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INFORMATION

December 14, 1984

To: Members of the Executive Board
From: The Secretary
Subject: Sudan - Staff Report for the 1984 Article IV Consultation

The attached supplement to the staff report for the 1984 Article IV consultation with Sudan has been prepared on the basis of additional information.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion on Wednesday, December 19, 1984, they should contact Mr. Clawson (ext. 7142).

Att: (1)

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INTERNATIONAL MONETARY FUND

SUDAN

Staff Report for the 1984 Article IV Consultation
Additional Information

Prepared by the Middle Eastern Department,
and the Exchange and Trade Relations Department

Approved by Paul Chabrier and S. Kanesa-Thanan

December 14, 1984

The staff would like to provide to the Executive Board additional information that has become available on agricultural prospects and monetary and fiscal developments since the preparation of the Staff Report on the 1984 Article IV consultation with Sudan (SM/84/253, November 9, 1984) and on a number of changes that have been made in Sudan's exchange system. The Sudanese authorities have also requested assistance in the formulation of appropriate economic policies aimed at improving the balance of payments position and thereby discharging Sudan's outstanding obligations to the Fund. In this connection a staff team arrived in Khartoum November 24, 1984 and is expected to return December 16, 1984. The staff is expected to make an additional oral presentation at the time of the Board meeting on Sudan.

1. Prospects for agriculture

The impact of drought conditions on the 1984/85 harvest is likely to be more severe than anticipated. Crop production prospects have deteriorated for nearly all principal crops and real value-added in agriculture (including livestock) is projected to decline by 12 percent in 1984/85 compared with an initial projection of a 7 percent decline. Constraints on the availability of water in the irrigated schemes have led the authorities to ban the cultivation of wheat with the result that an additional 150,000 tons of imported wheat will be required in 1985. Cotton output is now projected to be about 100,000 bales less than the previous year crop level of 1,167,000 bales. However, the quality is reported to be much higher and the outlook for international prices of cotton has improved, particularly for the long staple, as reflected in the higher opening prices for the new Egyptian cotton crop.

2. Money and banking developments

Monetary growth during the period July to September 1984 continued at about the same annual rate as during the 1983/84 fiscal year. The continued moderation in monetary growth resulted in part from policy action in limiting the credit available to public entities to their seasonal requirements, but also reflected continued economic uncertainty,

engendered by recent institutional changes, which effectively limited new demand for bank borrowing. As a consequence, private sector credit remained virtually unchanged over the three month period. The impetus for growth in money supply resulted in the main from the weak government budgetary position which gave rise to an increase in net credit to Government between July and September of LSd 200 million (6.3 percent of money supply at end-June 1984).

The movement toward the elimination of interest-bearing features of banking transactions has been further advanced by a recent judicial decision emphasizing the illegality of payment or receipt of interest. Accordingly, the non-Islamic commercial banks were instructed on November 21, 1984 not to charge their customers interest and have complied with this, mainly by substituting commissions and charges.

3. Budgetary developments

Preliminary data on the outturn of the budget covering the three month transitional period between the end of the old and the beginning of the new fiscal year, i.e., the period July 1 to September 25, show the fiscal position deteriorated more rapidly than had been anticipated at the time of the Article IV consultation. Total revenue collections of LSd 344 million were marginally higher than the previous staff projection, largely reflecting a successful effort at the collection of tax arrears. Expenditures, however, at LSd 662 million were 8 percent higher than projected giving rise to a deficit of LSd 318 million (about 11 percent of GDP on an annualized basis). The entire increase in expenditure emanated from unidentified extrabudgetary operations. The deficit was covered by LSd 118 million of foreign financing, which was higher than expected partly because of underrepayment of foreign obligations, and by LSd 200 million in domestic bank financing. Bank financing which had amounted to 1 percent of GDP in 1983/84 rose during the period of the transitional budget to 7 percent of GDP on an annualized basis.

Since the beginning of the new fiscal year the Government has taken certain actions to compensate for the revenue losses corresponding to those taxes which were abolished upon the introduction of Zakat. Some of these measures have been reported in the Staff Report. The most recent of these actions were the introduction on November 25, 1984 of a social justice tax and a consumption tax. The social justice tax is a progressive direct tax on individual incomes and profits to partnerships and corporations, and as such is equivalent to the previously levied personal income and business profits taxes. The threshold levels for payment of the tax are substantially higher and rates are at a lower level than under the previous personal and corporate income taxes. With the introduction of this tax, the Zakat on corporations and partnerships was abolished while the Zakat for individuals was allowed to be offset against the amounts due under the social justice tax. The consumption tax will be levied on a variety of domestically manufactured or processed goods intended for consumption (at the intermediate or retail level) in Sudan. The tax is mainly on an ad valorem basis with rates ranging from

5 percent (for the majority of commodities) to a maximum of 55 percent, though for certain commodities including wheat flour, beverages, and tobacco, a specific tax will be levied. The tax is equivalent to the previously levied excise duties and development tax. As a result of the recent tax changes, the prospects for tax revenue during fiscal year 1984/85 are assessed as showing no deterioration compared with original budget estimates. However, collections from the social justice tax on partnerships and corporations which will begin in 1985/86 are not expected to compensate for the abolition of the income tax on business profits.

4. Changes in exchange system

A number of adjustments have recently been made in the exchange system described in the Staff Report. On October 21, 1984, the commercial bank exchange rate was depreciated from LSd 1.80 to LSd 2.10 per U.S. dollar. At the same time, all exports, with the exceptions of cotton and gum arabic, were valued at the commercial bank foreign exchange rate rather than at the previous rate which was a composite of 75 percent of the official market rate and 25 percent of the commercial bank rate. The effective depreciation for these exports was thus 48 percent (from LSd 1.42 to LSd 2.10 per U.S. dollar). The 75:25 composite rate (now LSd 1.50 per U.S. dollar) continues to be applied to exports of cotton and gum arabic. In addition to these changes, export receipt surrender requirements were partly liberalized. Under the new system, 50 percent of foreign exchange receipts from exports must be surrendered to the Central Bank compared with 75 percent under the previous system. The liberalization did not apply, however, to cotton or gum arabic (75 percent surrender) or sesame (where a 100 percent surrender requirement now applies). On the import side there has also been some progress in moving transactions from the official to the free market. Thus, all imports of goods under commodity aid agreements, including wheat and wheat flour, have, since the beginning of the fiscal year, been valued at the commercial bank rate rather than at the official rate or at composite rates as has previously been the case. In addition, all future commercial purchases of both wheat and sugar are to be financed through the free market. Aside from these changes, all invisible payments and receipts previously transacted through the official market have been transferred to the commercial bank market. The commercial bank rate is now applied to most inflows for investment purposes and receipts from tourism as well as all government payments for invisibles excepting debt service.

The differential between the rates quoted in the free market by the commercial banks and the licensed exchange dealers has widened considerably in recent months due to a steep depreciation of the free market rate. While the commercial rate has been depreciated from LSd 1.80 to LSd 2.10 per U.S. dollar, the dealer's rate has moved from LSd 2.40 per U.S. dollar at the end of September 1984 to about LSd 3.00 per U.S. dollar in early December 1984.