quota), excluding SDR 20.7 million (35.7 percent of quota), purchased under the CFF. Full use of the requested stand-by arrangement, together with scheduled repurchases, would raise Fund holdings of leones subject to repurchase to SDR 83.6 million (or 144.4 percent of new quota), excluding purchases under the CFF.

According to the phasing of the proposed stand-by arrangement (Table 1) purchases may be made in four installments. An amount equivalent to SDR 10.0 million (19.9 percent of the amount of the stand-by arrangement) would be available upon Executive Board approval of the arrangement. The second purchase of SDR 9.0 million may be made by Sierra Leone after meeting the performance criteria for end-March 1984. The third purchase of SDR 17.6 million will be subject to the satisfaction of the end-June performance criteria and the completion of the review of the program by July 31, 1984, at which time understandings will be reached with the Fund on producer prices, incomes policies, exchange rate, interest rate, budgetary and other policies. The final purchase of SDR 13.6 million will be effected after successful compliance with the end-September performance criteria to be established at the time of the mid-term review of the program.

II. Performance under the 1980/81 Program and Recent Economic Developments 1/

In early 1981 the Sierra Leone Government embarked on a program of structural adjustment covering the period 1980/81-1983/84 (July-June). Performance under the program in 1980/81 was not satisfactory; adverse external developments invalidated some of the major assumptions underlying the program and there were also slippages in policy implementation. As a result, the budget deficit/GDP ratio was twice the programed level, and was financed mainly by domestic bank borrowing. Thus, the end-June 1981 ceilings on net credit to the Government and on total domestic credit were greatly exceeded, though private sector credit expansion was kept within its implicit limit. The external payments position also deteriorated: the current account deficit, including official transfers, exceeded program targets by about 3 percentage points of GDP, and as net capital inflows were lower than had been foreseen, the overall balance of payments deficit exceeded the program target by a wide margin. The performance criteria on external arrears and external borrowings in the one-to-five years' maturity were also not met. Efforts to initiate corrective action were largely stalled by a failure to reach understandings with the Fund on the exchange rate question, and the extended arrangement became inoperative in July 1981.

1/ For detailed analysis of recent developments and performance under the 1980/81 program, see SM/83/200 (9/7/83) and SM/83/202 (9/21/83).

Table 1. Sierra Leone: Proposed Schedule of Purchases and Repurchases during the Stand-By Period

(In millions of SDRs)

	Operations in 1984				
	Jan.-March	April-June	July-Sept.	Oct.-Dec.	Total
Purchases	10.00	9.00	17.60	13.60	50.20
Ordinary resources	5.98	4.50	8.80	6.80	26.08
Borrowed resources	4.02	4.50	8.80	6.80	24.12
Repurchases					
Stand-by and extended arrangements	2.13	2.13	2.13	4.28	10.67
Net purchases	7.87	6.87	15.47	9.32	39.53
	(In percent of new quota) 1/				
	November 1983	March 1984	June 1984	Sept. 1984	Dec. 1984
Fund holdings subject to repurchase (end of period)	113.5	125.4	137.3	164.0	180.1
Under compensatory financing facility	35.7	35.7	35.7	35.7	35.7
Under tranche policy	77.8	89.7	101.6	128.3	144.4

Sources: IMF, Treasurer's Department; and the stand-by arrangement contained in Attachment A.
1/ New quota of SDR 57.9 million under the Eighth General Review.

During 1981/82 and 1982/83, Sierra Leone's economic and financial situation continued to deteriorate (Table 2): observed real growth stagnated, as diamond production and agricultural output (measured by the official purchases of these commodities for export) continued to be depressed, in part because of the high incidence of smuggling; expansionary budgetary and credit policies continued to exacerbate internal and external imbalances; the foreign exchange situation remained very tight, in part because of high import prices, but also because of the weak enforcement of surrender requirements for export proceeds. As a result of these factors, the inflation rate accelerated sharply, the debt servicing problem became more acute, gross reserves were virtually depleted, and external arrears continued to accumulate rapidly.

III. Adjustment Program for 1983/84

1. Introduction

Against this background, the Sierra Leonean authorities commenced discussions with the Fund staff on the elements of a stabilization program. As a result of these discussions, effective December 17, 1982, a dual exchange rate system was introduced under which approximately half of Sierra Leone's total foreign exchange transactions were to be effected in a commercial market, where the rate was to be determined by the forces of supply and demand, in the context of fortnightly foreign exchange auctions (EBS/82/240). During these auctions, the rate struck remained in the narrow range between Le 2.40 = US$1.00 and Le 2.50 = US$1.00; the base rate remained unchanged at Le 1.25 = US$1.00. Effective July 1, 1983, Sierra Leone unified the official and commercial rates of exchange for the leone at the rate of Le 2.50 = US$1.00; this rate implies a devaluation of 50 percent (100 percent in local currency terms) of the exchange rate (EBS/83/149). At the same time several key policy measures were enacted in the framework of a stabilization program: the measures were both far-reaching and wide-ranging, and encompassed substantive actions in the areas of exchange rate, producer pricing, fiscal, and monetary policies.

2. Production and investment policies

The producer price increases in the agricultural sector granted during 1982/83 proved insufficient to discourage smuggling to neighboring countries, given the shortage of foreign exchange and implicit leone prices which could be obtained from trading in the parallel market. Accordingly, the Government announced substantial increases in producer prices on July 1, 1983 well in advance of the 1983/84 crop season. Specifically, these increases were 82 percent for coffee, 93 percent for cocoa, 82 percent for palm kernels and 118 percent for ginger. As a result of these increases the smuggling of agricultural exports is expected to be sharply curbed as Sierra Leone's producer prices have become more competitive in U.S. dollar terms with those in neighboring countries. With the assistance of the World Bank and other donors, the Government is also pursuing efforts to increase the production of these export crops.

Table 2. Sierra Leone: Selected Economic and Financial Indicators, 1978/79-1983/84 1/

	1978/79	1979/80	1980/81	1981/82	1982/83	1983/84 Program
	(Annual percent change, unless otherwise specified)					
Income and expenditure						
GDP at constant factor cost	6.0	4.1	0.5	—	—	1.0
GDP at current market prices	21.1	12.3	15.8	17.0	27.5	25.2
Gross domestic expenditure at current prices 2/	24.8	19.7	13.5	16.5	20.6	23.0
Consumer prices (average)	14.1	19.3	13.7	26.3	49.4	40.0
External sector (on the basis of SDRs)						
Exports, f.o.b.	-12.3	44.7	-25.7	-9.9	-19.9	39.2
Imports, f.o.b.	31.1	24.3	-10.4	2.0	-28.4	-8.0
Oil imports, f.o.b.	69.0	37.1	25.7	68.6	-34.6	14.7
Diamond export volume	9.1	-20.5	-32.9	-29.4	21.3	1.0
Terms of trade (deterioration -)	-26.1	9.8	-7.2	5.1	11.5	...
Nominal effective exchange rate 3/ (depreciation -)	-4.2	-5.4	0.4	4.7	5.5	...
Real effective exchange rate 3/ (depreciation -)	0.6	-2.1	5.0	23.5	20.6	...
Government finance						
Total revenue and grants	8.3	10.3	18.9	-9.6	-12.0	55.3
Total revenue	6.9	—	25.4	-13.6	-14.8	36.4
Total expenditure 4/	20.6	15.1	21.7	0.4	0.4	17.6
Money and credit						
Domestic credit	35.5	21.4	39.5	31.9	39.4	23.8
Government	36.3	28.1	44.7	38.1	44.3	24.3
Private sector	33.3	3.8	22.4	7.8	15.3	21.2
Money and quasi-money (M_2)	28.3	16.7	3.6	25.5	36.0	29.3
Velocity (GDP relative to M_2)	4.8	4.6	5.2	4.8	4.5	4.4
Interest rate 5/ (annual rate on one-year deposits)	8.5	11.5	11.5	11.5	11.5	13.5
	(In percent of GDP, unless otherwise specified)					
Overall government deficit (cash basis)	11.3	12.3	11.5	10.3	13.5	8.0
Overall government deficit (commitments basis)	11.3	12.3	13.3	12.9	11.4	8.0
Domestic bank financing	5.7	4.8	8.5	8.9	11.3	7.1
Percent of initial money stock	35.2	26.1	45.5	54.1	69.3	40.3
Foreign financing	4.5	6.1	2.4	2.0	2.0	0.7
Gross domestic investment 2/	13.4	16.3	13.5	11.6	8.6	9.8
Gross domestic savings	5.2	0.9	0.4	-1.0	2.1	5.2
External sector						
Current account deficit (millons of SDRs)	141.0	145.1	157.8	181.5	128.5	75.6
Ratio to GDP	18.7	17.2	16.1	15.9	10.3	8.0
Balance of payments deficit (millions of SDRs)	47.9	45.6	122.2	120.2	70.5	75.0
Ratio to GDP	6.4	5.4	12.5	10.5	5.7	7.9
External debt 5/	29.5	31.2	30.4	26.9	28.9	46.8
Inclusive of use of Fund credit 5/	31.1	34.3	33.2	30.8	34.0	49.2
External debt service 6/ as percent of exports 7/	33.7	24.8	40.5	40.3	59.9	50.1 8/
Gross official foreign reserves 5/ (months of imports)	1.5	1.3	0.8	0.5	0.6	...
External payments arrears 5/ (millions of SDRs)	38.6	54.7	113.3	199.5	254.9	153.9

Sources: Data provided by the Sierra Leonean authorities; and staff estimates.
1/ Fiscal years July/June.
2/ Includes changes in stocks.
3/ Trade-weighted; reflects official rate only.
4/ Commitments basis, i.e., including unpaid obligations.
5/ End of period.
6/ Debt service due.
7/ Exports of goods only.
8/ Does not include impact of rescheduling.

In the case of rice, the producer price was raised by 43 percent in February 1983. In an effort to encourage greater domestic production, the authorities have given a commitment to raise the producer price further by at least 5 percent by February 1984. As far as the distribution of imported rice is concerned, effective July 1, the Sierra Leone Produce Marketing Board (SLPMB) was divested of its monopoly right to import rice in the interest of improving resource allocation and of avoiding the possibility of a budgetary subsidy. To facilitate private sector participation in this activity, the retail price of rice was raised though the authorities continued to control profit margins in order to prevent excessive profiteering.

The IBRD is presently engaged in preparatory work for a sectoral adjustment loan in the agricultural sector. The loan (US$29.4 million), which is scheduled to commence in July 1984, is for a program which combines elements of institutional reform and investment projects. The areas of institutional reforms which have been identified include the proposed merger of the Ministry of Agriculture and Forestry with the Ministry of Natural Resources, the reduction in the size of the payroll of the daily-wage staff of these ministries, the reorganization of the financial and accounting systems of the ministries, and the integration of the existing agricultural development projects within the Ministry of Agriculture.

The Sierra Leonean authorities have prepared a draft of the second National Development Plan covering the period 1983/84 to 1985/86 which projects planned public investment at Le 702 million in current prices. Reflecting the emphasis on improving infrastructure and economic services, investment in electricity accounts for 35 percent of the planned total while investment in agriculture and mining accounts for 24 percent and 11 percent, respectively.

To reverse the declining trend in the production of alluvial diamonds, the authorities have agreed along with the Sierra Leone Selection Trust (SLST) to establish a Kimberlite underground mining project. Under the terms of the shareholders' agreement signed in July 1983, the Government's share in DIMINCO, the management group, would be 60 percent and SLST's 40 percent. The authorities are at present involved in negotiating the arrangement to finance the cost of the project, estimated at US$140 million, with the prospective purchasers of the Kimberlite diamonds. It is estimated that construction and production will commence simultaneously in July 1984.

The Bumbuna hydroelectric project, costing a projected US$217.6 million, is to be constructed, starting in 1987. Preparatory work on construction camps amounting to US$20 million has been financed by the Italian Government and IDA has already committed US$20 million to the project. A donors' conference for this project which is to be sponsored by the IBRD is awaiting the Government's review of an IBRD study which has evaluated the impact of the project on the economy. Meanwhile the IBRD is considering a project for US$39 million to be disbursed during the next two years to rehabilitate the electricity distribution system in Freetown.

