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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 84/3

10:00 a.m., January 9, 1984

W. B. Dale, Acting Chairman

Executive Directors	Alternate Executive Directors
	J. K. Orleans-Lindsay, Temporary
	G. Ercel, Temporary
	X. Blandin
	R. J. J. Costa, Temporary
	J. C. Williams, Temporary
	M. Z. M. Qureshi, Temporary
T. Hirao	T. Yamashita
	Jaafar A.
R. K. Joyce	
A. Kafka	
	W. Moerke, Temporary
	C. P. Caranicas
	A. S. Jayawardena
	J. E. Suraisry
J. J. Polak	T. de Vries
A. R. G. Prowse	K. G. Morrell
	H. Alaoui-Abdallaoui, Temporary
F. Sangare	E. I. M. Mtei
M. A. Senior	
	A. K. Juusela, Temporary
N. Wicks	T. A. Clark
Zhang Z.	

A. Wright, Acting Secretary
L. Collier, Assistant

Also Present
African Department: O. B. Makalou, Deputy Director; R. J. Bhatia, Deputy Director; N. Abu-zobaa, E. L. Bornemann, E. A. Calamitsis, R. O. Carstens, M. E. Edo, U. R. Gunjal, S. M. Nsouli, R. L. Sharer, E. S. Williams, A. C. Woodward. Asian Department: H. C. Kim. Exchange and Trade Relations Department: D. K. Palmer, Associate Director; T. Hatayama, S. Kanesa-Thasan, N. E. Weerasinghe. External Relations Department: Z. Zhang. Fiscal Affairs Department: R. R. Schneider, R. J. Hurnard. Legal Department: W. E. Holder. Research Department: W. C. Hood, Economic Counsellor and Director; N. M. Kaibni, K.-Y. Chu, E. C. Meldau-Womack, D. Sapsford. Advisors to Executive Directors: E. A. Ajayi, S. E. Conrado, S. M. Hassan, H.-S. Lee, D. I. S. Shaw. Assistants to Executive Directors: E. M. Ainley, J. R. N. Almeida, J. Bulloch, M. Camara, M. B. Chatah, M. Eran, I. Fridriksson, G. Gomel, V. Govindarajan, D. Hammann, C. M. Hull, J. M. Jones, H. Kobayashi, M. J. Kooymans, Y. Okubo, G. W. K. Pickering, M. Rasyid, A. A. Scholten, Shao Z., S. Sornyanyontr.

1. RATE OF REMUNERATION, POLICY ON ENLARGED ACCESS, AND ACCESS LIMITS UNDER SPECIAL FACILITIES - PRESS RELEASE

Mr. Kafka commented that in the recent press release (No. 84/1) on the decisions regarding enlarged access and the rate of remuneration, the penultimate paragraph seemed unfortunately formulated. The press release language--"although access limits have been lowered in percentage terms"--was incorrect; in fact, the normal maximum access limits had been lowered. The release had given the impression that the Board's action was more severe than it actually had been. It was too late to retract the press release, but he would appreciate it if the staff would be more careful in future formulations.

The Executive Board took note of Mr. Kafka's comment.

2. ZAMBIA - REVIEW UNDER STAND-BY ARRANGEMENT

The Executive Directors considered the staff paper on the review of the exchange rate policy under the stand-by arrangement for Zambia (EBS/83/274, 12/23/83).

The staff representative from the African Department informed Executive Directors that Zambia had continued the gradual downward movement of its exchange rate described in EBS/83/274. From the end of November 1983 to date, there had been a further depreciation of 8.5 percent--including the 3 percent change mentioned in the staff paper--and the staff had been assured that Zambia would continue its flexible exchange rate policy.

A staff mission was scheduled to visit Zambia in the first half of February to conduct the 1984 Article IV consultation discussions and to initiate discussions on a financial program covering 1984, the staff representative stated. During those discussions, Zambia's exchange rate policy would be reviewed by the staff.

Mr. Sangare made the following statement:

> Executive Directors may recall that on September 16, 1983 at the time of the midterm review of the current stand-by arrangement for Zambia, the Board decided that purchases after November 30, 1983 would be subject to a review of Zambia's exchange rate policy, in addition to the observance of the end-October performance criteria.
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> The staff report shows that my Zambian authorities have implemented all the measures agreed with the Fund at the time of the midterm review, including a flexible exchange rate policy, and have met all performance criteria as of the end of October. However, the external position of Zambia remains difficult. As a result of a decline in world market prices for copper, the country's leading export commodity, export receipts are projected

to be 7 percent below earlier estimates in 1983. Although the current account deficit is expected to improve compared with 1982, recent estimates show that the deficit is likely to be about SDR 56 million higher than envisaged under the program. Under the circumstances, the overall balance of payments deficit is estimated at SDR 83 million, as against the original projection of SDR 60 million, after adjustments have been made for the refinancing of arrears to commercial banks and the nearly concluded debt rescheduling agreement.

Pressure on Zambia's external payments position has been intensified by the delays in scheduled purchases from the Fund, resulting in an estimated financing gap of SDR 53 million in 1983. The authorities therefore had to resort to short-term loans, which, Directors will no doubt appreciate, are too costly and exacerbate the external debt situation. My authorities were compelled to undertake these short-term borrowings in order to cover the financing gap and comply with the performance criteria, particularly on external payments arrears. They are aware, however, that short-term market borrowing is expensive and can be seen only as a temporary palliative. Accordingly, a number of concrete steps have been taken aimed at a more lasting solution to the balance of payments problems, including successful implementation of cost-reducing measures in the mining sector, and the authorities are committed to introducing additional measures to improve its efficiency further. On the other hand, the authorities continued to implement a flexible exchange rate policy aimed at improving the profitability of the mining sector. In line with this commitment, the kwacha has been depreciated by about 35 percent during 1983. However, the continued depressed market demand for copper has offset the improvement in competitiveness of the export sector, particularly the mining industry, that resulted from the exchange rate action. The authorities had to effect a further downward adjustment in the value of the kwacha just last week, as confirmed by the staff. Because the long-awaited upturn in the copper market has been slow in coming, and given the volatility of copper prices, my authorities have reservations about the practicality of having to link exchange rate adjustment to changes in the price of copper. Directors may note that it is the intention of my Zambian authorities to continue the flexible exchange rate policy in place, and the staff has expressed satisfaction with the exchange rate and complementary measures taken.

In conclusion, I wish to express my authorities' appreciation of the positive manner in which the Fund staff has conducted the review discussions, and I urge the Board to approve the proposed decision.

Mr. Orleans-Lindsay said that he welcomed the minireview to determine the appropriateness of the exchange rate policy in the context of the adjustment program supported by Zambia's one-year stand-by arrangement. He endorsed the staff's assessment that the authorities were implementing the policy in a flexible manner, as envisaged under the program; he therefore supported the adoption of the proposed draft decision.

It was encouraging that since the midterm review, the Zambian authorities had succeeded in implementing all the measures outlined under that review and had met all the performance criteria for end-October 1983, Mr. Orleans-Lindsay remarked. He commended the authorities for their efforts to keep the program on track. The courageous and important action taken by the authorities in January 1983, when they had devalued the kwacha by 20 percent, had been followed by a series of discrete adjustments which had resulted in a cumulative depreciation of the kwacha by 31.8 percent against the SDR in November 1983. Added evidence of the authorities' commitment to managing the rate in a flexible manner had been provided by the further depreciation of the kwacha effected in December 1983, thus bringing the cumulative depreciation of the currency since January 1983 to 34.8 percent vis-à-vis the SDR. The information provided by the staff indicated that a further depreciation of the currency by about 10 percent in terms of the U.S. dollar had taken place. The depreciation seemed to be of the right magnitude, as it had contributed to reducing the value of imports to SDR 776 million, compared with SDR 786 million forecast at the time of the midterm review. Similarly, payments for services and transfers had been kept at the level projected earlier.

The beneficial effects of the flexible exchange rate policy on the financial position of the mining company could not be verified, Mr. Orleans-Lindsay noted, because statistical information was not available for assessing the extent of the financial resources channeled into rehabilitation and investment in capital equipment for expanding copper production and exports. At the midterm review, his chair had noted that the success of Zambia's adjustment efforts up to that time--and of further measures to improve the domestic and foreign exchange prospects for 1983 and the medium term--depended crucially on developments in the international copper market. Furthermore, the pursuit of diversification away from the economy's high dependence on the mining sector and the priority given to the development of the agricultural and manufacturing sectors gave the authorities little room for maneuver.

The medium-term outlook for Zambia's balance of payments remained gloomy, Mr. Orleans-Lindsay commented, as copper prices on the world market were forecast to remain at about 65 cents a pound in 1984 and beyond, resulting in a 7 percent decline in export receipts compared with estimates in 1983. The current account deficit of the balance of payments had thus worsened to SDR 263 million in 1983, compared with SDR 207 million estimated at the time of the midterm review. The overall balance of payments deficit was forecast at SDR 83 million for 1983, instead of SDR 60 million envisaged earlier, after allowing for settlement of commercial arrears and the debt rescheduling arrangement. It was therefore a matter of grave concern that the current pressures on Zambia's balance of payments could be attributed partly to delays in making scheduled purchases from the Fund, which had led the Zambian authorities to resort to short-term bridging loans to finance the gap of SDR 53 million that had emerged.

The staff had expressed satisfaction with the implementation of the flexible exchange rate policy by the Zambian authorities, Mr. Orleans-Lindsay noted. The authorities' commitment to continuing that policy as part of the overall package of adjustment measures to reduce internal and external financial imbalances and to establishing conditions that would permit a sustained recovery in Zambia's economic activity was praiseworthy.

Mr. Clark said that he supported the proposed decision and welcomed the completion of the review of Zambia's exchange rate policy. The authorities were to be commended for the resoluteness that they had shown in implementing the further exchange rate adjustment announced by the staff. Their determination to carry out, in difficult circumstances, all the measures included in the September midterm review of the program was laudable. He did, however, encourage the authorities to persevere with their efforts so that the full benefit of the measures could be realized.