3. Prices and incomes policy

The unification of the exchange rates with effect from July 1 has had a direct impact on the domestic prices of oil and oil-related products. The price of premium gasoline was increased by 47 percent, from Le 3.40 to Le 5.00 per gallon (equivalent to US$2.00 per gallon), and the price of gas-oil rose by 50 percent, from Le 2.66 to Le 4.00 per gallon (equivalent to US$1.60 per gallon). On July 28, in recognition of the increased costs of providing transportation services, official approval was given to increase taxi and bus fares by an average of 76 percent. The increase in the prices of gasoline and of gas-oil on July 1 did not, however, complete the pass-through of increased costs associated with the exchange rate adjustment. The authorities have given an undertaking to complete the pass-through by the first week in March, when it is expected that the prices of petroleum products will rise on average by Le 1.02-Le 1.34 per gallon.

With regard to wage and salary policies, the program emphasizes the need for continued moderation. On July 1, the authorities announced an average increase of 20 percent in salaries for government workers following the substantial devaluation of the leone and after a period of almost three years during which there had been no increase while the annual inflation rate averaged about 30 percent. The authorities do not intend to grant additional increases during the period of the stand-by arrangement; incomes policy for the 1984/85 fiscal year will be examined within the context of the review of the program.

4. Fiscal policies

In the fiscal area, the program targets a reduction of 3.4 percentage points of GDP in the overall deficit (commitments basis), from 11.4 percent in 1982/83 to 8.0 percent of GDP in 1983/84 (Table 3). Including the impact in 1982/83 of the substantial net reduction in domestic arrears effected in that year, the overall deficit on a cash basis is programed to decline by 5.5 percentage points, from 13.5 percent to 8.0 percent. Net foreign financing is projected at Le 18.3 million (0.7 percent of GDP), while bank financing of the government deficit is to be limited to Le 177.7 million (7.1 percent of GDP, or 40.3 percent of beginning money stock), compared with Le 224.8 million (11.3 percent of GDP, or 69.3 percent of beginning money stock) in 1982/83. Policy measures to achieve these targets feature restraint on all elements of expenditure, intensified efforts at revenue collection, notably from the agricultural sector, and improvements in financial management.

Table 3. Sierra Leone: Central Government Operations, 1981/82-1983/84

(In millions of leones)

	1981/82	1982/83	1983/84 Budget	1983/84 July-October Budget 1/	1983/84 July-October Actual	1983/84 Program
Total revenue and grants	206.3	181.5	324.2	108.1	...	281.8
Taxes on net income and profits	42.6	42.7	71.9	24.0	15.1	69.9
Of which: SLPMB	(--)	(--)	(26.0)	(8.7)	(--)	(24.0)
Taxes on goods and services	45.2	38.5	51.2	17.1	14.6	44.2
Import duties and fees	69.2	51.6	98.1	32.7	21.6	68.1
Export duties	14.0	5.4	5.8	1.9	1.2	5.8
Other revenue and grants	35.3	43.3	97.2	32.4	...	93.8
Total expenditure 2/	408.3	409.8	534.4	178.1	...	481.8
Current expenditure	248.8	261.7	364.2	121.4	...	341.8
Wages and salaries	(117.5)	(125.1)	(155.7)	(51.9)	(50.5)	(149.7)
Interest payments	(39.4)	(43.0)	(76.2)	(25.4)	(...)	(67.9)
Other	(91.9)	(93.6)	(132.3)	(44.1)	(32.5)	(124.2)
Development expenditure	94.9	100.0	170.2	56.7	...	140.0
Of which: domestic	(25.1)	(27.1)	(47.0)	(15.7)	(7.5)	(32.0)
Other expenditure	64.6	48.1 3/	--	--	--	--
Overall deficit (commitments basis)(-)	-202.0	-228.3	-210.2	-70.1		-200.0
Net change in domestic arrears (reduction -)	41.2	-41.3	--			--
Overall deficit (cash basis) (-)	-160.8	-269.6	-210.2			-200.0
Financing	160.8	269.6	210.2			200.0
Foreign	31.9	42.0	15.8			18.3
Drawings	(63.6)	(69.0)	(85.8)			(75.8)
Amortization	(-31.7)	(27.0)	(-70.0)			(-57.5)
Domestic	128.9	227.6	194.4			181.7
Banking system	(140.0)	(224.8)	(180.0)			(177.7)
Nonbank sources	(-11.1)	(2.8)	(14.4)			(4.0)
			(In per cent of GDP)			
Revenue and grants	13.2	9.1	13.0			11.3
Revenue	11.7	7.7	10.0			8.5
Total expenditure 2/	26.1	20.5	21.4			19.3
Current expenditure	(15.9)	(13.1)	(14.6)			(13.7)
Development expenditure	(6.1)	(5.0)	(6.8)			(5.6)
Other expenditure	(4.1)	(2.4)	(--)			(--)
Overall deficit (commitments basis)	12.9	11.4	8.4			8.0
Overall deficit (cash basis)	10.3	13.5	8.4			8.0
Bank financing	8.9	11.3	7.2			7.1
Percent of beginning money stock	54.1	69.3	40.8			40.3

Sources: Data provided by the Sierra Leonean authorities; and staff estimates.

1/ One third of budget estimates for the full year.

2/ Commitments basis.

3/ Comprises Le 26 million net lending to SLPRC, Le 14 million in subsidies associated with finance of oil payments at the commercial exchange rate, and Le 8.1 million in unpaid commitments in respect of the domestic counterpart of increases in arrears on external interest payments.

Total revenue and grants are programed to increase by 55 percent, or 2.2 percentage points of GDP, over the provisional 1982/83 outturn. This increase reflects the impact of the July 1 exchange rate unification on foreign trade-related receipts (equivalent to about 2.2 percentage points of GDP), higher revenues from the SLPMB following the expected supply effects of the substantial increases in producer prices (0.8 percentage points), and the conversion by the Federal Republic of Germany of loan disbursements to grants (0.7 percentage points), partly offset by the revenue effects (about 1.4 percentage points) of a contraction in import tax receipts: due to a sharp contraction in the value of imports, and a shift in their composition away from higher-taxed luxury items, collections from import duties and excises during the first four months of the financial year were Le 14 million below the budgeted rate. Under the new system introduced for 1983/84, whereby SLPMB is now subject to the profits tax instead of export duties, revenue collections are projected to be at least Le 24 million, to be paid in quarterly installments of at least Le 6 million; the first such payment was made in November, and subsequent installments are payable by the end of each quarter.

On the expenditure side, the program emphasizes firm restraint of both current and development outlays. Growth of current expenditures will be limited to 31 percent, implying a decline of about 7 percent in real terms: within this amount, the wage and salary bill is projected to rise by 20 percent, reflecting the average salary increase of a similar amount (the first increase for almost three years) which was announced in the 1983/84 budget. Growth of other current expenditures (i.e., excluding wages, salaries, and interest) will be held to 33 percent implying a 5 percent reduction in real terms, and development outlays, with a nominal increase of 40 percent, will also be somewhat lower in real terms than in 1982/83.

To meet the fiscal targets of the program while taking account of the revised revenue outlook, the authorities have identified reductions in all major expenditures categories below the originally budgeted levels. For other current expenditure, these reductions amount to Le 21.1 million, of which Le 13 million is required to offset the estimated cost (not included in the budget estimates) of the temporary subsidy arising from the incomplete pass-through of the effects of the July 1 exchange rate adjustment on prices of petroleum products; reductions in development expenditure are targeted at Le 30.2 million, of which the local cost component would account for Le 15 million. The program projections for wages and salaries reflect adjustment for an overprovision of some Le 6 million in the original budget estimates of the impact of the salary increase; in addition, vacancies are to be filled only in exceptional circumstances, and no increase in salaries is envisaged during the remainder of the stand-by period. Projected domestic interest payments take account of the fact that only one half-yearly coupon payment is due in 1983/84 on new securities issued to convert outstanding ways and means advances, whereas the budget provided for a full year's interest on these obligations, while provision for external debt service is based on anticipated results of debt rescheduling. Reflecting the authorities' policy of expenditure restraint, during the first four months of 1983/84, non-interest current expenditures were Le 13.0 million below the budgeted rate.

Implementation of appropriate expenditure restraint under the program will be supported by measures to strengthen financial management. Expenditures under both the current and development budgets will be controlled through a new system of quarterly allotments, and will be monitored through regular reporting of actual developments to the staff. No increase in domestic arrears will be permitted during the program period, other than on a temporary basis in respect of the domestic counterpart of external debt service payments which are expected to be rescheduled. The program includes as fiscal performance criteria, ceilings on net credit from the banking system to Government at end-March and end-June 1984; in addition, an indicative target has been established for December 1983. To improve the monitoring of budgetary developments and prevent the accumulation of domestic arrears in respect of external debt service payments which will not be rescheduled, a special blocked account for the domestic counterpart of official external debt service payments is to be established at the Bank of Sierra Leone by end-December 1983. Transfers to this account from the Government's regular accounts will comprise an initial sum of Le 29.0 million less actual debt service already paid and debited to the Government during 1983/84 prior to establishment of the blocked account, to be followed by two quarterly payments, each of Le 19.35 million, due by end-January and end-April 1984. These transfers are calculated such that adequate provision is made from domestic budgetary resources for the programed leone counterpart of external debt service payments, after allowing for the impact of rescheduling (Table 4); should the actual result of rescheduling prove to be less favorable than assumed for the program, any shortfalls in the provision made in the blocked account as of end-March and as of end-June will be made good by additional transfers from the Government's regular accounts before the end of the month concerned and within the existing credit ceilings established for those dates.

5. Money and credit

Monetary and credit policies during the program period are designed to eliminate excess liquidity in the economy, thereby reducing excess demand and inflationary pressures while at the same time providing for the legitimate credit needs of Government and the private sector. To achieve these objectives, measures to control commercial bank credit and liquidity have been implemented. On July 1, 1983 interest rates on commercial banks' deposits were increased by 2 percentage points, while the ceiling on commercial bank loan rates was abolished. At the same time, interest rates on government securities as well as the central bank's discount rate were increased by the same amount. The effective required liquidity ratio of the commercial banks was increased by 5 percentage

Table 4. Sierra Leone: Provision for Domestic Counterpart of Official External Debt Service, 1983/84

(In millions of leones)

	Total for Year				
	Originally due	After re-scheduling	First Half	Third Quarter	Fourth Quarter
Interest	28.40	26.10	8.20	8.95	8.95
On nonrescheduled obligations	...	16.40	8.20	4.10	4.10
Moratorium interest	...	9.70	--	4.85	4.85
Amortization on medium-and long-term loans	119.50	41.60	20.80	10.40	10.40
Total	147.90	67.70	29.00 1/	19.35 2/	19.35 3/

Sources: Data provided by the Sierra Leonean authorities; and staff projections.

1/ Blocked account for official external debt service to be opened by end-December 1983 with this amount less actual debt service already paid and debited to the Government prior to establishment of the account.

2/ Transfer due to blocked account by end-January 1984; any shortfall from the cumulative amount provided (Le 48.35 million) and actual debt service due in the first three quarters after rescheduling to be met by an additional transfer by end-March.

3/ Transfer due to blocked account by end-April 1984; any shortfall from the cumulative amount provided for the year (Le 67.7 million plus any required end-March adjustment as described in footnote 2) and actual debt service due after rescheduling to be met by an additional transfer by end-June.

points on September 1, 1983. Furthermore, the authorities have blocked at the Bank of Sierra Leone the bulk (about Le 40 million) of the domestic counterpart of the external payments arrears (amounting to Le 55.2 million or over 10 percent of total bank deposits) owed by the refinery to foreign oil companies; the remainder, approximately Le 15 million, is to be blocked by January 10, 1984. Given that overall credit developments in Sierra Leone are largely dominated by the Government's borrowing requirements, the authorities have decided to reduce bank financing of the overall budget deficit and to drastically curtail the Government's direct reliance on ways and means advances from the Bank of Sierra Leone. Domestic financing of the budget deficit will henceforth be provided by the issue of Treasury bills and development stocks. The increased interest rates on government paper are expected to induce the commercial banks as well as non-bank financial institutions to hold a higher proportion of government issues, while the increased bank deposit rates together with the lifting of the ceiling on bank loan rates should encourage the growth of bank deposits.

Total domestic credit is programed to rise from Le 850.3 million to Le 1,052.8 million or by 23.8 percent during 1983/84 compared to an overall increase of 39.4 percent in 1982/83 (Table 5). Credit to Government will be limited to an overall increase of Le 177.7 million or 24 percent compared to an increase of 44 percent in 1982/83. With regard to bank credit to the private sector, the Bank of Sierra Leone has issued directives to the commercial banks limiting the total increase in bank credit to the private sector in 1983/84 to Le 24.9 million, an increase of 21 percent over 1982/83.

Provisional data indicate that credit developments during the first four months of the program period have been characterized by a very rapid increase in credit to the private sector and a slow growth of credit to Government. The increase in credit to the private sector during this period has been due to several factors, the most important being: seasonal factors related mainly to the agricultural harvesting and marketing season; the near doubling of the producer prices of agricultural export crops which has increased the credit needs of buying agents; and the special needs of the diamond industry. These credit developments during the first half of 1983/84 are expected to be partly reversed during the second half of the program period as seasonal influences change and as the credit and liquidity control measures on commercial banks slow the pace of commercial bank lending. The slow growth of credit to the Government during the early months of the program period has been due largely to strict control on expenditure commitments and the nonpayment of external debt service which is expected to be rescheduled.

Table 5. Sierra Leone: Monetary Survey, 1982-84

(In millions of leones)

	1982		1983			1984		
	June	Dec.	March	June	Sept.	Dec.	March	June
Foreign assets (net) 1/	-236.96	-241.56	-243.38	-258.01	-278.51	-595.0	-635.0	-678.4
Central bank	-243.15	-250.56	-261.08	-280.19	-297.48			
Commercial	6.18	9.0	17.70	22.18	18.97			
Domestic credit	609.87	722.18	751.02	850.27	875.54	967.4	1,007.4	1,052.8
Claims on Govt. (net)	507.79	603.89	634.42	732.50	747.41	812.4	857.4	910.2
Claims on private sector	102.08	118.29	116.60	117.68	128.13	155.0	150.0	142.6
Money and quasi-money	324.49	419.64	435.14	441.29	513.24	525.6	549.9	570.6
Money	169.34	253.22	264.75	256.86	325.51			
Quasi-money	155.15	166.42	170.50	184.43	187.73			
Other items (net) 2/	48.42	60.98	72.50	150.97	83.79	-153.2	-177.5	-196.2

Sources: Bank of Sierra Leone; and staff projections.

1/ Net foreign assets are revalued at the new exchange rate (December-June). The revaluation counterpart is reflected in other items, net. For June 1984 net foreign assets shown reflect projected movements in net foreign assets, which are:

- Net use of Fund credit of Le 33.7 million.
- Counterpart of blocked oil arrears: Le 110.38 million.
- A decline in reserves of the Bank of Sierra Leone and commercial banks amounting to Le 11.8 million and Le 28.42 million, respectively.
- A cash reduction in arrears of Le 2.6 million; all estimates and projections are based on an SDR/Leone exchange rate of 0.38.

2/ Included under other items net is Le 15 million needed to be borrowed by the refinery in order for it to provide the counterpart of the $44.151 million in arrears. It should be noted that these will be blocked at an exchange rate of Le 1.25 = US$1, although in the revaluation of the central bank's liability the new exchange rate is used.

The programed increase in total domestic credit together with the targeted decline in net foreign assets of the banking system would be accompanied by an increase in broad money of Le 129.3 million or an increase of 29 percent over the level at the end of 1982/83, compared with an increase of 36 percent in 1982/83, and with a projected increase in nominal GDP of 25 percent in 1983/84. The program assumes that velocity will stabilize after a declining trend, with the restrictive stance of monetary and credit policies. The slowdown in the growth of broad money also takes into account the blocking of deposits relating to oil payments arrears during 1983/84.

Quarterly ceilings for domestic credit and for credit to the Government, which constitute performance criteria, have been set for end-March and end-June 1984 (Table 6); indicative targets have been set for end-December 1983. The credit ceilings for end-September, and the indicative ceiling for end-December 1984 will be set in the context of the mid-term review.

6. External policies and medium-term prospects

a. External policies

The principal external objectives of the program are a reduction in the current account deficit from 10.3 percent to 8.0 percent of GDP during 1983/84, and a decline in external arrears, principally through consolidation and rescheduling. The policies under the program include exchange rate action, measures to enlarge the supply of exportable goods, improved mobilization of foreign exchange resources through an overhaul of retention privileges and surrender requirements, and limitations on new foreign non-concessional borrowing. As of July 1, 1983, the official and commercial rates of exchange for the leone were unified at the rate of leone 2.50 = US$1. This rate implied a devaluation of 50 percent (100 percent in local currency terms) of the official rate of exchange. The authorities opted for a large one-step change in the rate in contrast to the alternative of moving toward unifying of the rates in stages, as previously discussed with the staff. At the same time, Sierra Leone abandoned the previous leone/SDR peg, and pegged the currency to the US dollar. Having made this substantial move in the rate, the authorities now intend to use the exchange rate more flexibly than in the past, adjusting it as necessary to encourage the flow of exports through official channels, moderate import growth and maintain their competitive position. As a result of the strengthening of the dollar in international currency markets, the real trade-weighted exchange rate 1/ of the leone has appreciated by 9.3 percent between July and October (see Chart). In order to avoid such unintended shifts in the effective rate, the authorities intend to move to a more appropriate peg for the leone. Exchange rate policy will be an important element in the mid-term review of the program, and understandings in this area will be reached at that time.

1/ The calculations are based on estimated price data.

CHART

SIERRA LEONE

NOMINAL AND REAL EFFECTIVE EXCHANGE RATES, TRADE-WEIGHTED

(1980=100)

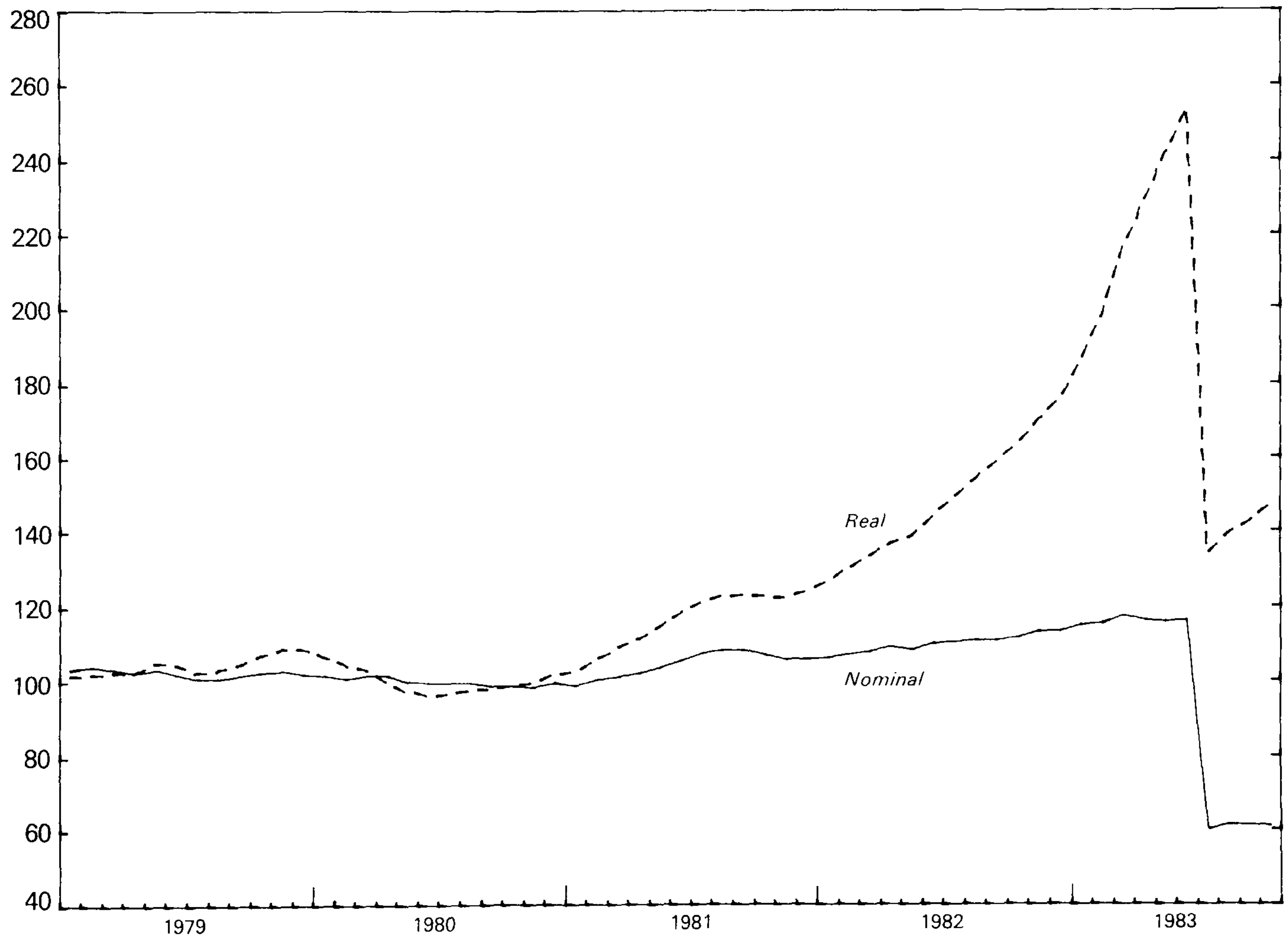

Table 6. Sierra Leone: Stand-By Arrangement--Quantitative Performance Criteria for March and June 1984

	Actual June 1983	Actual Sept. 1983	Projected Dec. 1983	March 1984	June 1984
			(In millions of leones)		
Net credit to Government from the banking system	732.5	747.4	812.4	57.4	910.2
Total domestic bank credit	850.3	875.5	967.4	1,007.4	1,052.8
			(In millions of U.S. dollars)		
External public debt					
Ceilings on new loans of maturities between 1-12 years 1/	--	--	10.0	10.0	10.0
Ceilings on new non-trade credits of maturities less than 1 year	--	--	15.0	15.0	15.0
			(In millions of SDRs)		
External payments arrears					
Minimum cash reduction by end of period 2/	--	--	--	0.5	1.0

1/ For Kimberlite and Bumbuna projects only.
2/ From the November 18, 1983 level of SDR 259.4 million. It is expected that there will be an additional reduction through consolidation and rescheduling.

The change in the exchange rate has enabled the Government to increase producer prices for coffee, cocoa, ginger and palm kernels as already noted, and the authorities expect that there will be a favorable supply response to the increased prices, and a diversion into official channels of agricultural exports, much of which were previously smuggled. At the same time, Sierra Leone is expected to benefit from improved world prices for all of its major agricultural exports, especially cocoa, palm kernels and ginger. Export volumes of coffee and palm kernels are also expected to increase substantially from the depressed levels of 1982/83, while cocoa export volumes should be maintained. Official exports of alluvial diamonds had already shown some increase in response to the creation of the dual exchange market in late 1982; it is expected that the trend will be maintained. Negotiations for the financing of the Kimberlite project are going forward with a view to starting construction as well as production in July 1984. The program also assumes that the volume of iron ore exports will double as activity at the Marampa mine is stepped up, while the new facility for drying bauxite will also come into operation. Total exports are projected to grow by 39 percent in value terms (Table 7).

Despite the programed improvement in exports, foreign exchange resources will continue to be severely constrained because of the heavy burden of debt service and the overhang of payments arrears. Reflecting this constraint as well as the devaluation of the leone and tighter demand management policies, imports are expected to show a further decline of 8 percent in 1983/84. After provision for necessary items, especially crude oil and rice, less essential imports are being licensed restrictively at present, on the basis of foreign exchange availability. Imports of crude oil will show an increase from the unusually low level of 1982/83, when foreign exchange constraints led to an interruption of the supply of crude oil and temporary reliance on imports of refined products. The Government is seeking to conserve supplies of petroleum products by increasing retail prices, and by improving the efficiency of the energy sector with the help of the IBRD. Imports of rice are being discouraged by enforcement of a 10 percent duty, and the Government is considering an increase in this levy. At the same time, the domestic producer price has been raised and will be raised again in February 1984, to stimulate import substitution. The overall result of these developments relating to exports and imports is expected to be a reduction in the trade deficit to less than half of its amount in the pre-program year.