For various reasons, it had not been possible for Zambia to make the purchase scheduled for the October-December quarter on time, and that delay had caused some difficulties, Mr. Clark noted. He hoped that it would be possible for the review of budgetary policies for 1984 under the stand-by arrangement to proceed in a timely fashion; he invited the staff's comments on that point.

One objective of the exchange rate policy had been the maintenance of a competitive position for the copper mining industry, Mr. Clark recalled. Copper accounted for about 90 percent of exports, but he wondered whether the staff could give some indication of how the exchange rate for the kwacha was affecting other sectors of the Zambian economy.

Mr. Moerke remarked that Zambia's performance under the program had been encouraging. The authorities had implemented the measures included in the midterm review, and all the performance criteria for end-October had been observed. A deterioration in the financial position of the mining company had been successfully countered by cost-cutting measures. The recent depreciations of the kwacha reflected the authorities' commitment to pursuing an exchange rate policy flexible enough to ensure that the program targets remained on track. However, as long as the current level of the world market price for copper prevailed, the authorities would be faced with substantial losses by the mining company. Under those circumstances, additional cost-cutting measures, as well as the continuation of a flexible exchange rate policy, would be crucial. He would appreciate staff comment on the outlook for copper prices. Finally, he could support the proposed decision.

Mr. de Vries said that he continued to support the Zambian program. He wished to comment, however, that the paucity of material in the staff paper describing the exchange rate policy made the Board's task of reviewing the appropriateness of the policy difficult. Although the exchange rate had been depreciated and exchange rate policy seemed fairly flexible, it was impossible to reach a judgment.

He noted with satisfaction that the performance criteria had been met under difficult circumstances, Mr. de Vries remarked, although it was unfortunate that, because rescheduling and therefore cash payments had not taken place as foreseen, the authorities had engaged in short-term borrowing. He recalled that when Zambia's program had been discussed, a number of Directors had stated that structural changes were of the essence; a central point was the increased profitability and efficiency of the copper mining plant. He hoped that the measures necessary to achieve that goal would be introduced.

Referring to Table 3 on page 5 of EBS/83/274, Mr. de Vries inquired why the last two columns, one for estimates at the time of the midterm review and the other for revised estimates, were identical in the section on services and unrequited transfers.

Mr. Blandin stated that he had no difficulty in approving the proposed decision regarding the review of the exchange rate policy under Zambia's existing stand-by arrangement, allowing the country to make long-awaited drawings. The delay in transacting the purchase linked to the October performance criteria had been caused by the Fund's request that the authorities should change their exchange rate policy. Although that change had been implemented before the end of December 1983, the normal lapse of time necessary for document preparation and Board discussion had delayed the authorization for Zambia to draw until after December 30. Consequently, the country had had to resort to costly bridging loans in order to meet the end-December performance criteria. He wondered whether in such a case it would not have been preferable to grant a waiver rather than force an already heavily indebted country to engage in new borrowings for only a few days.

The requested change in Zambia's exchange rate policy raised an interesting theoretical question, Mr. Blandin said. On what basis must a deterioration in the terms of trade of a country be followed by a corresponding devaluation of the exchange rate? Such a devaluation resulted in a reduction in relative real wages in the devaluing country compared with other countries, despite an unchanged level of labor productivity. If all countries producing the commodities responsible for the deterioration in the terms of trade had the same reaction, the result would, in fact, nullify the deterioration in the terms of trade by making it more tolerable for the countries hit by falling prices. However, another result would be a reduction in real wages in all those countries, not only in the sectors producing the export commodity with falling prices, but also in all other sectors of the economy, at least in terms of imported goods, without any corresponding downward change in labor productivity. Subsequently, a contraction of global demand with potential deflationary consequences would occur. He therefore wondered whether the remedy proposed by the staff to palliate the deterioration in the terms of trade was valid only in the framework of partial equilibrium analysis while theoretically ill founded in the framework of general equilibrium theory.

Mr. Williams stated that he supported the proposed decision. It was imperative for the success of the Zambian program and, more important, for the longer-term structural adjustment effort needed by the economy, that the Zambian authorities should continue to pursue a flexible exchange rate policy. He was pleased to note that the Fund and the authorities were in agreement on that vital area, although it was unfortunate that the review had been slightly delayed. He strongly urged the authorities to reach agreement quickly with the Fund on the policies to be discussed during the next review in February, so that the momentum toward adjustment that had been established would be maintained.

Mr. Prowse said that he supported the decision on the appropriateness of the exchange rate policy. In principle and theory, the policy was appropriate; however, he agreed with Mr. de Vries that the staff paper was not as comprehensive on the specific issue as he would have wished. The previous staff paper (EBS/83/176, 8/18/83) had provided a theoretical description of the policy, but he would have preferred more explicit information in the present paper on how the real effective rate had moved. Table 1 and portions of the text describing the depreciation referred to nominal rates only, but it would be important to describe the real effective rate. A diagram showing the movement of the real rate and nominal rates would have been a helpful addition to the paper.

The present paper's brevity was welcome, Mr. Prowse continued, but it and the previous paper, while listing a number of objectives for the exchange rate, did not indicate what the relative weights were, and some objectives were not necessarily complementary. It was evident that the most important objective was to assist the copper mining activities. Could the staff measure the extent of the benefit for ZCCM, the mining company? He would also appreciate staff comment on the danger that a soft approach to wages might be associated with a willingness to depreciate the exchange rate, which would not be the best overall policy.

Mr. Zhang remarked that, although the discussion focused on the flexibility of Zambia's exchange rate policy, it was difficult to know how to react to the staff's statement that Zambia had recently announced a further devaluation of 10 percent. What was the total amount of devaluation advocated by the staff under the current stand-by arrangement? Had the recent devaluation been approved by the staff?

Because the price of Zambia's main export, copper, was quoted in U.S. dollars on the world market, the devaluation would not greatly stimulate Zambia's exports, Mr. Zhang observed. As indicated by the staff, the purpose of the devaluation was to increase the profits of the mining company, which had been falling because of the decline in the price of copper. Hence, would the Zambian Government attempt to appreciate the kwacha when the world market price of copper rose to the prerecession level, or would the authorities attempt to tax away the profits from the company? Would the increase in profits lead to increased investment in the copper industry, or would those profits be expatriated? What would be the impact of the devaluation on domestic prices? He would appreciate comment on those technical points;

meanwhile, on the basis of Mr. Sangare's statement, he believed that the current exchange policy was appropriate, and he supported the proposed decision.

Mr. Juusela said that his chair supported the proposed decision. At the time they had reviewed the performance of the Zambian economy under the present stand-by arrangement, Executive Directors had found developments to be satisfactory; all performance criteria had been observed. The staff paper, supported by the staff statement announcing further adjustments in the exchange rate for the kwacha, illustrated the Zambian authorities' continued efforts to follow appropriate adjustment policies. The performance criteria for further drawings appeared to have been met, although it was somewhat difficult to judge some technical aspects of the exchange rate for the kwacha. For example, it might prove unnecessary and unfruitful to calculate various traditional effective rates and similar indicators of exchange rate development. Similarly, he would have to rely on the staff's expertise that relating the kwacha to the SDR was as good an indicator as any other alternative.

He hoped that the Zambian authorities would continue to pursue a determined adjustment policy in the longer term, Mr. Juusela commented. Such a strategy would help the Board to support possible further financial cooperation between Zambia and the Fund should the need for a future financial arrangement arise.

Mr. Suraisry said that he supported the proposed decision. The Zambian authorities were continuing to take strong measures to reduce the serious imbalances in their economy. Performance under the stand-by arrangement had been good, and all the quantitative criteria had been met at end-October. It was also encouraging that budgetary expenditure was being cut back as projected and that government borrowing from the domestic banking system was likely to remain within the agreed ceiling.

It was, however, clear that Zambia continued to face severe external problems, Mr. Suraisry continued. The recent fall in copper prices had had an adverse effect on export receipts and on the financial position of ZCCM, the state mining company. In those circumstances, an improvement in the external position would depend in large part on continued adjustment as well as on debt relief from donor countries.

The steady depreciation of the kwacha was an important element in the authorities' strategy, and he welcomed their continued commitment to a flexible exchange rate policy, Mr. Suraisry stated. In short, Zambia's recent performance justified the purchase of SDR 67.5 million, which would be very helpful at the present time.

Mr. Jayawardena complimented the Zambian authorities for resolutely persevering with a flexible exchange rate policy under most difficult circumstances. He supported the proposed decision. The exchange rate was undoubtedly a crucial factor in the adjustment process of Zambia, a country overwhelmingly dependent on a single export commodity--copper--whose future role in trade appeared to be declining not only because of the recession but also because of certain technological developments, such as optical fibers. It was therefore unclear how exchange rate policy would help the copper industry, although a flexible policy could help to diversify the economy by encouraging the food and agricultural sectors. He joined other Directors in asking the staff whether the policy had helped other sectors of the economy.

Zambia's most recent purchase had been postponed as a result of the delay in the present review, necessitating resort to short-term bridge financing, Mr. Jayawardena noted, and he wondered whether it was necessary for the Board to take up individual aspects of policy in special minireviews. He suggested that it might be preferable, with all the facts at the Board's disposal, to discuss all aspects in a formal Article IV discussion or midterm review.

The staff representative from the African Department recalled that in the original program approved in April 1983, the present review had not been envisaged. For various reasons, the program had gone off track in the middle of the year, and after a series of discussions, staff visits, and visits by the Zambian authorities, the midterm review had been concluded in September. In that midterm review, two additional reviews had been inserted that had not been part of the original program: the present one governing the purchase linked to the end-October performance criteria, and another review linked to the end-December performance criteria relating to budgetary policy for 1984. The objective of the present review was essentially to ensure that Zambia's exchange rate policy was operating flexibly. Therefore, the purpose of the staff paper was not to provide a full analysis of exchange rate policy, which would be given in the context of the Article IV consultation scheduled for the first half of February 1984. The staff had believed that it would not be useful to have a full review at present, followed shortly by another review of exchange rate policy during an Article IV discussion, together with discussions regarding a possible new program covering calendar year 1984. In September 1983, the staff had expected that the present review could be concluded by the end of December and that disbursement of the purchase would be made at that time. However, for various reasons, including some delays by the Zambian authorities in taking additional exchange rate action, that schedule had not been possible.