Sierra Leone has been accumulating external payments arrears during the past few years, especially since the 1980 OAU conference for which heavy expenditures were undertaken. At the end of June 1983, these arrears amounted to SDR 255 million, more than twice the level of 1982/83 exports. From June until mid-November, total arrears rose further to SDR 259 million on account of unpaid official debt service obligations. In view of the extremely tight foreign exchange position, the program provides only for a token minimum cash reduction of SDR 1 million in arrears by June 30; a

Table 7. Sierra Leone: Medium-Term Balance of Payments Projection, 1982/83-1987/88

(In millions of SDRs)

	1982/83	1983/84	1984/85	1985/86	1986/87	1987/88
Trade balance	-82.0	-30.6	-41.6	-38.1	-10.6	-4.3
Exports	94.9	132.1	151.0	160.5	184.7	197.5
Imports	-176.9	-162.7	-192.6	-198.6	-195.3	-201.8
Of which:						
Oil	(49.7)	57.0	59.8	62.8	65.9	69.2
Rice	(24.5)	23.6	22.4	21.3	20.2	19.2
Kimberlite project	(--)	--	11.4	11.4	11.4	11.4
Energy rehab. project	(--)	--	11.3	11.3	--	--
IBRD sectoral project	(--)	--	3.8	3.8	3.8	--
Other imports	(102.7)	82.1	83.9	88.0	94.0	102.0
Services balance	-56.1	-55.0	-59.3	-62.1	-68.9	-75.1
(Of which: official interest) 1/	(-9.4)	(-10.8)	(-10.6)	(-15.8)	(-21.7)	(-26.7)
Private transfers	9.6	10.0	10.0	11.0	11.0	12.0
Current account	-128.5	-75.6	-90.9	-89.2	-68.5	-67.4
Long-term capital (net)	29.2	15.9	43.7	58.2	44.2	45.9
Official capital	19.0	9.6	22.9	27.9	13.2	14.6
(Transfers)	(18.3)	(26.2)	(22.2)	(22.2)	(22.2)	(22.2)
(Official Drawings)	(42.4)	(28.8)	(47.7)	(51.2)	(37.5)	(38.0)
of which:						
IBRD Sectoral Adjustment Loan	(--)	(--)	(9.0)	(9.0)	(9.0)	(--)
IBRD Energy Rehab.	(--)	(--)	(16.0)	(16.0)	(--)	(--)
(Repayments) 1/	(-41.7)	(-45.4)	(-47.0)	(-45.5)	(-46.5)	(-45.6)
Of which: Trust Fund	(0.3)	(1.5)	(2.8)	(4.7)	(4.9)	(4.6)
Private capital 2/	29.0	22.5	34.8	40.3	41.0	41.3
Export earnings retained	-18.8	-16.3	-14.0	-10.0	-10.0	-10.0
Short-term capital and errors and omissions	28.8	-15.3 3/	--	--	--	--
Overall balance before debt rescheduling	-70.5	-75.0	-47.2	-31.0	-24.3	-21.5
Net impact of rescheduling of debt and arrears 4/	34.1	43.7	19.8	14.5	13.1	2.9
Overall balance after debt rescheduling	-36.4	-31.3	-27.4	-16.5	-11.2	-18.6
Financing	36.4	31.3	10.8	-17.3	-23.3	-29.6
Arrears (decrease-) 5/	33.3	3.5	-10.0	-10.0	-10.0	-10.0
Fund credit						
(Drawings)	(20.7)	(19.0)	(31.2)	(...)	(...)	(...)
(Repurchases)	(-2.3)	(-6.2)	(-10.4)	(-7.3)	(-13.3)	(-19.6)
Net	18.4	12.8	20.8	-7.3	-13.3	-19.6
Reserves (increase-) 5/	-15.3	15.0	--	--	--	--
Financing gap	--	--	16.6	33.8	34.5	48.2

Sources: Sierra Leonean authorities; and Fund staff estimates.

1/ Before rescheduling.

2/ Includes an allowance of US$17.5 million per year from 1984/85 for Kimberlite diamond project.

3/ Includes payment due on a short-term commercial bank loan of SDR 23.8 million for oil imports, which has now been rescheduled.

4/ For 1983/84 rescheduling is assumed to include current payments due on Paris Club debt, supplier credits and short-term bank debt, as well as arrears in payments, short-term Eurodollar loans and on debt due to oil companies.

5/ The change in arrears is shown on a cash basis. For 1983/84 the figure includes a build-up of SDR 4.5 million in arrears before conclusion of the stand-by program and a reduction of SDR 1 million during the remainder of the year.

6/ Net foreign assets of the banking system.

ceiling for September 30 will be set during the mid-term review. In addition, however, the Government is negotiating a rescheduling of a major portion of its debt which should result in a substantial reduction in the level of arrears outstanding.

The largest category of arrears are those on commercial payments which are centralized in a "pipeline" against which deposits are blocked at the Bank of Sierra Leone, where they earn no interest; these arrears amounted to SDR 105 million at mid-November 1983. A number of individuals and firms whose applications for foreign exchange are blocked in the pipeline have recently requested permission to withdraw their deposits, indicating that they no longer have need of the foreign exchange. The Government intends to review these requests and to approve them selectively where there is adequate documentation to ensure that the foreign creditor is relinquishing his claim. This procedure would also reduce the level of outstanding arrears. If some part of these applications should be approved in future, and blocked deposits released, credit ceilings under the program will be adjusted downward correspondingly.

As indicated in Table 7, the schedule of debt repayments is particularly heavy in 1983/84, with the result that the capital account of the balance of payments would show a net outflow. Sierra Leone's debt service profile is generally unfavorable (Table 8), because of the relatively high proportion of the debt which is in the form of supplier credits with nonconcessional terms. As part of the program, the Government has negotiated the rescheduling of current payments and arrears due on supplier credits not subject to official guarantees in the exporting countries, payment due on a short-term commercial bank loan of US$25 million for oil imports as well as arrears on Eurodollar loans and on payments due to oil companies. The impact of these reschedulings on the balance of payments is estimated at about SDR 39.6 million in the current year. In addition, the Government will also request debt relief from the Paris Club as soon as possible. The stand-by arrangement prohibits new borrowing in the one- to twelve-year range except for an allowance of US$10 million for possible requirements for the Kimberlite and Bumbuna projects. New nontrade borrowing with maturity of less than one year is limited to US$15 million, consisting essentially of temporary bridging loans.

Sierra Leone's balance of payments problem has been aggravated by failure to collect foreign exchange earnings. Some of these are withheld through the existence of generous retention privileges, especially in the mineral sector. The privileges were usually granted to firms starting operations at a time when exports were very small, but now that exports have grown, the amount of foreign exchange involved has increased substantially. The Government has undertaken to review all of these contractual arrangements within the program period, and to ensure that retention is permitted only on a highly selective basis for essential imports and debt service obligations. More generally the authorities have been lax in enforcing surrender requirements; a Memorandum of Understanding on Surrender Requirements detailing measures which are being implemented in this area is attached to the letter requesting the stand-by.

Table 8. Sierra Leone: Debt Service Profile, 1982/83-1987/88 1/

	1982/83	1983/84	1984/85	1985/86	1986/87	1987/88
			(In millions of SDRs)			
Debt service payments (non-Fund)	51.1	56.2	57.6	61.3	68.2	72.3
Principal	41.7	45.4	47.0	45.5	46.5	45.6
Interest 2/	9.4	10.8	10.6	15.8	21.7	26.7
Debt service payments (Fund) 2/	5.7	10.0	13.7	13.6	22.3	28.2
Repurchases	2.3	6.2	10.4	7.3	13.3	19.6
Charges	3.4	3.8	3.3	6.3	9.0	8.6
Debt service payments (Fund and non-Fund)	56.8	66.2	71.3	74.9	90.5	100.5
Interest payments (Fund and non-Fund)	12.8	14.6	13.9	22.1	30.7	35.3
			(Debt service in percent of merchandise exports only) 3/			
Debt service ratio						
Debt service payments (non-Fund)	53.8	42.5	38.1	38.2	36.9	36.6
Debt service payments (Fund and non-Fund)	59.9	50.1	47.2	46.7	49.0	50.9
Interest payments (Fund and non-Fund)	13.5	11.1	9.2	13.8	16.6	17.8
Memorandum item						
Exports of goods 3/	94.9	132.1	151.0	160.5	184.7	197.5

Sources: Data provided by the Sierra Leonean authorities; and staff estimates.

1/ Based on debt outstanding as of end-June 1983, as well as projected new borrowing; excludes any assumptions relating to debt rescheduling.

2/ Including projected new borrowing as well as IMF Trust Fund.

3/ Data on exports of services are unavailable.

b. Medium-term prospects

The current program has been drafted in the context of a continuing difficult balance of payments outlook in the medium-term (Table 7). As the table indicates, a number of new projects will be started during the next four years, including the Kimberlite project (largely privately financed), the energy rehabilitation project of the IBRD which is the first phase of the Bumbuna project, and an IBRD sectoral project for agriculture. The medium-term balance of payments projections make no allowance for an IBRD Structural Adjustment Loan which is under discussion, or for the Bumbuna hydroelectric dam, for which the feasibility study is under review. The impact on the capital account and on imports of the projects which are included, is indicated in the table.

The medium-term forecast includes a detailed projection of exports, which shows an average annual value increase of 12 percent in the next four years, including an annual average increase of 5 percent in the volume of diamond exports, as Kimberlite output expands more rapidly than the depletion of alluvial reserves. Diamond prices are assumed to rise by 5 percent a year, in line with current world inflation. Export volumes of coffee and cocoa are assumed to grow on average by 5 percent and 2.5 percent per annum, respectively, with price increases averaging 3 percent and 1 percent. The volume of palm kernel exports is expected to drop initially by 25 percent below the high level of 1983/84 and then to remain stable, with an annual average price increase of 2 percent. Exports of bauxite (wet and dry), rutile, and iron ore are forecast to rise toward the limits of present productive capacity, while price increases for these mineral products are forecast to average about 6 percent per annum over the four-year period. The output and the price of gold are forecast to remain stable.

In projecting imports it has been assumed that the volume of oil imports will be stable because of conservation measures, while prices will rise by 5 percent a year. Rice imports are projected to decline by 5 percent per year, reflecting increased domestic production. After allowance for imports related to specific projects, residual imports have been projected to rise in nominal terms at an average annual rate of 6 percent from the low base level of 1983/84, implying continuing constraint.

For the capital account, inflows have been projected conservatively. Apart from the projects already mentioned, the only major development would be a decline in the retention of export earnings. No allowance has been made for short-term capital inflows, although these have averaged SDR 17 million per annum in the past five years. The forecast assumes further debt rescheduling (of current payments due, not already rescheduled) in each year, and a minimum cash reduction of SDR 10 million a year in external payments arrears. The impact of debt rescheduling will become less favorable over time as grace periods expire and payments fall due on rescheduled obligations, including past arrears. Thus the balance of payments projection shows a financing gap which rises from SDR 17 million in 1984/85 to SDR 48 million in 1987/88. No assumption has been made regarding further use of Fund resources after the arrangement now proposed or regarding any exceptional official aid beyond debt relief.

7. Summary of the financial program, 1983/84

a. Targets

(1) The current account deficit in the balance of payments is programed to decline to SDR 75.6 million in 1983/84 before debt rescheduling from SDR 128.5 million in 1982/83. However, the overall deficit would reach SDR 75.0 million compared with SDR 70.5 million in 1982/83, 1/ (before debt relief), because of a sharp rise in debt repayments falling due. After debt relief the overall deficit is projected to decline to SDR 31.3 million.

(2) The annual average rate of inflation is forecast to be about 40 percent during 1983/84 due to a substantial extent to the large devaluation effected at the beginning of the year; the annual average increase in the CPI during 1982/83 was 49.4 percent.

(3) Real GDP is projected to rise by 1.0 percent in 1983/84. A recovery in the official exports of agricultural crops and mineral products is expected to provide the impetus to growth.

b. Assumptions

(1) The rate of inflation in Sierra Leone's trading partners is expected to be 5 percent in 1983/84. Crude oil imports are projected to rise by 15 percent largely reflecting a return to more normal volumes. Rice imports are, however, assumed to decline with increased self-sufficiency. Other residual imports are projected to decline by 20 percent in 1983/84 as a result of continuing adjustment policies. The assumptions used in forecasting export growth at 39 percent in 1983/84 include some recovery of world commodity prices as well as the expectation that the 50 percent devaluation of July 1983 would divert exports of both diamonds and agricultural commodities into official channels (see 3 below) and, by permitting a substantial increase in producer prices for major crops, would expand the exportable supply of agricultural commodities.

(2) The rescheduling of Paris Club obligations is calculated on the basis of the terms granted in recent comparable cases.

1/ As a ratio to GDP, the current account deficit is to decline from 10.3 percent to 8.0 percent, while the overall deficit rises from 5.7 to 7.9 percent; however, changes in the ratios for 1983/84 are biased upward by the statistical impact of the devaluation on the leone value of external deficits.

(3) Short-term capital inflows (including errors and omissions) are expected to decline from SDR 28.8 million in 1982/83 to an outflow of SDR 15.3 million in 1983/84 based on the assumption that previously unrecorded private foreign exchange inflows are rechanneled through the official banking system. Gross international reserves are projected to decline by SDR 15 million during 1983/84 or by the full amount of reserve increase which occurred in 1982/83 as a result of borrowing undertaken by the commercial banks.

c. Principal elements of the program

(1) Fiscal policies

The central government budget deficit (commitments basis) is programed at Le 200 million (8.0 percent of GDP) in 1983/84, compared with an outturn of Le 228 million (11.4 percent of GDP) in 1982/83; bank financing of the budget deficit is limited to Le 177.7 million (7.1 percent of GDP), compared with Le 224.8 million (11.3 percent of GDP) in 1982/83. Understandings on fiscal policies for 1984/85 will be reached in the context of the mid-term review.

To help achieve the 1983/84 targets, the SLPMB is committed to paying at least Le 24 million in profits tax, and the authorities have identified expenditure savings amounting to Le 35.4 million on current expenditures and Le 30.2 million on development outlays. No further increase in government salaries is envisaged, and vacancies are to be filled only in exceptional circumstances.

Expenditures are to be monitored through a system of quarterly allotments, with actual developments reported to the staff within one month after the end of each quarter. No increase in domestic arrears will be permitted, other than on a temporary basis in respect of official debt service obligations subject to rescheduling. To prevent the accumulation of arrears during 1983/84 on official debt service obligations, the domestic counterpart of such payments will be channeled through a special blocked account at the Bank of Sierra Leone to be established by end-December 1983.

(2) Money and credit

Quarterly ceilings for March and June 1984 have been established as performance criteria for (a) total domestic bank credit and (b) net credit to Government from the banking system; in addition, indicative targets have been set for December 1983. Total domestic credit is programed to expand by 23.8 percent during 1983/84 (39.4 percent in 1982/83), while broad money is projected to expand by 29.3 percent (36.0 percent in 1982/83).

On July 1, 1983, interest rates on commercial bank deposits were raised by 2 percentage points, and ceilings on bank loan rates were abolished. The Bank of Sierra Leone discount rate and interest rates on government paper were also increased by 2 percentage points. On September 1, 1983, the effective required liquidity ratio of commercial banks was increased by 5 percentage points. The Bank of Sierra Leone has reintroduced the system of quarterly quantitative ceilings on commercial bank credit to the private sector.

(3) External sector

The exchange system was unified on July 1, 1983 at Le 2.50 per U.S. dollar, implying a 50 percent devaluation of the official rate for the leone (100 percent in local currency terms). The authorities intend to maintain a more flexible exchange rate policy; understandings on future exchange rate policy will be reached within the context of the mid-term review.

Other than a total amount of up to $10 million for the Kimberlite and Bumbuna projects, no new external loans in the maturity range 1-12 years will be contracted or guaranteed by the Government. New nontrade credits of initial maturity less than 1 year are subject to a ceiling of $15 million.

External arrears are to be reduced through cash payments by SDR 0.5 million as of end-March 1984, and SDR 1 million as of end-June 1984. The program includes the impact of debt reschedulings, including debts owed to the Paris Club.

Measures have been adopted to strengthen foreign exchange surrender requirements, and existing retention privileges are to be curtailed.

(4) Prices and production

Increases of between 82 and 118 percent in the producer prices for export crops were implemented July 1, 1983. The producer price of rice is to be increased by at least 5 percent by February 1984. The SLPMB's monopoly of rice imports has been abolished, and the retail price of imported rice partly decontrolled. To encourage greater energy conservation, the pass-through of increased oil import costs following the devaluation of the official exchange rate has been already effected up to 61 percent; the remaining 39 percent of the pass-through is to be implemented by the first week of March 1984, when prices of petroleum products will be increased by an average of between Le 1.02 and Le 1.34 per gallon.

Incentives to private sector investment are to be strengthened through implementation of a newly revised foreign investment code.

IV. Staff Appraisal and Proposed Decisions

The attached memorandum on the economic and financial program of the Government indicates that the Sierra Leonean authorities have embarked on a strong program of adjustment. The policies underlying the adjustment program are timely, considering that they are being implemented against a background of large and worsening internal and external imbalances experienced by Sierra Leone over a number of years, characterized by stagnant growth, expansionary budgetary and credit policies, high import costs, particularly of oil, weak enforcement of exchange surrender requirements, a virtually depleted level of gross external reserves, and increased accumulation of external arrears.

In the staff's judgement, there is now a strong sense of commitment on the part of the authorities to the implementation of substantial adjustment in an orderly fashion. Beginning in mid-1982, the authorities engaged in serious discussions with the staff on appropriate adjustment policies and have since made commendable progress in implementing them. Following a transitional dual exchange rate system, the official exchange rate of the leone was devalued by 50 percent (100 percent in domestic currency terms); the fiscal adjustment underlying the budget for 1983/84 represents a major major break with policies of the past; substantial increases in producer prices have already been announced; the interest rates on commercial banks' deposits have been increased and ceilings on lending rates have been eliminated; the liquidity ratio of the commercial banks has been increased; quarterly quantitative credit guidelines for the commercial banks' credit to the private sector are in place; additional measures to mop up the liquidity overhang in the economy have been effected; the monopoly hitherto enjoyed by the SLPMB the importation of rice has been abolished; the reschedulings of the arrears and debt service payments due in 1983/84 on non-Paris Club debts have been negotiated; measures to improve the surrender of foreign exchange earnings are being implemented; in addition, the authorities have approached the Paris Club to seek further debt relief. Furthermore, before the mid-year review of the program, additional measures will be implemented in the areas of producer prices, economic pricing of petroleum products, and exchange retention privileges. These, as well as the results of Sierra Leone's debt rescheduling with the Paris Club and the budgetary situation are to be reviewed by the staff before end-March 1984. Further, during the mid-year review before end-July 1984, understandings will be reached on policies for 1984/85 with particular attention to producer prices, incomes policies, exchange and interest rate policies and the budget for 1984/85.

Under the program, care has been taken, particularly in the form of prior actions, to minimize slippages in policy implementation. This approach reflects the authorities' firm commitment to implement a successful stabilization program, as well as an awareness of the importance of re-establishing Sierra Leone's credibility with the international financial and business communities. The Sierra Leonean authorities are also cognizant of the need to monitor the program carefully, and to implement further corrective measures, without delay, should some of the key underlying assumptions not be realized. They will remain in close contact with the staff, particularly with the assistance of the Fund representative in Sierra Leone. Also, as noted earlier, staff missions are programed to visit Sierra Leone twice during the first half of 1984 to review the program.

The authorities realize that Sierra Leone needs fundamental changes in its economic policies and that the current adjustment program, while substantial in itself, will need to be followed by a sustained implementation of policies directed at effecting structural changes over an extended period of time. They are also aware that the rescheduling of external debt will provide only a temporary easing of the country's serious balance of payments problems and that further external borrowings on nonconcessional terms, including from the Fund, will have to be strictly limited.

In the circumstances of Sierra Leone, the amount of resources that the Fund can offer directly has to be limited. The Fund's role has to be essentially that of a catalyst in promoting appropriate domestic adjustment on the one hand, and in mobilizing external support from non-Fund sources, including debt relief, for Sierra Leone's adjustment efforts on the other. In deciding on the size of the proposed arrangement (of 86.7 percent of quota), the management and staff took two exceptional circumstances into account. First is the fact that the current program had been under discussion with the authorities since mid-1982, and that, from late 1982, the authorities have implemented several important adjustment measures proposed by the staff, including a major exchange reform. A more important consideration was the fact that the measures already taken and to be taken under the program constitute a very substantial initial move toward balance of payments adjustment, by a country which has so far made relatively limited use of Fund resources. In light of these considerations, it was felt that the level of Fund support under the proposed arrangement could be more than would normally apply in cases where a member is facing severe external debt problems and where the attainment of balance of payments viability over the medium term is uncertain. It should be stressed, however, that the above-mentioned considerations will not apply to any further financial arrangements that Sierra Leone may have with the Fund. Moreover, it should be noted that purchases under the proposed arrangement are backloaded so that slightly more than 60 percent will be available only after the comprehensive review of the program in mid-1984.

Sierra Leone's exchange system involves a foreign exchange allocation scheme and external payments arrears giving rise to restrictions on payments and transfers for current international transactions which are subject to approval under Article VIII. The existing bilateral payment agreements with Fund members are inconsistent with Article VIII. The counterpart deposit requirement against commercial arrears constitutes a multiple currency practice also subject to approval under Article VIII.

Measures are already being taken to liberalize the exchange system and to reduce outstanding external payments arrears. These restrictions on payments and transfers for current international transactions were not approved by the Executive Board in October 1983 when it discussed the staff report on the 1983 Article IV consultation. The staff now recommends their approval.

On the basis of the measures which are already in place, and those which are being implemented, the staff believes that the program for which the Sierra Leonean authorities have requested Fund assistance in the form of a stand-by arrangement is deserving of Fund support. As noted earlier, the authorities have also indicated that they will review the program and adopt additional appropriate measures, when necessary, to ensure that the objectives of the program are achieved.

Accordingly, the following draft decisions are proposed for adoption by the Executive Board:

A. Stand-by arrangement

1. The Government of Sierra Leone has requested a stand-by arrangement for the period January __, 1984 to January __, 1985, in an amount equivalent to SDR 50.2 million.

2. The Fund approves the stand-by arrangement attached to EBS/84/2.

3. The Fund waives the limitation in Article V, Section 3(b)(iii).

B. Exchange practices

1. Sierra Leone's exchange system involves restrictions on payments and transfers for current international transactions, including external payment arrears, and a multiple currency practice as described in EBS/84/2. The Fund notes the intention of the authorities to remove these restrictions as soon as possible. In the meantime, the Fund grants approval for their retention until July 31, 1984 or the completion of the 1984 Article IV consultation with Sierra Leone, whichever is the earlier.

2. Sierra Leone also continues to maintain bilateral payments agreements with Fund members. The Fund urges Sierra Leone to terminate these agreements as soon as possible.

Sierra Leone--Relations with the Fund
(As of November 30, 1983)

Date of membership:	September 10, 1962	
Status:	Article XIV	
Quotas:	Old: SDR 46.5 million New: SDR 57.9 million	
	Millions of SDRs	Percent of old quota
Fund holdings of leones:		
Total	112.2	241.3
Of which:		
compensatory financing facility	(20.7)	(44.5)
credit tranches	(11.5)	(24.7)
extended Fund facility	(16.3)	(35.1)
supplementary financing facility	(17.2)	(37.0)
SDR holdings:	SDR 91,135, or 0.5 percent of the net cumulative allocation of SDR 17.46 million	
Gold distribution:	21,396 troy ounces of fine gold	
Direct distribution of profits from gold sales:	US$3.99 million	
Trust Fund loans outstanding:		
Total	SDR 23.73 million	
First period	SDR 9.82 million	
Second period	SDR 13.91 million	
Technical assistance:	Sierra Leone is receiving technical assistance from the Fund in the central banking and budgetary fields. In September 1983 the Fund resident representative who was stationed in Freetown for the past two years returned to Washington; a new Fund representative is expected to be posted to Freetown shortly.	
Exchange practice under Article VIII:	Until 30, 1983 the leone was pegged to the SDR at the rate of Le 1 = SDR 0.731566. Effective July 1, 1983, the leone/SDR peg was abandoned, and the leone was pegged to the U.S. dollar at the rate of US$1.00 = Le 2.50. Sierra Leone maintains restrictions on payments arrears and a multiple currency practice arising from the nonpayment of interest on the leone counterpart of commercial arrears.	