As stated in earlier papers, the staff considered that the main aim of exchange rate policy in Zambia was to assist, as a supply-side instrument, in the long-term diversification of the economy away from copper toward other sectors, mainly agriculture, the staff representative continued. To date, however, there had been little evidence of success because structural diversification obviously would take time. In addition, Zambia and the rest of southern Africa had suffered two poor harvests in a row, owing to severe droughts. Apparently the current year's crop would be much better, and he hoped that during the course of the consultation discussions some evidence of the more flexible exchange rate policy's effect on structural diversification would become available.

A subsidiary short-term purpose of the flexible exchange rate policy was to improve the viability of ZCCM, the mining company, the staff representative said. During the midterm review, the staff had made estimates of the viability of the mining company based on an average price of copper of 76 cents a pound, which had prevailed until the fall of 1983, when it had begun to decline. The copper price had fallen to the low 60s in November and at present was close to 65 cents. Therefore, the average for 1983 would be about 5 cents lower than estimated, and the mining company's financial situation would remain difficult despite various cost-cutting measures. It was worth noting, however, that if the Zambian authorities had not maintained a flexible exchange rate policy, the mining company would be facing large financial deficits; as a result of the exchange rate policy, the accounts of the mining company were approximately in balance.

During the November mission to Zambia, the staff representative continued, the staff had forecast that, based on the current copper price of 65 cents, there would be a substantial financial deficit that would presumably have to be financed by bank credit and would lead to the surpassing of agreed credit ceilings. At that time, it had been agreed that a 10 percent devaluation below the level reached on November 30, together with additional cost-cutting measures, would enable the mining company to maintain its financial accounts in balance for the next two quarters. The question of exchange rate policy would be taken up again at the time of the Article IV consultation in the light of a possible program for 1984 and of future copper price developments.

Periodic papers on indicators of real effective exchange rates presented to the Board showed that Zambia's real effective exchange rate had remained approximately unchanged from 1978, the staff representative remarked. Taking into consideration the recent devaluation, the real effective exchange rate had fallen. However, Zambia's problem was not excessive domestic inflation vis-à-vis foreign countries but rather a decline in the terms of trade. Therefore, the purpose of the devaluation was not primarily to affect the real effective exchange rate but to offset the decline in the terms of trade. A country like Zambia, with copper accounting for 95 percent of its exports, had no practical alternative; if the terms of trade declined and the country wanted to maintain its mining industry at a viable level, it would have to move the rate. Nevertheless, in the forthcoming consultation report, the staff would give somewhat wider perspective to the role that exchange rate policy should play in the process of Zambia's diversification.

With regard to future copper price developments, the staff representative commented that predictions were difficult to make. The current price was about 65 cents a pound, but he recalled that when the Board had discussed Zaïre, the forecast for copper for calendar year 1984 had been 79 cents a pound. A sharp rise in copper prices would not be used as an argument to appreciate the exchange rate for the kwacha, because the medium-term aim of the exchange rate policy, as agreed with the Zambian authorities, was diversification.

The exchange rate adjustment, by making imports more expensive, had been a factor in reducing import demand, the staff representative explained, but the main instrument for limiting imports continued to be Zambia's restrictive import licensing policy. With regard to the figures for services and unrequited transfers in Table 3, the staff had not received data on which to base any change in the figures. However, during the forthcoming consultation discussions, the 1983 balance of payments data would be reviewed, estimates would be made for 1984, and the usual medium-term forecast for Zambia's balance of payments and debt profile would be formulated.

As mentioned previously, the next purchase, which would be based on end-December performance criteria, would also be subject to a review of budgetary policies for 1984, the staff representative from the African Department concluded. As the discussions would cover the general situation as well as the possible program for 1984, he was unable to state how speedily the review could be concluded and whether delays could be avoided. In any case, the final purchase could be made only after February 15, following assurances that the end-December performance criteria had been met and the conclusion of the review of budgetary policies for 1984.

Mr. Zhang noted that the staff had explained that the devaluation was necessary to intensify diversification of Zambian exports. He wondered whether in a country like Zambia, where nontraditional exports amounted to only 5 percent of total exports, any devaluation would have the favorable effects expected by the staff. He looked forward to further discussion of that point when the Board considered the next Article IV consultation report on Zambia.

Mr. de Vries said that, while he supported the Zambian program and the proposed decision, he remained doubtful about the procedure adopted in the present case. The staff had stated that the purpose of the review was to ascertain whether the exchange policy was flexible. For the planned budgetary review, he hoped that the staff paper would not simply state that budgetary policy continued to be cautious without supplying further information. Much more could have been written about Zambia's exchange rate policy; for example, a table noting the real exchange rate against specific balance of payments data would have been helpful. Until the recent depreciation, the real effective exchange rate of the kwacha had been approximately the same as in 1978; a great deal had happened since that time, and therefore he wondered whether Zambia had been able to make any real progress. His suggestions were offered in the hope that it would make other minireviews more meaningful.

The Acting Chairman remarked that it was worrying that the price of copper, at a time when some parts of the world were expanding economically, remained so low: about 65 cents a pound compared with an earlier estimate of 76 cents. The annual average price for 1983 was estimated to be 72 cents, whereas an earlier estimate had been 76 cents. The Commodities Division undoubtedly collaborated with the World Bank staff in arriving at copper price estimates, which were very important for Zambia, Zaïre, Peru, and Chile. Why was the reaction of copper prices so perverse in relation to economic expansion? Had substitution, especially in the telecommunications industry, played a role that was perhaps difficult to quantify at the present time?

A question had been raised earlier by Mr. Zhang whether profits could be used for investment in the mining company, the Acting Chairman recalled. Although profits might be insignificant, there was presumably some investment in relation to the cost-cutting efforts of the company. Were those investments significant, or were the cost-cutting measures related mainly to internal administration rather than capital investment?

The staff representative from the African Department explained that the latest official copper price forecast by the Fund's Commodity Division for calendar year 1984 was 79 cents, which was the price used in the Zaïre papers and which had resulted in a substantial purchase under the compensatory financing facility. It was difficult to explain why the copper price was not higher. One answer seemed to be that the supply and demand situation was not yet in balance. Until recently, the supply of copper had exceeded demand, and stocks, as shown in the statistics of the London Metal Exchange, had continued to rise. Production in Latin American countries had apparently increased substantially, while demand for copper continued to be weak. In addition, there was a certain amount of substitution, particularly in the telecommunications industry. Another factor was that Zambia's traditional markets for copper, Western Europe and Japan, had not experienced the strong economic recovery of the United States. It was hoped that, with the increasing recovery in Western Europe and Japan, demand for copper--linked to construction and housing--would increase. It was also worth noting that there was a strong speculative element in copper, which made it difficult to forecast the direction of prices.

There continued to be a substantial amount of investment in the mining company, largely for rehabilitation, the staff representative stated. The World Bank had been discussing a copper sector rehabilitation loan of $70 million, mainly geared to improving the facilities of the mining company. There had been considerable delays, but final negotiations between the World Bank and the Zambian delegation would begin on that very day. It was hoped that the copper sector loan could be presented to the World Bank Executive Board in March 1984. The thrust of the investment effort in Zambia was not so much to increase production as to maintain and rehabilitate the copper mining facilities; unless substantial rehabilitation took place, it would be impossible to sustain the existing level of production.

Mr. Sangare, responding to Executive Directors' comments, noted that two points had particularly attracted his attention. First, he wished to stress the authorities' commitment to continuing the flexible exchange rate policy currently in place. However, his authorities were concerned about a too-rigid association between the exchange rate and copper prices, which did not seem practical or logical, and which did not take into consideration the adverse implications of an exchange rate change for the rest of the economy.

Although the financial position of the mining sector was important, Mr. Sangare continued, Directors should not make it their only concern when considering whether a given exchange rate was appropriate, particularly when it was unclear whether the country would be required to appreciate its currency in the event of an increase in the price of copper, as Mr. Zhang had correctly pointed out. It was the hope of his authorities that the Fund would give greater consideration to that issue in order to arrive at a more balanced view of exchange rate adjustment.

Second, the worsening of the pressure on the exchange payments position of Zambia had resulted from delays in purchases from the Fund, forcing the authorities to enter into a bridging loan at high cost, Mr. Sangare remarked. That action could not alleviate Zambia's problems. The staff had indicated that Zambia might not meet the end-December performance criteria on external arrears and would need to obtain such bridge financing. Should that be the case, he would urge the Board to grant a waiver of the performance criteria. Finally, he wished to affirm the full commitment of his authorities to achieving the present program.

The Executive Board then approved the following decision:

> Zambia has consulted with the Fund in accordance with paragraph 4(b) of Executive Board Decision No. 7531-(83/142), adopted September 16, 1983, and paragraph 8 of the letter of the Prime Minister and Minister of Finance dated August 16, 1983, in order to review with the Fund the appropriateness of exchange rate policy. The Fund finds that no further understandings are necessary.

Decision No. 7595-(84/3), adopted
January 9, 1984

3. ZIMBABWE - 1983 ARTICLE IV CONSULTATION, REVIEW UNDER STAND-BY ARRANGEMENT, AND PURCHASE TRANSACTION - BUFFER STOCK FINANCING FACILITY - INTERNATIONAL SUGAR AGREEMENT

The Executive Directors considered the staff report for the 1983 Article IV consultation with Zimbabwe and review under the stand-by arrangement (EBS/83/264, 12/7/83; Sup. 1, 12/23/83; and Sup. 1, Cor. 1, 1/9/84), together with Zimbabwe's request for a purchase equivalent to SDR 2.099 million under the decision on the buffer stock financing facility (EBS/83/254, 11/29/83; Cor. 1, 12/9/83; and Sup. 1, 12/30/83). They also had before them a report on recent economic developments in Zimbabwe (SM/83/247, 12/9/83).