Sierra Leone--Financial Relations with the World Bank Group
(As of September 30, 1983)

(In millions of U.S. dollars)

	Disbursed		Undisbursed	
	IBRD	IDA	IBRD	IDA
IBRD/IDA lending operations				
Agriculture	5.0	15.9	--	13.8
Education	--	10.2	--	20.0
Transportation	6.0	5.3	--	8.4
Power and utilities	7.7	10.2	--	3.0
Technical assistance	--	1.6	--	0.9
Total	18.7	43.2	--	46.1
Of which: repaid	(7.6)	(0.3)		
Total outstanding	11.1	42.9	--	46.1
IFC investment				2.1

Source: World Bank Group.

Sierra Leone--Stand-By Arrangement

Annexed hereto is a letter, with attached memoranda, dated December 3, 1983, from the Minister of Finance and the Governor of the Bank of Sierra Leone requesting a stand-by arrangement and setting forth:

a. the objectives and policies that the authorities of Sierra Leone intend to pursue for the period of this stand-by arrangement;

b. the policies and measures that the authorities of Sierra Leone intend to pursue during the first six months of this stand-by arrangement; and

c. understandings of Sierra Leone with the Fund regarding reviews that will be made of progress made in realizing the objectives of the program and of the policies and measures that the authorities of Sierra Leone will pursue for the remaining period of this stand-by arrangement.

To support these objectives and policies, the International Monetary Fund grants this stand-by arrangement in accordance with the following provisions:

1. For the period from January __, 1984, to January __, 1985, Sierra Leone will have the right to make purchases from the Fund in an amount equivalent to SDR 50.2 million, subject to paragraphs 2,3,4, and 5 below, without further review by the Fund.

2. (a) Purchases under this stand-by arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 10.0 million until March 31, 1983; the equivalent of SDR 19.0 million until June 30, 1984; the equivalent of SDR 36.6 million until September 30, 1984.

(b) None of the limits in (a) above shall apply to a purchase under this stand-by arrangement that would not increase the Fund's holdings of Sierra Leone's currency in the credit tranches beyond 25 percent of quota or increase the Fund's holdings of that currency resulting from borrowed resources beyond 12.5 percent of quota.

3. Purchases under the stand-by arrangement shall be made from ordinary and borrowed resources in the ratio of 1 to 1 until total purchases under the arrangement reach the equivalent of SDR __ million and thereafter from borrowed resources only, provided that any modification by the Fund of the proportions of ordinary and borrowed resources shall apply to amounts that may be purchased after the date of modification.

4. Sierra Leone will not make purchases under this arrangement other than the initial purchase in an amount equivalent to SDR 10.0 million, that would increase the Fund's holdings of Sierra Leone's currency

in the credit tranches beyond 25 percent of quota or increase the Fund's holdings of that currency resulting from purchases of borrowed resources beyond 12.5 percent of quota:

(a) during any period in which the data at the end of the preceding calendar quarter falling within the period of this arrangement indicate that:

(i) the ceiling on total domestic credit from the banking system described in paragraph 2c of Section II of the Memorandum on the Economic and Financial Program of the Government of Sierra Leone attached to the annexed letter (hereafter referred to as the Economic Memorandum); or

(ii) the ceiling on net domestic credit to the Government from the banking system described in paragraph 2c of Section II of the Economic Memorandum attached to the annexed letter; or

(iii) the target for the reduction of external payments arrears described in paragraph 3a of Section II of the Economic Memorandum attached to the annexed letter; or

(iv) the ceiling on contracting and guaranteeing of new nonconcessional external borrowing with a maturity of between 1 and 12 years described in paragraph 3a of Section II of the Economic Memorandum attached to the annexed letter; or

(v) the ceiling on the contracting and guaranteeing of new non-trade credits with a maturity of less than one year described in paragraph 3a of Section II of the Economic Memorandum attached to the annexed letter, is not observed;

(b) during the period June 30 to January ___, 1985, until understandings have been reached on the economic and financial policies and suitable performance criteria have been established for the remainder of the program period in consultation with the Fund as contemplated in paragraph 2 of the annexed Letter or after such understandings and performance criteria have been established, while they are not being observed;

(c) during the entire period of this stand-by arrangement if Sierra Leone

(i) imposes or intensifies restrictions on payments and transfers for current international transactions; or

(ii) introduces or modifies multiple currency practices;

(iii) concludes bilateral payments agreements that are inconsistent with Article VIII; or

(iv) imposes or intensifies import restrictions for balance of payments reasons.

When Sierra Leone is prevented from purchasing under this stand-by arrangement because of this paragraph 4, purchases will be resumed only after consultation has taken place between the Fund and Sierra Leone and understandings have been reached regarding the circumstances in which purchases can be resumed.

5. Sierra Leone's right to engage in transactions covered by this stand-by arrangement can be suspended only with respect to requests received by the Fund after (a) a formal ineligibility, or (b) a decision of the Executive Board to suspend transactions, either generally or in order to consider a proposal, made by an Executive Director or the Managing Director, formally to suppress or limit the eligibility of Sierra Leone. When notice of a decision of formal ineligibility or of a decision to consider a proposal is given pursuant to this paragraph 5, purchases under this arrangement will be resumed only after consultation has taken place between the Fund and Sierra Leone and understandings have been reached regarding the circumstances in which such purchases can be resumed.

6. Purchases under this stand-by arrangement shall be made in the currencies of other members selected in accordance with the policies and procedures of the Fund, and may be made in SDRs, if on the request of Sierra Leone, the Fund agrees to provide them at the time of purchase.

7. The value date of a purchase under this arrangement involving borrowed resources will be normally either the 15th day or the last day of the month, or the next business day if the selected day is not a business day. Sierra Leone will consult with the Fund on the timing of purchases involving borrowed resources.

8. Sierra Leone will pay a charge for this arrangement in accordance with the decisions of the Fund.

9. (a) Sierra Leone will repurchase the outstanding amount of its currency that results from a purchase under this arrangement, in accordance with the provisions of the Articles of Agreement and decisions of the Fund, including those relating to repurchase as Sierra Leone's balance of payments and reserve position improves.

(b) Any reductions in Sierra Leone's currency held by the Fund shall reduce the amounts subject to repurchase under (a) above in accordance with the principles applied by the Fund for this purpose at the time of the reduction.

(c) The value date of a repurchase in respect of a purchase financed with borrowed resources under this stand-by arrangement will be normally either the 6th day or the 22nd day of the month, or the next business day if the selected day is not a business day, provided that repurchase will be completed not later than seven years from the date of purchase.

10. During the period of the stand-by arrangement, Sierra Leone shall remain in close consultation with the Fund. These consultations may include correspondence and visits of officials of the Fund to Sierra Leone or of representatives of Sierra Leone to the Fund. Sierra Leone shall provide the Fund, through reports at intervals or dates requested by the Fund, with such information as the Fund requests in connection with the progress of Sierra Leone in achieving the objectives and policies set forth in the annexed letter and attached memoranda.

11. In accordance with paragraph 2 of the annexed letter, Sierra Leone will consult the Fund on the adoption of any measures that may be appropriate, at the initiative of the Government or whenever the Managing Director requests consultation because any of the criteria in paragraph 4 above have not been observed or because he considers that consultation on the program is desirable. In addition, after the period of the arrangement and while Sierra Leone has outstanding purchases in the upper credit tranches, the Government will consult with the Fund from time to time, at the initiative of the Government or at the request of the Managing Director, concerning Sierra Leone's balance of payments policies.

Washington, D.C.
December 3, 1983

Mr. J. de Larosière
Managing Director
International Monetary Fund
Washington, D.C. 20431
U.S.A.

Dear Mr. de Larosière,

The attached memorandum sets forth the economic and financial objectives of the Government's one-year stabilization programme for 1983/84; policies for 1984/85 will be articulated in detail in the context of the mid-term review of the programme. The attached memorandum includes measures which the Government has already taken in the areas of exchange rate policy, producer prices, money and credit, fiscal policies and external debt management; it also delineates the nature of additional measures which the Government intends to take during the programme period in order to meet the programme targets. In support of this programme, the Government of Sierra Leone requests use of Fund resources under a one-year stand-by arrangement in the amount of SDR 50.2 million.

The attached memorandum also indicates the performance criteria of the programme for the second half of FY 1983/84 (i.e., March and June). These performance criteria relate to (a) net government borrowing from the banking system; (b) total bank credit; (c) external payments arrears; (d) external debt contracted, guaranteed or authorized by the Government; and (e) the foreign trade and exchange system, including the import licensing regime. Before March 31, 1984 the Government of Sierra Leone will consult with the Fund staff on the implementation of the programme, including, in particular, the pass-through of increased oil prices, progress toward the reduction of external arrears, as well as of retention quotas, and toward the strengthening of foreign exchange surrender requirements, the results of debt rescheduling, and budgetary performance. Before July 31, 1984 the Government of Sierra Leone will consult with the Fund on the policies for 1984/85, and reach understandings on the performance criteria for September 1984 and the indicative targets for December 1984 and on producer prices, incomes policies, exchange rate, interest rate, budgetary and other policies.

The Government believes that the policies described in the attached memorandum are adequate to achieve the objectives of the programme. However, it will take any additional measures that might become necessary for this purpose. Furthermore, Sierra Leone will consult with the Fund, in accordance with Fund policies.

We have been instructed by His Excellency the President to transmit to you this letter as reflecting the policies and intentions of the Government of Sierra Leone.

Sincerely yours,

Dr. J. Funna
Governor
Bank of Sierra Leone

The Hon. S. Jusu-Sheriff
Minister of Finance

Attachments

WASHINGTON, D.C.

Memorandum on the Economic and Financial Programme of the Government of Sierra Leone

I. Introduction

1. In recent years, Sierra Leone has experienced serious economic and financial difficulties arising from a number of factors, including the depressed levels of prices of virtually all the country's exports, the high cost of oil imports, the vexed problem of smuggling, and the insufficient enforcement of surrender requirements for export proceeds. As a result, growth has stagnated and Sierra Leone's development efforts have been seriously hampered; in addition, since government revenues did not keep pace with the growth of expenditures, the Government has had to resort to bank borrowing on a large scale, and this in turn has exacerbated internal and external imbalances. Accordingly, gross reserves have been virtually depleted, external arrears have continued to increase rapidly, the debt servicing problem has become more acute, commercial and industrial activities have been seriously curtailed, and the rate of inflation has accelerated.

2. Efforts to deal with these problems in 1982/83 did not produce the desired results: although producer prices were increased, their levels remained relatively low and uncompetitive. However, the budget for FY 1982/83 made useful progress: current expenditures were strictly controlled at the commitment stage, and, for the first time in recent years, there were no extrabudgetary expenditures, while at the same time domestic arrears were substantially reduced. Despite these achievements, the overall budgetary deficit relative to GDP remained high. At a time when the rate of increase in credit to the private sector also accelerated, the resulting large amount of bank financing of the budget deficit continued to fuel monetary expansion, increase pressures on the exchange rate of the leone, and aggravate both the external imbalances and the inflation rate. Under these circumstances, the Government decided to intensify its efforts to implement appropriate and comprehensive measures in order to deal with the country's economic and financial difficulties.

II. Programme for 1983/84

1. Economic policies

a. In the agricultural sector, producer prices for the major crops, which had already been increased in 1982 and early 1983, have been raised again, well in advance of the 1983/84 crop season, so as to provide timely incentives for producers; the higher levels of producer prices have been made possible by the recent exchange rate action implemented by the Government. The increases are 82 percent in the case of coffee, 93 percent for cocoa, 82 percent for palm kernels, and 118 percent for ginger;

the Government believes that these higher prices will assist in increasing Sierra Leone's earnings for agricultural exports by attracting sales into official channels and reducing smuggling. In addition, the Government will continue its efforts to expand acreage, and improve farming methods with the help of extension services and assistance provided by the World Bank and other donors. Regarding imported foodstuffs, some 20 percent of the staple product, rice, is now imported. Whereas in the past all rice imports were channeled through the Sierra Leone Produce Marketing Board, the SLPMB has now been divested of its monopoly in this area, both to ease the financial burden on the SLPMB and to permit participation by the private sector. Controls on the retail price of rice have been eased with a view to encouraging domestic production. In addition, the Government intends to maintain and enforce collection of the 10 percent duty on imported rice, and is also contemplating an increase in this duty, in order to improve the competitiveness of local production. The producer price for rice was increased by 43 percent in February 1983; a further increase of at least 5 percent is envisaged for February 1984. The Government is also reviewing other policy options for stimulating local agricultural production in collaboration with the IBRD. Meanwhile, several foreign-financed projects, aimed at improving agricultural productivity, are being financed by the IDA, EEC, ADB, and other donors. The IBRD is presently considering a sectoral adjustment loan, which could start in mid-1984.

b. With respect to mineral production and exports, the Government has recently signed a new agreement for the mining of Kimberlite diamonds, Sierra Leone's major single resource. Further negotiations are being conducted with potential investors for the financing of the project; construction and full-scale production are tentatively scheduled to start in July 1984. Open-cast mining of the Kimberlite pipes is already under way, with output projected at 17,500 carats in 1983/84. In the meantime, although reserves of alluvial diamonds are gradually being depleted, the Government intends that the continued implementation of a more realistic exchange rate policy will discourage smuggling of alluvial diamonds and increase official receipts. The Government believes that the recent exchange rate action will increase the profitability of investment in the mining sector.

c. Planned public investment for the draft three-year Second National Development Plan covering the period 1983/84-1985/86 is targeted at Le 702 million, of which electricity is to account for 35 percent and agriculture 23 percent. However, the implementation of the three-year plan will be carried out in the framework of the annual development budget, taking account of the availability of domestic and foreign resources. For 1983/84 development expenditure was budgeted at Le 170 million, of which about 82 percent or Le 140 million would be provided by foreign financing; however, as indicated in the attached fiscal memorandum of understanding, further economies in this area have been delineated for the programme.

d. In the private sector, the Government's policy is to encourage private investment in export and in import substitution industries. In this context, while a major constraint has been the dearth of foreign exchange resources, the Government also considers the continued maintenance of a realistic exchange rate policy as important. In addition, the Government has now completed the review of the foreign investment code, with a view to attracting foreign investment in resource-based, exportoriented and import-substitution industries by creating appropriate incentives and guarantees. These incentives and guarantees will include protection against nationalization, preferential tax treatment, and the right to remit foreign capital, profits, and dividends subject to prevailing exchange controls.

e. In the energy sector, Sierra Leone remains dependent largely, for the time being, on imported oil. However, some economies have already been achieved in the consumption of oil as a result of high import prices, greater conservation efforts, and the scarcity of foreign exchange; imports of crude oil have amounted to just over 200,000 tons a year in the past two years, significantly less than in earlier years. The Government is actively reviewing the arrangements for procuring crude oil, with a view to reducing outlays of foreign exchange. The Government also plans to conserve on oil consumption still further, mainly through increased prices of petroleum products. Thus, effective July 1, 1983, with the unification of exchange rates, the pump price of gasoline was increased by 47 percent from Le 3.40 per gallon to Le 5 per gallon; taxi and bus fares were also increased by an average of 76 percent. However, the complete pass-through of the exchange rate effects will require a further increase in average petroleum product prices of Le 1.02 to Le 1.34 per gallon by the first week in March 1984. For the longer term, the Government is also trying to raise the necessary financing to start the construction of the Bumbuna hydroelectric power project, which would substantially reduce the need for imported oil. The IBRD, which is expected to convene a donors' conference for the project in 1984, has indicated that the earliest date at which the project could begin would be 1987. The Government is reviewing the IBRD evaluation of the Bumbuna project; the outcome of this assessment will be discussed during the review of the programme.

f. Domestic prices in Sierra Leone have been rising at an accelerated rate. The consumer price index rose by about 26 percent in 1981/82 and 49 percent in 1982/83; this acceleration reflects, in part, extensive parallel market activities which the Government is determined to tackle. The Government recognizes, however, that expansionary fiscal and monetary policies have also contributed to rising prices; consequently, it intends to bring these policies under firm control. With regard to wage and salary policies the Government believes in the need for continued moderation in view of the tight prospects for the budget in the medium-term. Accordingly, in its 1983/84 budget, the Government granted an average increase of 20 percent in salaries for government employees; the Government considers that this increase was justified by the substantial depreciation of the leone and the absence of any increase in salaries in the past three years, despite an average inflation rate of about 30 percent per annum during the same period. However, the Government does not intend to grant further increases in salaries during the remainder of the stand-by period.

2. Domestic financial policies

a. For the fiscal year 1982/83, the overall budget deficit on a cash basis (including the reduction of arrears) was Le 270 million or 13.5 percent of GDP; bank financing of the overall deficit amounted to 11.3 percent of GDP. Fiscal policy for 1983/84 has been formulated to support the Government's adjustment effort by reducing the overall budgetary deficit and its associated bank financing, which have contributed to the imbalances in the economy and to the pressures on the exchange rate of the leone. For 1983/84 the budgetary deficit is programmed at Le 200 million or 8 percent of GDP, a decline of 5.5 percentage points over the estimated outturn for last year. In addition, bank financing of the budget deficit will be limited to Le 178 million, about 7.1 percent of GDP. This represents a decline to 40.3 percent of beginning money stock in 1983/84 from 69 percent of beginning money stock in 1982/83. Furthermore, there will be no increase in domestic arrears, other than on a temporary basis for the domestic counterpart of external debt service payments which are expected to be rescheduled; this commitment will form an explicit element of the review of the programme. In order to improve the monitoring of budgetary developments, the programmed leone counterpart of current official external debt service payments will be channeled through a special blocked account at the Bank of Sierra Leone to be established by end-December 1983. Measures to facilitate the attainment of the fiscal targets for 1983/84 have been incorporated in a separate Memorandum of Understanding (Attachment II). Meanwhile, given the revenue shortfall from budget estimates (about Le 20.7 million for the first quarter), the Government has lowered expenditures correspondingly below budgeted estimates; for the first quarter of fiscal year 1983/84 non-interest expenditures are running at Le 19.2 million lower than budget estimates. The Government intends to continue with this policy of reductions in expenditures.

b. With regard to public enterprises, the one major subsidy generated by enterprise operations has been that paid to SLEC (now NPA) to cover its operating costs; these losses had been reduced, but not eliminated, by a 70 percent increase in electricity tariffs in March 1982, as recommended by the IBRD. The Government intends to discuss these issues further with the IBRD, and subsequently with the Fund staff during the review of the programme.

c. The Government considers that a restrictive monetary policy is an essential element of the adjustment effort. Total domestic credit, as defined in the technical memorandum (Attachment III), which rose by 39.4 percent in 1982/83, from Le 609.9 million at end-June 1982 to Le 850.3

million at end-June 1983, and which now stands at Le 873.0 million at end-October 1983, will increase by no more than Le 117.1 million between end-June 1983 and end-December 1983, and by no more than Le 157.1 million between end-June 1983 and end-March 1984, and by no more than Le 202.5 million for the whole of the financial year 1983/84. The limits on the expansion of total domestic credit will be reduced by the amounts of any approved withdrawals of blocked deposits from the commercial arrears pipeline. Within the overall limit, net credit to the Government (as defined in the technical memorandum mentioned above) which increased from Le 507.8 million at end-June 1982 to Le 732.5 million at end-June 1983, and which, as of October 31, stood at Le 732.9 million, will increase by no more than Le 79.9 million between June 30, 1983 and December 31, 1983; and by no more than Le 124.9 million between June 30, 1983 and end-March 1984; and by no more than Le 177.7 million for financial year 1983/84. The credit ceilings for end-September 1984, as well as the indicative ceilings for end-December 1984, will be established in the context of the programme review with the Fund. A system of quarterly quantitative credit guidelines for bank credit to the private sector has been reinstated. Effective July 1, 1983 the interest rates on deposits were increased by an average of 2 percentage points, while the ceiling on the lending rates of the commercial banks was eliminated. The scope for further adjustments in interest rates will be examined at the time of the review of the programme. As of September 1, 1983, the effective liquidity ratios of the commercial banks have been increased by 5 percentage points. Meanwhile, with a view to mopping up excess liquidity in the economy and for purposes of monitoring arrears outstanding, the domestic counterpart of arrears of the oil refinery will have been blocked at the Bank of Sierra Leone by January 10, 1984.

3. External policies

a. The programme aims to reduce the current account deficit of the balance of payments from SDR 128.5 million for 1982/83 (10.3 percent of GDP) to SDR 75.6 million (8.0 percent of GDP) in 1983/84. The programmed 2 percentage points decline in the ratio of the current account deficit to GDP understates the adjustment because of the upward statistical impact of the depreciation on the leone value of the current account deficit. External payments arrears (as defined in the technical memorandum) will be reduced during FY 1983/84 by SDR 1 million on a cash basis from their November 18, 1983 level of SDR 259 million; 1/ of the cash reduction, SDR 0.5 million will be achieved by end-March 1984. External arrears will also be reduced by debt rescheduling and by permitting withdrawals from the commercial pipeline. The Government intends that there will be

1/ This figure excludes an amount of SDR 86 million in unprocessed applications at the Bank of Sierra Leone, against which counterpart funds have not so far been deposited. To the extent that funds are blocked in respect of approved applications in future, the ceilings on total domestic credit will be increased.

no further increase in external payments arrears by the end of the programme period. In the liquidation of external arrears a priority scheme has been established for essential imports, such as raw materials; the rest will be liquidated on a first-in first-out basis. The Government intends to request through the Paris Club a rescheduling of its debt, in the expectation that the request will be dealt with prior to March 1, 1984. Rescheduling of non-Paris Club debts owing to various suppliers, to the commercial banks, and to the oil companies are under way and will be completed in the near future. Debt service on account of external public debt already contracted and disbursed will remain high over the medium term; consequently, external policy has to be most cautious in order to enhance the prospects for medium-term viability in Sierra Leone's balance of payments outlook. Accordingly, during the stand-by period the Government will neither contract, guarantee, nor approve nonconcessional loans for itself or for public enterprises with initial maturities of from one to twelve years, except possible loans for the Kimberlite and Bumbuna projects up to a total amount of $10 million; for new nontrade credits with initial maturity of less than one year the limit will be $15 million and will be confined essentially to bridging loans.

b. As of July 1, 1983, the Government unified the exchange rate for the leone at the rate of Le 2.50 = US$1; this unification entailed a depreciation of the leone by 50 percent in foreign currency terms (about 100 percent in leone terms). The Government intends to use exchange rate policy more flexibly in the future than in the past, and exchange rate policy will be reviewed and understandings will be reached during the scheduled review of the programme. In the meantime, however, the Government will maintain a unified exchange rate.

c. Substantial foreign exchange leakages exist, partly because of the existence of generous retention privileges, the bulk of which are now, in any event, outmoded. In order to increase the mobilization of the country's foreign exchange resources, the Government intends to minimize the use of retention quotas. To this end, Government will complete a review of existing contractual retention arrangements within the programme period. Similarly, given the high and rising proportion of the country's foreign exchange which is lost because of the lack of strict enforcement of surrender requirements, the attached memorandum (Attachment IV) outlines measures to be taken to strengthen the existing surrender requirements for foreign exchange. The practice of extending commercial bank loans on the basis of guarantees provided by foreign financial institutions has been discontinued, except in cases of direct investment projects, as approved by the Bank of Sierra Leone. Furthermore, the system of unnumbered import licenses, which had been a convenient vehicle for the utilization of the country's foreign exchange which had not been surrendered, or which had been otherwise retained abroad, has been discontinued, and will not be reintroduced during the period of the stand-by arrangement.

d. During the stand-by period the Government will not introduce new multiple currency practices or impose new or intensify existing restrictions on payments and transfers for current international transactions, conclude bilateral payments agreements with Fund members, or introduce new restrictions on imports for balance of payments reasons.