Mr. Sangare made the following statement:

> The staff report on the review of the stand-by arrangement and the 1983 Article IV consultation with Zimbabwe gives a clear picture of the continuing economic difficulties facing the country. It also highlights the Government's resolve to continue with the stabilization program approved by the Fund last March. In this

connection, it is pleasing to note that all performance criteria were met as of the end of September 1983; more importantly, the authorities are optimistic that the objectives of the program appear to be attainable.

It is necessary to stress at the outset, however, that the authorities are aware that the vulnerability of the economy to prolonged drought as well as to the impact of recessionary conditions abroad are serious constraints that render the task of managing their economy much more difficult, as demonstrated by the experience of the past two years. During this period, poor weather resulted in reduced agricultural output, and depressed demand abroad precipitated a decline in export prices, which led to the closure of some mines, while others operated below capacity. The net effect was a significant drop in the rate of growth of real GDP.

In the light of the foregoing, the Government of Zimbabwe continues to give priority to the goal of creating conditions conducive to sustainable economic growth. Accordingly, efforts are being directed at developing the major productive sectors of the economy, i.e., manufacturing, agriculture, and mining. Resources are also being channeled into the transport sector, which plays a vital role in Zimbabwe's landlocked economy. There have been some delays in project implementation, but the authorities are taking steps to improve the situation, which should increase the rate of disbursement of development assistance pledged by donor countries. Meanwhile, the private sector is being encouraged to play a major role in development and is expected to provide a significant part of total investment under the current development plan.

Many of the key economic indicators during the past year showed unsatisfactory results. Real GDP remained stagnant, reflecting adverse conditions and depressed external demand. The rate of inflation increased from about 14.6 percent in 1982 to 18 percent. The balance of payments deficit also widened owing in part to the exchange liberalization measures adopted earlier, coupled with the fact that capital inflow was less than expected. However, it is to the credit of the authorities that fiscal policy continued along the path of restraint in 1982/83. Actual expenditure during the period was below the level envisaged in the program, even though supplementary appropriations amounting to Z$60 million were made to cover emergency assistance to farmers affected by drought. The rise in the ratio of the budget deficit to GDP by about 1 percentage point more than expected during the period was therefore not due to the Government's policy becoming more expansionary, but rather to a shortfall in revenue, despite the additional tax measures taken in February 1983. It is important to note that the shortfall was most pronounced in the company income tax and sales tax, which reflected the destabilizing effect of the slowdown in economic activity.

The policies for the current fiscal year, many of which are already being implemented, continue to stress demand restraint in order to contain inflation and reduce pressure on the balance of payments. In this connection, a number of new revenue measures have been adopted, including an increase in the surcharge on individual income tax and company income tax, an increase in the rate of sales tax, and an increase in the import surtax. The authorities expect that the new tax package will help to maintain the ratio of tax revenue to GDP at 30 percent. Steps have also been taken to restrain the growth in expenditure. For instance, subsidy payments have been reduced by 27 percent, a shift made possible by substantial price adjustments that have significantly improved the financial position of the marketing boards. The railway and electricity corporations have also benefited from price increases. Another area where economies are to be effected is the public sector wage bill. Not only do the authorities intend to maintain a tight employment policy, they are also continuing with the policy of wage restraint. The increase in the wage bill is expected to be reduced by half compared with the annual average increase of 22 percent over the past three years. With capital expenditure being limited to the same nominal level as in 1982/83, the budget deficit is projected to decline to the equivalent of 7.3 percent of GDP from 8.5 percent in the previous year. The deficit is expected to be financed mainly through an accelerated inflow of external capital, so that net domestic credit to the Government is projected to increase by 19 percent, compared with 26 percent in 1982/83.

In the external sector, several measures are being implemented to promote exports, including favorable foreign exchange allocation for registered exporters, a revolving fund that provides assistance to new exporters or registered exporters with unexpectedly large orders--this fund has been boosted by the World Bank export promotion loan of US$70.6 million approved in February 1983--and a price structure that provides special incentives for the cultivation of crops with good export potential. However, there was a further decline of 12 percent in exports in 1983, contrary to the program assumption that they would increase by 7 percent. The exchange rate actions appeared to have had beneficial effects in imporving the competitiveness of Zimbabwe's manufacturing sector. However, the effect of the global recession, which subdued demand for the country's export commodities, remained. Although the trade and current account balances were stronger than envisaged under the program, it is important to note that the situation resulted mainly from a 22 percent decline in imports rather than from an improvement in underlying conditions. With capital inflows being less than expected, the overall balance of payments deficit is projected to increase to SDR 283 million in 1983, compared with the program estimate of SDR 227 million.

Since the exchange rate actions taken in late December 1982 and early 1983, the authorities have continued to implement a flexible exchange rate policy. The objective is to prevent an appreciation of the real effective exchange rate during the period of the program.

With regard to Zimbabwe's medium-term prospects, the vulnerability of the economy to exogenous forces, as mentioned earlier, points to the need for caution in making assumptions about the future. As for the outcome in 1984, much will depend on the strength of the recovery in external demand, the level of international commodity prices, developments in the agricultural sector, and the level of capital inflow, particularly the rate of disbursements of assistance under the Zimbabwe Conference on Reconstruction and Development (ZIMCORD). With these provisos in mind, the current account deficit is projected to increase in nominal terms but to decline slightly in terms of GDP, while the overall balance of payments deficit is projected to show a small reduction. If the assumptions outlined in the staff paper remain relevant over the medium term, the balance of payments is expected to be in surplus by 1987.

The justification for the request to purchase SDR 2.009 million under the buffer stock financing facility has been spelled out clearly by the staff. In June 1982, Zimbabwe constituted its minimum stock obligation of 15,337 tons of sugar for the 12-month period ended June 30, 1982. This has been verified by an on-site inspection carried out by the International Sugar Organization. The balance of payments need of Zimbabwe cannot be overemphasized, and the staff agrees that the authorities have been and are continuing to cooperate with the Fund in an effort to improve their external payments position.

In closing, I would only say that the policies that my Zimbabwean authorities have put into effect in the recent past lead one to the conclusion that economic performance would have been far better had there been no prolonged drought and had conditions in the international economy been less harsh. However, the setbacks experienced have not weakened their commitment to the pursuit of agreed policies, which, they believe, will eventually stabilize and strengthen the economy. This being said, I would urge Directors to approve the draft decisions that appear in EBS/83/264, Supplement 1, including the modification to the performance criteria that will enable Zimbabwe to purchase the amounts originally scheduled for 1983 under the stand-by arrangement upon today's completion of the review. I also recommend for approval the proposed decision on the buffer stock purchase.

Mr. Wicks stated that he endorsed the staff appraisal and firmly supported the proposed decisions, including the drawing under the buffer stock financing facility. Undoubtedly, economic policymaking in Zimbabwe had been made much harder in recent years by circumstances outside the country's control, such as the severe drought, transport difficulties in shipping exports, the effects of the world recession, and the continuing effects of the situation inherited by the new Government. Although some weaknesses in economic policymaking had also contributed to the adverse trends, it was to the credit of the Zimbabwean Government that it had courageously tackled those problems by devaluing the currency, raising producer prices, holding down real incomes, and controlling public expenditure. He especially commended the prompt remedial action taken in the summer to deal with the emergency expenditure necessitated by the drought and with the lower revenue resulting from the reduction in economic activity.

With regard to wages and price policy, Mr. Wicks continued, he praised the difficult decision to raise consumer prices well above the general rate of inflation and the intention to restrict wage increases to a rate well below that of inflation. Although those measures were unpalatable, that policy was essential if the share of consumption in GDP--at present an excessive 90 percent--were to be reduced, and if the current account deficit were to be contained. He wished to repeat his concern expressed in March that unprofitable industrial and mining companies appeared unable to lay off workers because of the current labor laws; those companies therefore had to borrow at high rates in order to pay salaries, obviously hindering the companies' competitiveness. He also noted that the prices paid to farmers for maize and other crops had been increased at a rate equivalent to or slightly below the rate of inflation. He wondered whether the staff regarded the current level of agricultural producer prices sufficient, in the aftermath of the drought, to give farmers the incentive to maintain and increase production.

Fiscal policy seemed to be moving in the right direction, Mr. Wicks commented, but further reductions in the overall public sector deficit--below the projected 7.2 percent of GDP for 1983/84--should be carried out in the next two years. He was unclear about the reason for the new treatment of parastatal losses referred to on page 14 of EBS/83/264; he hoped that it was not a sign of recourse to "off-budget" transactions, which would undermine the budgetary control procedures that had been strengthened in recent months. The Government had recently announced a substantial program of support for the Zimbabwe Iron and Steel Company, including capital expenditure and reimbursement of trading losses for three to five years. Although the industry was important to Zimbabwe for foreign currency conservation, the company was working at only 50 percent capacity, and, as his own country knew from bitter experience, support for the steel industry could prove expensive. He therefore hoped that support for the company fit into the recovery program and would show a positive return fairly quickly.

On monetary policy, he urged the authorities to move interest rates on savings to positive real levels as quickly as possible, Mr. Wicks stated. With regard to external policy, first, continued maintenance of a competitive exchange rate was important; Zimbabwe had already witnessed the advantages of the difficult decision that it had taken on that front, and he hoped that exchange rate competitiveness would be maintained. Second, he endorsed the authorities' caution about undertaking further non-concessional debt in 1983. Continued prudence should lessen the projected debt service peak of 34 percent forecast by the staff for 1988. In particular, he urged caution in contracting short-term bank credit, which could handicap recovery by imposing a higher early servicing burden. He therefore welcomed the continuance of strict limits on external borrowing under five years, the ban on all new net short-term borrowing, and the ban on commercial borrowing for balance of payments purposes with maturity of less than one year. The maintenance of a strong private sector element in the economy was laudable, and he hoped that the authorities would encourage foreign private investment.

Economic policy in Zimbabwe was proceeding in the right direction, Mr. Wicks stated. Movement to a firmer balance of payments position was an ambitious but essential task, which was not beyond the capacity of Zimbabwe with its broadly based economy, its diverse exports, its relatively well-developed infrastructure and skilled bureaucracy, and its rich natural resources. Nevertheless, the proposals and tables in the staff paper on the medium-term balance of payments prospects were worrying. In Table 7 of EBS/83/264), the staff had identified a financing gap through 1988 under one principal scenario, while Table 8 showed a rise in the debt service ratio from 10 percent in 1982 to 34 percent in 1987. He wondered whether those scenarios were sustainable. He would have liked to see a quicker move to a firmer balance of payments position than that shown in the tables, and he hoped that in the next review the staff and the Zimbabwean authorities would endeavor to illustrate how that move could be achieved.

Zimbabwe's problems had a strong structural element and would require adjustment over the medium term, Mr. Wicks observed. Part of that adjustment had to focus on macroeconomic policy, which was a traditional concern of the Fund. But equally important were structural adjustment measures at the microeconomic level--further improvement of infrastructure, particularly transportation, and strengthening and diversification of the industrial and agricultural base--which were concerns of the World Bank. He was pleased to note that the World Bank was active in that respect.

Further Fund support almost certainly would be required after the termination of the present stand-by arrangement, Mr. Wicks stated. Such support should be determined in the context of a medium-term economic framework, but not necessarily an extended arrangement. The extended Fund facility should be used, for example, only when there was a reasonable hope that the member would be in an externally sustainable position by the end of the program period. Although his mind was not closed regarding an extended arrangement to follow the current stand-by arrangement, the medium-term scenarios in the staff paper suggested that further policy measures leading to a stronger degree of adjustment would be required before confidence in the member achieving that adjustment could be reached. Much depended on the success in implementing the remainder of the current program and on the production of a coherent medium-term framework, which he hoped to see in the next review.

Mr. Polak observed that the authorities had adhered to the agreed policies in spite of the deterioration in the external position. It was clear that government revenue in 1982/83 had fallen short of expectations, mainly owing to the failure of gross domestic product to grow as expected because of bad weather. Nevertheless, it was commendable that the Government had been able to observe its expenditure targets. Naturally, those developments had led to budget deficits in 1982/83 and 1983/84 that were larger than originally planned, causing the nonobservance of the June criterion for bank credit to the Government. However, the performance criterion for total domestic credit had been observed, possibly facilitated by the fact that total domestic credit at the end of 1982 had been 3 percent lower than stated earlier. He invited the staff to comment on that development. He especially wished to commend the authorities for the price measures that they had taken recently, as a result of which agricultural prices had been increased to a level that should eliminate subsidies.

He was not clear about the budget deficit of the parastatals, Mr. Polak commented. Unlike the budgets of previous years that had covered the considerable losses of the agricultural marketing boards, the National Railways of Zimbabwe, and Air Zimbabwe, the 1983/84 budget provided coverage for only half of those deficits; the narrower coverage reduced the government deficit and thereby bank credit to the Government in 1983/84 by as much as 3.2 percent of GDP. With that in mind, the present estimates for that deficit of 8.5 percent and 7.3 percent for 1982/83 and 1983/84, respectively, did not compare favorably with the original targets of 7 percent and 5 percent. He would appreciate further explanations by the staff.

On the external side, Mr. Polak continued, the staff appraisal had mentioned that Zimbabwe's medium-term balance of payments outlook remained difficult. That clearly was an understatement; the situation had become even less sustainable than it had appeared in earlier papers. In March 1983, he had suggested that Zimbabwe should aim at a shorter adjustment period than the five years envisaged at that time. The present medium-term scenario did show a somewhat shorter period, with a current account deficit of SDR 400 million in 1987 instead of the SDR 700 million forecast in March. Nevertheless, the present interest payment and export projections entailed a debt service ratio of 34 percent in 1987 instead of the 22 percent estimated earlier and the current 17 percent. The medium-term scenario showed exports reaching the earlier 1983 target in 1984 and imports reaching the 1983 target only in 1988; he invited the staff to comment on those disparate forecasts. The scenario was based on a continued improvement in Zimbabwe's competitiveness as a result of exchange rate policy. However, it was clear that the exchange rate policy would do no more than prevent any real effective appreciation. Why should the maintenance of the real effective exchange rate stimulate exports in the longer run? In addition, it seemed clear from the medium-term scenario that a stronger exchange rate adjustment was called for in order to bring about a quicker and more certain adjustment than the one foreseen for the medium term.

The object of the present review was to concentrate on the adequacy of the exchange rate policy, Mr. Polak stated. In March 1983, he had asked the staff to explore that matter further during the present review because there had been considerable doubt whether the exchange rate at that time had been overvalued. It was not encouraging that import surcharges had been increased from 15 percent to 20 percent.

Fund involvement with Zimbabwe continued to suffer from the lengthy periods spent in negotiations, Mr. Polak observed. It had been planned to conclude the present review before June 30, 1983 and the following review before the end of 1983. Because it was only an 18-month program, he wondered why the two reviews had not been combined. On a technical point, the staff paper mentioned that the performance criteria for September 1983 had been met but that the Board would set those performance criteria in the proposed decision. What was the actual value of criteria set after the event? Nevertheless, he had been impressed by the substantial efforts made by the Government of Zimbabwe, and he was pleased to support the three proposed decisions.

Mr. Orleans-Lindsay stated that he was in broad agreement with the staff evaluation of the Zimbabwean economy's developments and prospects. The papers provided a clear analysis of the problems facing the country and emphasized the authorities' resolve to persevere in attaining the objectives of the stabilization program, which had gained Fund support in March 1983. Therefore, he supported the revised proposed decisions and the purchase under the buffer stock financing facility.

During the past two years, Mr. Orleans-Lindsay continued, the Zimbabwean economy had suffered serious setbacks, mainly as a result of a long period of drought together with the adverse impact of exogenous factors. Agricultural output had declined, the international recession had led to a reduction in exports, and overall there had been a substantial decline in the rate of growth of real GDP from 12 percent in 1981 to about 1 percent in 1983. The rate of inflation had increased to 18 percent in 1983, from about 14 percent in 1981--a reflection in part of the depreciation of the currency in January 1983. The budget deficit had increased slightly as a proportion of GDP--by about 1 percentage point--between 1981/82 and 1982/83, largely due to a shortfall in revenue stemming from the impact on receipts of depressed economic activity, poor weather, and the sluggish international trade. Partly as a result of the decline in exports and the higher net outflow of investment income, the current account deficit of the balance of payments had widened from SDR 616 million in 1981 to SDR 703 million in 1982. The deficit on the overall balance, on the other hand, had been reduced from SDR 151 million in 1981 to SDR 86 million in 1982 because of an increase in net foreign capital inflows.

It was encouraging that the authorities had responded promptly to those adverse developments and had adopted strong adjustment measures, giving priority to the objective of creating the conditions that would be conducive to sustainable economic growth, Mr. Orleans-Lindsay noted. He welcomed the emphasis that had been placed on the development of the agricultural, mining, and manufacturing sectors. In the transportation sector, which was vital to the landlocked economy, the authorities should eliminate the delay in project implementation associated with the low rate of disbursement of project assistance funds.

He commended the Zimbabwean authorities for meeting all performance criteria for the September 1983 quarter of the 1982/83 program, after the initial difficulties that they had experienced in observing the ceiling on net bank credit to the Central Government for the June 1983 quarter, Mr. Orleans-Lindsay said. He welcomed the policies and measures that had been formulated for implementation during the remainder of the program period in the context of the 1983/84 budget. The thrust of those policies, which continued to emphasize the need to restrain demand in order to contain inflation and reduce pressures on the balance of payments, seemed appropriate. Both the new revenue measures that had been adopted for improving the ratio of tax revenue to GDP to about 30 percent, and those that had been taken to restrain growth in expenditure, were in the right direction. He welcomed in particular the 27 percent reduction in subsidy payments through significant price adjustments effected as part of the program to improve the financial position of the marketing boards. Like Mr. Wicks, he was unsure about how the authorities intended to bear the losses of the parastatals in the budget, and he asked the staff for further comment.

The authorities intended to maintain a policy of wage restraint and tight employment, under which they expected to obtain greater control over the overall wage bill, Mr. Orleans-Lindsay remarked. Although total capital expenditure would be limited to its 1982/83 level in nominal terms as a way of reducing the projected budget deficit to 7.3 percent of GDP in 1983/84, such cutbacks in capital expenditure seemed unfortunate in relation to Zimbabwe's medium-term development prospects. It was encouraging to note that the authorities proposed to limit their reliance on bank financing of the budget deficit, which would be financed largely by an inflow of external resources.

In the external sector, the authorities' intention to continue their policy of managing the exchange rate in a flexible manner was most welcome, Mr. Orleans-Lindsay commented. The exchange rate action taken in December 1982 and early 1983 appeared to have had positive results, notably an improvement in the competitiveness of the manufacturing sector. The measures being implemented to promote exports, such as favorable foreign exchange allocations for registered exporters, should go a long way toward counteracting the effects of the international depression that had adversely affected the country's export commodities. Zimbabwe's medium-term prospects had been based on assumptions that projected a surplus on the balance of payments in 1987, but the economy would remain dependent on external factors over which the authorities had no control. In the immediate future, Zimbabwe would remain in balance of payments need, and it was encouraging to note that the authorities were determined to continue to cooperate with the Fund to find and implement appropriate measures for improving the external payments position.

Mr. Caranicas noted that it was useful to combine Article IV consultations with reviews under stand-by arrangements. In the present case, the staff report, combined with the letter of the Minister of Finance, Economic Planning and Development of Zimbabwe, the Government's Memorandum on its Economic Financial Policies, and Mr. Sangare's informative statement, contributed to easier and shorter Board consideration of the Zimbabwean economy. He was in broad agreement with the staff's appraisal and supported both revised proposed decisions.

It was only logical that, upon conclusion of the present review, Zimbabwe should be permitted to purchase the amounts originally scheduled for 1983, Mr. Caranicas continued. It was also reasonable that further purchases during 1984 should remain subject to the completion of the second review scheduled to begin in February, and to the observance of relevant performance criteria until another discussion of the case in March. Ceilings would be established later than originally planned, and the phasing of purchases would have to be adjusted accordingly.