December 1, 1983

Memorandum of Understanding on Fiscal Policies Between the Government of Sierra Leone and the International Monetary Fund

The purpose of this memorandum is to articulate in greater detail certain aspects of the fiscal policies for 1983/84 contained in the Memorandum on the Economic and Financial Programme of Sierra Leone, which supports Sierra Leone's request for a stand-by arrangement. This memorandum also establishes a reporting schedule for monitoring government expenditures in the remainder of FY 1983/84.

1. Prior to consideration by the Fund's Executive Board of Sierra Leone's request for a stand-by arrangement, the Sierra Leonean authorities will notify the staff that the relevant executive orders for the implementation of the following measures have been issued.

a. In recognition of the need for increased mobilization of resources from the Sierra Leone Produce Marketing Board (SLPMB) as part of the effort to improve the budgetary position, under the new system whereby duties on the exports of the SLPMB have been replaced by the levy of income tax on the Board's profits (which were previously exempt), the Marketing Board has explicitly undertaken that its tax payments during 1983/84 will amount to at least Le 24 million. Furthermore, payments will be made in roughly equal installments; the first payment of Le 6 million was made on November 14, 1983. Subsequent payments, each of no less than Le 6 million, will be made before the end of the last month of each quarter, i.e., before end-December, end-March, and end-June.

b. In view of the need to intensify restraint on government expenditures, the authorities have identified possible savings in the following areas:

- wages and salaries	Le 6.0 million
- interest charges	Le 8.3 million
- other current expenditure	Le 21.1 million

In the case of each item of expenditure identified in this paragraph, authorizations to spend will be granted by the Ministry of Finance only up to the specified reduced amounts; the remaining allocations provided in the budget will not be used, unless there are compensating gains in revenue collection such as to leave the overall deficit unchanged at the programmed level of Le 200 million. Regarding wages and salaries, circulars will be issued to the effect that vacant posts will not be filled during the balance of 1983/84 other than in exceptional circumstances.

c. Total development expenditures during 1983/84 will be held to Le 140 million, compared to the originally budgeted Le 170 million; the local component, budgeted at Le 47 million, will be limited to Le 32 million. Authorizations to spend will be granted only up to the reduced amounts, unless there are compensating gains in revenue collection and/or development receipts as to leave the overall deficit unchanged at Le 200 million.

d. A system of allotments for current expenditures will be used to facilitate the monitoring of expenditure under the programme, and similar arrangements have been established for the local component of development expenditure. The allotment system is designed to ensure that expenditure authorizations during 1983/84 are consistent with the overall targets of the programme. It is intended that actual allocations to the vote controllers will be updated at the beginning of the third and fourth quarters of 1983/84 such that the aggregates of allocations for (a) wages, salaries, and pensions; (b) other charges; and (c) domestic component of development expenditure at the end of any quarter do not exceed the corresponding cumulative total of the quarterly allocations specified in the attached table. The allotments will be regularly monitored by the Ministry of Finance and the Bank of Sierra Leone to ensure that no excess expenditures are incurred.

e. The smooth functioning of the quarterly allotments system will be facilitated by the operation of the expenditure control procedures at the Ministry of Finance. Under these procedures, all expenditures authorized by local purchase orders are subject to pre-audit in the Expenditure Control Unit, so that prior Ministry of Finance approval is required before Departments make commitments. In addition, all payment vouchers for purchases in Freetown in excess of Le 50 are checked at the Ministry's payments office before cheques are issued.

f. To improve the efficiency of procedures for purchase of stores and ensure that supplies are obtained from the least costly sources, the Government intends to initiate a review of the arrangements whereby orders are placed, stores are supplied to Departments, and payments made by the Government. Results of the review and the proposed measures for improving the procedures will be discussed with the staff of the International Monetary Fund no later than end-March 1984. All purchases will remain subject to the pre-audit procedures described in paragraph (e).

g. In the past, virement has been used to provide resources for outlays where original vote provisions were insufficient. If savings, in addition to those specified in preceding paragraphs of this memorandum, do not become available for such virement, necessary adjustments will be made in other votes, in order to ensure that overall expenditures do not exceed the programmed level. In any event, to minimize unnecessary expenditures, all requests for virement will be closely scrutinized by the Ministry of Finance before possible approval is granted.

2. To improve the monitoring of budgetary performance and to prevent the accumulation of arrears on the domestic counterpart of external payments, a special blocked account for the domestic counterpart of scheduled official external payments will be established at the Bank of Sierra Leone by end-December 1983. This account is designed to ensure that adequate provision is made from domestic budgetary resources for the domestic counterpart of such obligations, regardless of the availability of foreign exchange to complete the externalization of these payments. Beginning from the date of establishment of the account, all principal and interest payments on official external debt service chargeable to the budget will be debited to the blocked account at the time of their externalization.

The account will be opened by a transfer from the Government's regular accounts of an amount equal to Le 29.0 million less the leone equivalent of actual debt service (principal and interest) paid and already debited to the Government's regular accounts during the period between July 1, 1983 and the date of establishment of the blocked account. Subsequent resources for the account will be provided by two quarterly transfers from the Government's regular accounts, each of Le 19.35 million due by end-January and end-April 1984. These amounts are computed such that the total domestic resources provided for external debt service during 1983/84 are consistent with the assumptions of the programme after taking into account projected reschedulings of Sierra Leone's external obligations, namely Le 26.1 million for interest payments and Le 41.6 million for amortization of medium- and long-term debt. By end-March 1984, the actual 1983/84 debt service due by end-March and end-June after completion of debt rescheduling negotiations will be calculated. Any shortfall between the resources available in the blocked account and the actual amounts due by end-March will be made good before end-March; likewise, any similar such shortfall at end-June will be made good by an additional transfer before end-June. The blocked account described in this paragraph will be excluded from the calculation of net claims of the banking system on Government for the purpose of the credit ceilings established under the programme.

3. In order to improve the monitoring of trends in government finances, the Bank of Sierra Leone will collect data on government borrowing (net) from the banking system (including the commercial banks, as well as the Bank of Sierra Leone) on a daily basis, with immediate effect. Such data for each week will be reported to the Ministry of Finance at the beginning of the following week.

4. Data on actual expenditures and revenues will be reported to the Fund on a quarterly basis, as soon as possible after the figures become available, but in any event no later than one month after the end of the quarter. The Sierra Leonean authorities will consult with the Fund if

total expenditures, expenditures on wages and salaries, expenditures on other charges, or domestic development expenditures are deemed likely to significantly exceed the specified allotments (as set out in the attached table), in order to agree on additional fiscal policy measures (revenue or expenditure) required to enable the Government to meet its overall fiscal objectives.

December 1, 1983

Sierra Leone: Quarterly Allotment of Expenditure, 1983/84 1/

(In millions of leones)

	First quarter Actuals	Second quarter	Third quarter	Fourth quarter	Programme total	Budget estimate
Current expenditures	68.1	84.0	90.7	89.7	332.5	367.9
Wages, salaries and pensions	39.7	40.6	40.6	40.7	161.6	167.6
Interest payments	7.6	17.9	24.1	18.3	67.9	76.2
Other charges	20.8	25.5	26.0	30.7	103.0	124.1
Domestic development expenditure	5.0 2/	11.1 3/	7.9	8.0	32.0	47.0

Source: Data provided by the Sierra Leonean authorities.

1/ The classification of expenditures in this table is that adopted by the Budget Advisory Committee of the Ministry of Finance.
2/ The allotment for the first quarter was Le 11.0 million; the unused balance from this allotment is already implicitly included in the allotments for the third and fourth quarters.
3/ Allotment already issued.

TECHNICAL MEMORANDUM OF UNDERSTANDING

1. Total Domestic Credit as specified in the Memorandum on the Economic and Financial Programme is defined to include Net Credit to Government and Credit to the Private Sector.

Net Credit to Government is defined as:

1 Bank of Sierra Leone
Ways and Means Advances
Holding of Government Securities
Other Advances
SDR Allocation held by Treasury
Treasury IMF Accounts
(Use of Fund Credit)
(Less IMF Deposits)

Less Government Deposits
Current Account +
Blocked Account + 1/
IMF Trust Fund +
Bonds
Net Credit to Government

11 Commercial Banks
Holdings of Treasury Bills
Holdings of Government Stocks
Advances to Government

Less Government Deposits
Net Credit to Government

111 Total Net Credit to Government

Credit to the Private Sector is defined as:

A. Bank of Sierra Leone

1. Claims on Private Sector (line 12d)

B. Commercial Banks

1. Claims on official entities (line 22b)
Loans and advances to SLPMB
Loans and advances to other Government Corp.
Loans and advances to the Registrar of Co-ops.
Investment in other securities in Sierra Leone (N.D.B.)

1/ Excluding the blocked account for the leone counterpart of the Government's external debt service payments, and also the existing 1982/83 domestic arrears fund.

2. Claims on Private Sector

Bills discounted or purchased and payable in Sierra Leone
Loans and advances to other customers
(excluding Government, official entities, and the special credit to the refinery).

C. Total Bank Credit to Private Sector

2. Even though ceilings on Total Domestic Credit and Net Credit to Government for end-December 1983 as specified in the Memorandum on the Economic and Financial Programme do not constitute performance criteria, they have been established as indicative targets to assist compliance with the end-March ceilings which are performance criteria.

3. The Sierra Leonean authorities have agreed to issue guidelines to the commercial banks on credit to the private sector. These guidelines will assist in controlling the expansion in private sector credit and are consistent with the ceilings established for Total Domestic Credit for end-December 1983, end-March 1984, and end-June 1984.

4. External payments arrears as specified in the Memorandum on the Economic and Financial Programme are defined to include arrears to International Organizations, arrears due to foreign banks, arrears due to foreign Governments, suppliers' credit/contractor finance which are in arrears, the arrears pipeline of the commercial banks, the Euro-dollar loan arrears, the Bank of Sierra Leone pipeline arrears, the Sierra Leone Petroleum Refining Company's arrears to the oil companies, the Chinese Clearing Account, and any newly approved applications from the outstanding stock of SDR 86 million of previously unprocessed applications.

Memorandum of Understanding on Surrender Requirements

1. There exists a set of laws and regulations regarding the surrender of foreign exchange receipts; henceforth these laws and regulations will be vigorously enforced, existing penalties for non-surrender will be enforced, and new and tighter penalties will be introduced. The maximum period for surrender is reduced to 30 days, except for diamond exports and the exports of SLPMB.

2. Surrender requirements for all exports will be based on individual CD2 forms. A list of the serial numbers of CD2 forms will be compiled and monitored by the Bank of Sierra Leone. In addition to the penalties, the list of outstanding offenders will be published in the Gazette, regularly.

3. Borrowings by Government against future external trade receipts will be undertaken only in exceptional circumstances, and will be channeled through the Bank of Sierra Leone. No promissory notes payable in foreign currency will be issued against future external trade receipts.

4. Henceforth full surrender requirements will apply to the SLPMB. Surrender will be completed within ten days of shipment. Retentions in 1983/84 will be limited to a maximum of $14 million to cover obligations already incurred as of November 10, 1983. Thereafter, any further application for foreign exchange will be handled through normal procedures.

5. Diamond exports will be registered with CD2 forms prior to exportation, but for security reasons the exact date of shipment need not be declared. Full surrender of export proceeds will be completed within 60 days of shipment.

6. Prior to the issuance of the programme paper, the reserve centralization rules will be extended to apply to the Sierra Leone Commercial Bank.

7. The monitoring of the sales of bunker and aviation fuel will commence immediately.

8. Prior to Board discussion of the programme paper, the Bank of Sierra Leone will issue guidelines for the monitoring of invisible receipts such as those from technical assistance personnel, tourists, the Port Authority, and Sierra Leone Airlines.

9. Exporters (particularly in the mining sector) will be subject to full surrender requirements except as specified by statute. Any application for foreign exchange will be handled as a separate matter through normal procedures. Where retention has been specified by statutes these will be reviewed.

10. Progress in the enforcement of surrender requirements, and a quantitative assessment of the impact of these measures on foreign exchange inflows will form an integral part of the programme review.

December 1, 1983.