He also approved the purchase requested under the buffer stock financing facility because it met all the requirements, Mr. Caranicas commented. Zimbabwe had to be considered in the wider framework of continued drought and other natural disasters in Africa, the resulting poorest harvest in years, and the weak and delayed recovery in the industrial countries in 1983. Like other developing countries, Zimbabwe suffered also because of its overdependence on industrial countries, particularly the members of the OECD. The economy was vulnerable to prolonged drought as well as to the recessionary conditions in the world, and there were serious constraints that rendered the task of managing the economy much more difficult.

Zimbabwe was further afflicted by the legacy of the troubled years before independence, its evolving transformation under the social program of the Government, and the great expectations of its people from the land distribution program, Mr. Caranicas observed. The authorities had to balance the peasants' desire for land against the farmers' need to remain viable. On the other hand, the stringent budget had reduced allocations for land purchases with which to increase tribal trust lands. Another adverse factor was the slowness of the resettlement program, whose cost had been underestimated, contributing to the increasing uneasiness of the farm population. In passing, he noted that the recent cut in U.S. aid to Zimbabwe would not ease those tensions.

It was obvious that the optimistic export forecasts for 1983 had not materialized, as exports had declined in nominal terms year over year, Mr. Caranicas remarked. However, the lagged effect of the sizable real exchange rate realignment, which had occurred following the devaluation effected in December 1982 and January 1983, should improve the environment for exports of both agricultural and manufactured goods during 1984. That consideration appeared to underpin the staff's expectation of an export rise of about 12 percent in 1984. He wondered what assumptions had been made by the staff concerning world demand and commodity prices, particularly minerals, which had started 1983 under new pressures.

Fiscal developments had been disappointing, Mr. Caranicas continued. Revenue shortfalls had been the result of the severity of the recession, compounded by the drought and other adverse factors. He was not sure what the appropriate response of expenditures should be to the evolving situation.

It appeared that despite efforts of the authorities, current outlays had not been held back sufficiently. In the final analysis, the actual overall deficit for 1982/83 had not been smaller than two years earlier, and the targeted reduction in 1983/84--a little above 1 percent--did not seem adequate.

The medium-term balance of payments and debt scenario in Table 7 of EBS/83/264 offered useful information about the future outlook for Zimbabwe's external accounts, Mr. Caranicas observed. The financing requirement for the coming years was significant: persistently large through 1987, declining but still positive in 1988, and reversed only in 1989. Concessional external finance and balance of payments support would continue to be necessary in a significant proportion over the medium term. He urged a faster rate of disbursement of concessional assistance pledged under the Zimbabwe Conference on Reconstruction and Development (ZIMCORD). Finally, he shared previous speakers' commendation of the Zimbabwean authorities' policies. Their readiness to take further measures as necessary to achieve a strong foundation for a resumption of economic growth was commendable.

Mr. Jaafar said that he supported the staff appraisal and the revised proposed decisions on the Article IV consultation and the review under the stand-by arrangement. He commended the authorities for their courage in taking up those adjustments under extremely difficult circumstances. Severe droughts for the past two years had adversely affected output of maize, Zimbabwe's major crop. The shortages could again put pressure on domestic prices in the 1983/84 program period. While the devaluations of 20 percent in December 1982 and 5 percent in January 1983 had been necessary because of the reportedly overvalued exchange rate, he wondered whether they had been entirely appropriate in terms of timing. The rapid rise in prices of 18 percent in 1983 could flare up again if unanticipated agricultural supply shortages should occur in 1984, particularly in food items. In addition, the upward adjustment in prices of certain controlled items, while beneficial to the marketing board in terms of revenue, could be a source of instability if the once-and-for-all price increases did not adequately reflect the market. The role of expectations could augment pressure on prices so that they would have to be further adjusted. He therefore urged the authorities to remain flexible in their application of price controls.

He was concerned that, because of the unfavorable external and domestic situations, the initial advantage of devaluation in restoring competitiveness and export expansion might have been neutralized by inflation, Mr. Jaafar commented. It was therefore important that the authorities should remain committed to managing the exchange rate with flexibility. While there was a need for Zimbabwe to gain a competitive edge, the authorities would have to weigh it against the immediate need to restore price stability domestically. Any future move to devalue would have to be viewed in terms of the country's ability to respond quickly to such a stimulus.

On revenue and expenditure, there was an urgent need to stimulate the economy, especially in view of the extremely difficult situation as a result of the drought and recession, Mr. Jaafar remarked. The acceleration in expenditure as envisaged in the 1983/84 program would have to be matched realistically by revenue and external financing, for example, from ZIMCORD. The depression in the economy during the previous financial year had resulted in substantial shortfalls in revenue; a similar situation could be repeated in view of the expected modest increase in revenue in the coming fiscal year. Caution was called for, particularly in spending, as outlined in the budget. That uncertain outlook emphasized the importance of firming up pledged concessional flows to avoid repeating the substantial unanticipated shortfall of the previous fiscal year, which had also resulted in nonobservance of domestic credit subceilings. The authorities might have to streamline the administration and implementation of projects with a view to increasing capacity, as envisaged under ZIMCORD.

With regard to price adjustment, Mr. Jaafar continued, he hoped that the significant increase in prices would produce a once-and-for-all effect on inflation. In the medium term, more flexiblity should be introduced in managing commodity prices to ensure that they reflected the underlying market conditions in terms of supply and demand. The objective should remain that of letting the free play of the market determine prices of those commodities. He supported the wage restraint measures, but their effect might be harsh on wage earners because of the rapid rise in prices due to devaluation, drought, and significant increases in administered prices. Under the circumstances, he urged that any future restraint should not be so severe as to invite other undesired side effects. While he was pleased that the authorities had provided for wage reviews later in 1983/84 with a view to keeping the increase to no more than 5 percent, he noted that expected inflation in the coming fiscal year was 16 percent, three times the potential increase in wages. Finally, he supported Zimbabwe's request for the use of Fund resources under the buffer stock financing facility.

Mr. Suraisry remarked that he supported the proposed decisions, together with Zimbabwe's request for a drawing under the buffer stock financing facility. The authorities had made determined efforts in recent months to correct the imbalances in their economy. Performance under the present stand-by arrangement had been generally satisfactory, all but one of the quantitative criteria having been met. The economy, however, had been adversely affected by the continuing depression in world demand for minerals and by the severe drought, which had reduced agricultural output and export earnings. Real growth was stagnant, inflation remained high, and there were sizable deficits in both fiscal and external accounts. There was, therefore, no room to relax the adjustment effort. The authorities recognized the situation, and the program for 1983/84 seemed well designed to contain inflationary pressures and strengthen the external position. In particular, he welcomed the continuing emphasis on fiscal restraint in the 1983/84 budget. The decisions to freeze government employment and to reappraise the educational program should yield substantial savings on current expenditure. It was also sensible in present circumstances to limit capital expenditure to ongoing projects. Significant progress had already been made in improving the financial position of the public enterprises, and he hoped that the authorities would continue to explore new ways of making those enterprises more profitable in the future.

He welcomed the authorities' firm stand on wage policy, Mr. Suraisry remarked. It was encouraging that recent wage settlements had been within the 5 percent overall limit set by the Government. Similarly, the recent increases in consumer and producer prices should lead to a more efficient allocation of resources. In particular, the new structure of producer prices seemed to provide the necessary incentives for boosting production of export crops.

On the external sector, he agreed with the authorities that the exchange rate should continue to be managed flexibly in order to maintain Zimbabwe's competitive position, Mr. Suraisry commented. Although much of the adjustment in the current account in 1983 had been the result of a sharp reduction in imports, there were encouraging signs that exports were picking up as the lagged effects of the recent devaluation came through and the recovery became stronger.

The medium-term prospects were difficult to assess, Mr. Suraisry continued. Much would depend on three factors: a recovery in the world economy, the sustained pursuit of firm adjustment policies, and adequate foreign assistance on concessional terms. The authorities should take the necessary steps to improve project preparation and implementation and to make new arrangements with donors to speed up aid flows. Like Mr. Wicks, he hoped to see a better medium-term balance of payments outlook in the next review. In brief, the authorities appeared to be on the right course. If they adhered to present policies, there was a good chance of resolving their present difficulties. The next review in February would provide an important opportunity to evaluate progress and to consider any necessary adaptations in policy.

Mr. Joyce stated that he agreed with the general assessment and policy prescriptions set out in the staff paper; he supported the proposed decisions, including the waiver that would permit purchases to be made upon completion of the present review. He also supported the proposed purchase under the buffer stock financing facility. He was concerned, however, that as yet no performance criteria had been set for 1984, and he wondered why such criteria for the balance of the program period had not been established in conjunction with the present review.

The authorities had shown a commendable determination to tackle their economic difficulties and had taken a large number of welcome policy actions, Mr. Joyce continued, particularly, measures to increase government revenues, restrain government expenditures, adjust domestic prices, change the exchange rate, restrain wages, and conserve energy. In part because of those measures, the current account deficit of the balance of payments in 1983 and 1984 was projected to be much lower both in absolute terms and as a percentage of GDP than had originally been expected under the program, despite lower than expected export earnings. However, the current account deficit remained high, and the external situation still gave cause for concern. In particular, it was worrying to note that, with the marked shortfall in capital inflows, the overall balance of payments deficit had increased sharply in 1983 and was projected to remain large in 1984, with a financing gap of about SDR 100 million.

Like Mr. Wicks, he was concerned about the apparent need for exceptional financing envisaged through 1988, even assuming annual net capital inflows in 1985-88 double those of 1983, Mr. Joyce remarked. Even if such financing could be arranged, it would lead to a sharp rise in the debt service ratio, projected to increase from 17 percent in 1983 to 34 percent in 1988. Moreover, the projected rise in the interest component of the debt service ratio from 9.5 percent of exports of goods and services in 1983 to 12 percent in 1984 and 14.5 percent in 1987 was clearly a matter of concern. In the light of those considerations, it was important for aid donors to maintain, rather than cut back, aid flows to Zimbabwe, and to take whatever steps were necessary, in conjunction with the Zimbabwean authorities, to ensure that aid disbursements were made with dispatch.

Similarly, he urged the authorities to pursue adjustment measures with determination and to consider ways in which the adjustment process might be strengthened, Mr. Joyce continued. He welcomed the planned review early in 1984 and noted that it was intended to reach understandings to ensure that the 1984 balance of payments deficit would be fully financed. He urged the Zimbabwean authorities to prepare contingency policies that could be introduced speedily if capital inflows should again fall short of expectations.

He congratulated the authorities on the measures that they had taken to reduce the broad public service sector deficit from 10.5 percent of GDP in 1982/83 to 7.2 percent in 1983/84, Mr. Joyce said. That action was particularly impressive at a time of drought, which had inevitably led to certain emergency expenditures and, together with the recession in overseas markets, a reduction in tax revenues. He therefore welcomed, inter alia, the increases in administered prices that had resulted in sharp reductions in the losses of the parastatals and marketing boards, as well as the program intended to end railway subsidies by 1984/85. He wondered about the position of the remaining parastatals and whether some might still be in financial difficulties. Like Mr. Wicks and others, he was not clear how the deficits of the parastatals were to be financed, and he would appreciate further information from the staff. In any event, the authorities would have to continue to adjust prices to ensure that losses did not re-emerge.

He praised the wage restraint measures in the public sector and the decision to freeze the level of public service employment, Mr. Joyce continued. Those measures were not easy to implement in a developing country such as Zimbabwe, because pressures were extremely strong to use the public service to take up the slack in employment in the economy, a dangerous course to pursue. The new tax measures, which were designed to yield the equivalent of 2.4 percent of GDP in 1983/84, and the system of monitoring government expenditure introduced in 1983, were commendable. The government deficit remained high and was expected to be only slightly lower than in 1980/81 and 1981/82; any further action by the authorities to rectify the fiscal weakness would be welcome.

The authorities had made substantial progress in their reconstruction efforts, in eliminating the dual nature of the economy, and in bringing greater equity to Zimbabwean society, Mr. Joyce observed. They had taken a number of important steps to improve incentives for producers, and he was pleased to note that the currency devaluation and the continued flexible management of the exchange rate in 1983 appeared to be yielding positive results, at least in Zimbabwe's exports of manufactured goods. However, he would be interested in staff comment on whether there was room for further producer price adjustments at present and whether current agricultural producer prices were high enough in the aftermath of the drought. He would also appreciate the staff's view on the efficacy of the economy-wide price controls currently in effect. In conclusion, he wondered whether it would be advisable to provide incentives to the communal farms that controlled 81 percent of the land, so that those farms could increase their marketable surplus from the present low 10 percent of production.

Mr. Williams said that he supported the revised proposed decisions on the 1983 consultation and the review under the stand-by arrangement, as well as the purchase under the buffer stock financing facility. Zimbabwe's economic performance had been adversely affected by exogenous factors, which had made the current adjustment efforts more difficult but also more necessary. His authorities believed that, when viewed in the context of the unfavorable economic developments surrounding the end-June review date, it was remarkable that Zimbabwe had missed the criterion related to net bank credit to the Government by only 1 percent of public expenditure.

The approach taken by staff and management in the present case had been appropriately prudent and cautious, Mr. Williams continued, particularly in bringing the papers to the Board only after all the agreed pricing measures had been implemented. While that action had resulted in a delay of purchases by Zimbabwe, the adverse effects of the delay had been more than compensated for by the heightened confidence in the ultimate success of the program that had been gained by having the key adjustment measures firmly in place. Thus, he had no problem with the revised schedule of purchases indicated in Table 1 of EBS/83/264, Supplement 1. He hoped that the Zimbabwean authorities would be able to adopt and implement in a timely manner whatever adjustment measures might be required in the future to respond to economic and financial developments.

As indicated in Table 7 of EBS/83/264, Zimbabwe's medium-term prospects were difficult and would require the continued pursuit of appropriate demand management and structural adjustment measures for the next several years if a sustainable balance of payments position were to be attained, Mr. Williams observed. He welcomed further staff comment on what it considered essential elements of those policies over the medium term. The World Bank must continue to play a substantial role in Zimbabwe's medium-term structural adjustment efforts. The projections for debt service over the medium term were cause for concern; they reinforced his impression that it was essential to ensure that financing of Zimbabwe's current adjustment efforts was appropriate to its debt service capability.

Regarding fiscal policy, Mr. Williams noted that expenditures related to the drought seemed to have increased the overall deficit by about 55 percent. He encouraged the staff and the authorities to adjust future expenditure and deficit targets downward as climatic conditions improved.

The key element in Zimbabwe's efforts was the wage and price policies pursued by the authorities, Mr. Williams commented. The recent decisions with respect to producer and consumer prices were necessary if they were to attain their economic objectives. He encouraged the authorities to continue to pursue a market-oriented pricing policy, which should provide the basis, along with a flexible exchange rate policy, for achieving a sustainable balance of payments position over the medium term and favorable economic growth. He would appreciate staff comment on the procedures and methods that the authorities intended to use in the future to adjust prices on both the consumer and the producer sides.

Mr. Alaoui-Abdallaoui said that in view of the broadly satisfactory performance of the Zimbabwean economy under the stand-by arrangement and the authorities' successful efforts to meet the program's objectives and performance criteria, despite adverse external factors such as severe drought and prolonged regional instability, he joined other speakers in supporting the proposed decisions.

Mr. Qureshi remarked that Zimbabwe's request for a purchase under the buffer stock financing facility met all the requirements of the relevant Board decisions (Decisions No. 2772-(69/47), 6/25/69; No. 4913-(75/207), 12/24/75; and No. 5597-(77/171), 12/16/77; he therefore had no difficulty in supporting the request. With regard to the Article IV consultation and review under the stand-by arrangement, he was in broad agreement with the thrust of the staff appraisal and supported the proposed decisions. In spite of adverse exogenous developments, which had particularly affected the real sector and put additional strains on the external position, nearly all performance criteria had been met, and the overall adjustment effort had been sustained broadly in line with the path envisaged under the arrangement. The authorities deserved commendation for that achievement. It was also noteworthy that the adjustment effort had been fairly wide ranging, combining monetary and fiscal restraint with structural improvements, such as cost-price rationalization, the strengthening of the financial position of public enterprises, and the pursuit of a flexible exchange rate policy. But for the adverse exogenous developments, improvements in the economy's growth and financial performance would have been significantly greater.

Adjustment policies pursued to date and those to be pursued in the coming period promised an encouraging improvement in the economy's domestic and external financial performance over the medium term, Mr. Qureshi continued. He was pleased to note the authorities' determination to continue their financial and structural reform efforts, and to strengthen those efforts where needed. Clearly, the hoped-for improvement in economic performance over the medium term could not be attained without a continuing and firm commitment to adjustment. It should be equally clear, however, that the realization of the medium-term economic goals would also depend on improvements in the external economic environment, as well as on the maintenance of an adequate inflow of external resources.

Mr. Zhang stated that he supported the three proposed decisions.

The staff representative from the African Department said that, with regard to labor policy and, more specifically, the question whether companies were allowed to pursue flexible policies in the current economic situation, one of the largest nickel mines had closed, and several other mines were working at reduced capacity. There had been reports of several small and medium-sized enterprises that had reduced operations where required by their financial situation. In the government sector, no vacancies could be filled without the permission of the Minister of Finance and the Public Service Commission. Recently the Government had announced a reduction in the size of the Cabinet, and the Prime Minister had stated that it was his intention to reduce the size of the Government. It was, therefore, the authorities' understanding that the volume of employment would be related to the financial position both of the Government and of the various enterprises. In the case of the steel company and the various mining companies, government support had been in response to requests for assistance. The companies had argued that in other countries where similar companies had to compete with exporters, those companies received government assistance. The Fund staff had participated in lengthy discussions with the authorities, and the staff believed that the government measures taken to date had not been excessive; but the staff would continue to monitor the situation, particularly the measures announced for the steel companies.

As to producer prices, the staff representative continued, Table 3 in SM/83/247 indicated that the producer price for maize had been increased by about 50 percent in 1982, that for cotton by about 25 percent, and that for several other commodities by a substantial amount. For 1983, the increases had been about 10-20 percent, which were considered adequate. Calculations of the cost-benefit financial position for farmers indicated that the prices were not a disincentive. In fact, for many commodities, especially maize, prices were a powerful incentive, and the restriction on output in the past had been due to the drought rather than to low producer prices. However, the staff would review producer prices for the following season.

As to the monetary figures and the achievement of the overall credit ceiling in June 1983, the staff representative recalled that normally the agricultural marketing boards took in products at the beginning of the marketing season, usually March-April. In 1983, because of the severe drought, the maize crop had been only 610,000 tons, compared with 1.4 million tons in 1982, thus severely reducing the demand for credit by the marketing boards to finance crop purchases. As credit for normal private sector activity had been severely reduced, the overall ceiling had been observed despite a slight excess of government credit.

The exchange rate policy under the program had included a 25 percent devaluation at the outset and the maintenance of real effective exchange rates thereafter, the staff representative noted. The combination would lead to an increase in competitiveness and not to the maintenance of the relative exchange rate. At end-1983, an increase in orders for manufactured exports had been discernible, manufacturing being the sector most likely to respond favorably to changes in the exchange rate, and it was hoped that further progress would be achieved in 1984. In view of the medium-term prospects, the staff planned to keep that policy instrument under review and to recommend exchange rate action as required. Because of fiscal exigencies, increases in the import surcharge had not taken place. During the mission to discuss the budget for 1984/85, the staff would keep in mind Mr. Polak's statement that the exchange rate should be used more actively to influence exports and imports while, to the extent that the fiscal situation permitted, there should be less reliance on the import surcharge.

The Board was considering the present review after a number of measures had been taken by the Zimbabwean authorities, the staff representative remarked. The wage measures discussed in May had been implemented in September, and budget developments had been observed during the first six months of the fiscal year. It would be useful to have another review in February to examine, in more detail, developments during the agricultural season and to discuss the additional measures that would be necessary in 1983/84. In the meetings with the authorities, the indicative ceilings for 1984 would be examined and would be retained unless the situation required new measures. Those ceilings would enable the staff to have a benchmark from which to introduce additional measures if necessary.

With regard to export assumptions for 1984, the staff representative commented that slow growth in external market demand would result in volume growth of about 2-3 percent for many agricultural and mineral products. A large response was expected in the manufacturing sector, where marketing potential existed in some neighboring countries. Zimbabwe should try to develop new markets abroad, but meanwhile the staff was encouraged by developments in manufactured export orders that had been observed toward the end of 1983.

There were four categories of goods subject to price control, the staff representative said: 6 items had fixed prices; price increases for 18 other items had to be approved by the Minister; price increases for 14 items could be varied automatically following the Minister's approval of a pricing formula; other items were automatically adjusted by a previously agreed fixed markup. The authorities' actions had been impressive: price increases in the first category, which included many basic foodstuffs, had amounted to 50 percent at the end of 1982, followed by a large increase in September 1983; price increases had also been approved for items in the second category in 1983. The authorities had explicitly stated that one of the guidelines for determining price increases in the future would be that marketing boards should operate without operating losses; the staff would monitor that policy closely. A second guideline would be that any exchange rate change would trigger a corresponding adjustment in the prices of items subject to control; that policy would also be monitored. In practice, the government unit that received prices was small and exercised little price control; nevertheless, the staff would urge the authorities to remove the last two categories of commodities from the list of goods subject to price control.

While several parastatals in other countries had recourse to the budget for assistance, they did not in Zimbabwe, the staff representative remarked. The electricity company, for example, was self-sufficient, and Directors would have noticed that electricity prices had increased by 22-49 percent in October 1982 and by a further 60 percent in July 1983; that parastatal's policy was to pass all costs on to consumers in a manner that did not require government assistance. The marketing board losses of Z$165 million during the past year, which were not covered in the budget, occurred when the public sector deficit was declining from 10.5 to 7.2 percent of GDP. Although a monetary program had not been initiated in that operation, it was desirable not to have the debt on the books of the marketing boards; for that reason, the staff would require that the losses should be covered by the budget during the coming fiscal year.

The medium-term scenario was an area of concern, the staff representative from the African Department commented, and would be discussed with the authorities during the next mission. A number of criteria would guide the discussion: first, the staff would recommend a shift in emphasis from the nontraded goods sector to the traded goods sector, particularly exports in areas where the import content was not very high. Large pockets in the agricultural sector had traditionally performed well, and recent problems had been due to the drought of the past two years. The staff would also encourage measures to moderate the cost of production, limit domestic demand, and develop markets abroad. In many cases, the problem in Zimbabwe lay not in producing the goods but in finding the markets and buyers for them. Given the limits of low growth in potential partner countries, the staff had encouraged the use of trade fairs, promotional tours, and commercial activities in diverse embassies. Markets in the immediate area were limited by the financial problems of many of the countries; it would be advantageous to pursue potential markets further afield.

The staff representative from the Exchange and Trade Relations Department, commenting on the question whether the two reviews should have been combined, explained that a review in February was needed for the reasons given by the representative of the African Department. Therefore, combining the two reviews would have delayed the present discussion until February or March, which would not have been desirable. Regarding the significance of the September data on performance criteria, at a substantive level the discussion between the staff and the authorities had started in July, and the numbers discussed with the authorities for September had been effective guideposts for the policies that they had implemented during the early months of the fiscal year. At a technical level, with regard to the data's meaning and the linkage to the purchases under the stand-by arrangement, the purchase discussed at the present Board meeting would actually be authorized by the decision taken at the present meeting, not validated by the observance of performance criteria for a past date.

The staff representative from the Research Department informed the Board that the International Sugar Organization had notified the Fund that Zimbabwe had accumulated an additional amount of stocks in compliance with its obligation to accumulate such stocks under the terms of the International Sugar Agreement. The stocks had been accumulated in October 1983, and it appeared that the conditions for an additional request had been met, but to date the authorities had not expressed interest in making one.

Mr. Sangare thanked Directors for their interest in Zimbabwe's economy; he noted from their comments a recognition of the effort being made by the authorities of Zimbabwe to meet the performance criteria, including fiscal policy, which was considered a step in the right direction. Directors had welcomed the flexible exchange rate policy and the present competitive exchange rate, positive lending rates, and the restrained credit policy. Despite those commendable efforts, the balance of payments prospects in the medium term represented a serious problem that continued to plague the economy of Zimbabwe; it would be necessary to work out appropriate and far-reaching solutions.

Continued efforts would be needed to strengthen the economy, Mr. Sangare continued. The Zimbabwean authorities agreed that the medium-term balance of payments position would remain weak; hence, they hoped for a successor to the present arrangement. However, as the underlying problems were deep rooted and not only financial but structural in nature, his authorities believed that only an extended arrangement would be appropriate to address them. Those structural problems were aggravated by the fact that Zimbabwe was a landlocked country. The two successive years of drought had constrained agriculture, demonstrating the need to take urgent action to diversify production. With regard to manufacturing, although exports had recently showed some improvement as a result of the exchange rate, the response had proved to be limited.

The World Bank was expected to provide financing for several projects that would help to correct some of the structural deficiencies, Mr. Sangare noted. The cooperation of the Fund with the Zimbabwean authorities and the World Bank would be a positive step in developing a program that could be supported under an extended arrangement. He was pleased that Mr. Wicks would not preclude that possibility when the present stand-by arrangement had been completed satisfactorily. He urged the Board to join in that support, especially in view of the strong commitment of the authorities to remain current with their obligations under the present program.

The Acting Chairman made the following summing up:

Executive Directors were for the most part in agreement with the views expressed in the staff appraisal. They observed that Zimbabwe's economy had been in a very difficult situation the past two years, with little or no economic growth, a high rate of inflation, and a weak balance of payments. Directors agreed with the staff that the severe drought and weak international demand for Zimbabwe's minerals were among the factors responsible for these adverse economic adjustments. Directors praised the authorities for their willingness to take decisive action to address these problems. They specifically referred to the significant measures taken in the exchange rate, fiscal, prices, and incomes policy areas.

Directors also commended the authorities for the substantial action taken in the area of public finances, despite the present unfavorable economic environment. They noted that the next program review will provide an opportunity for assessing the fiscal developments in the first half of the year and for taking additional measures, if necessary, to ensure meeting the fiscal target. Directors emphasized that a continuing reduction in the fiscal deficit was needed over the next few years. In this context, Directors stressed the need for further expenditure restraint. Directors were concerned in this context about the financial positions of parastatals and about the amount of continuing price subsidies. Directors also noted the efforts made by the Zimbabwean authorities to increase the proportion of budgetary resources allocated to investment.

Directors expressed concern about the low rate of disbursement of pledged concessionary assistance and urged the authorities to take steps to accelerate the rate of disbursement of such assistance.

Directors urged the authorities to increase interest rates on deposits and stressed the need for greater flexibility in price policy, including producer prices for agricultural products.

Directors expressed considerable concern at Zimbabwe's medium-term balance of payments outlook, which contains major elements of structural weakness. It was suggested that external adjustment goals should be more ambitious. In view of the already high debt service ratio, which is projected to continue rising for some years, Directors agreed that recourse to nonconcessionary foreign borrowing should be severely limited. They considered that strong emphasis should be placed, in particular, on achieving a maximum expansion in exports. In this connection, Directors welcomed Zimbabwe's adoption of a more flexible exchange rate policy and hoped that this strategy would be pursued further.

It is expected that the next Article IV consultation with Zimbabwe will be held on the standard 12-month cycle.

The Executive Board then took the following decisions:

Decision Concluding 1983 Article XIV Consultation

1. The Fund takes this decision in concluding the 1983 Article XIV consultation with Zimbabwe, in the light of the 1983 Article IV consultation with Zimbabwe conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. Zimbabwe continues to maintain restrictions on payments and transfers for current international transactions as described in SM/83/247. The Fund encourages the authorities to take measures to reduce these restrictions as soon as possible.

Decision No. 7596-(84/3), adopted
January 9, 1984

Review Under Stand-By Arrangement

1. Zimbabwe has consulted with the Fund in accordance with paragraph 4 of the stand-by arrangement for Zimbabwe (EBS/83/44, Sup. 1, 3/24/83) in order to reach understandings subject to which further purchases may be made by Zimbabwe under the stand-by arrangement.

2. The letter from the Minister of Finance, Economic Planning and Development of September 30, 1983 shall be annexed to the stand-by arrangement for Zimbabwe, and the letter of January 24, 1983, attached to the stand-by arrangement, shall be read as supplemented by the letter of September 30, 1983.

3. The Fund decides, in view of the circumstances described in EBS/83/264 and Supplement 1, that Zimbabwe may proceed to make purchases under the stand-by arrangement, provided that such purchases are made before January 17, 1984 and that cumulative purchases under the arrangement shall not exceed the equivalent of SDR 175 million until further review by the Fund.

4. In accordance with the letter of September 30, 1983, the understandings referred to in paragraph 4(b) of the stand-by arrangement for Zimbabwe relating to the limits on the total domestic credit of the banking system and on net bank credit to the Government for end-December 1983 shall be those specified in paragraph 12 of the memorandum annexed to the letter.

Decision No. 7597-(84/3), adopted
January 9, 1983

Purchase Transaction - Buffer Stock Financing Facility - International Sugar Agreement

1. The Fund has received a request by the Government of Zimbabwe for a purchase of SDR 2.099 million under the Decision on Buffer Stock Financing Facility: The Problem of Stabilization of Prices of Primary Products (Decision No. 2772-(69/47), adopted June 25, 1969, as amended by Decision No. 4913-(75/207), adopted December 24, 1975) and the Decision on Buffer Stock Financing Facility: 1977 International Sugar Agreement (Decision No. 5597-(77/171), adopted December 16, 1977).

2. The Fund notes the representations of Zimbabwe and approves the purchase in accordance with the request.

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

Decision No. 7598-(84/3), adopted
January 9, 1984

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/84/2 (1/3/84) and EBM/84/3 (1/9/84).

4. POLICY ON ENLARGED ACCESS

Period and Annual Review

(a) The Fund may approve a stand-by or extended arrangement that provides for enlarged access under Decision No. 6783-(81/40) on the Policy on Enlarged Access until the end of 1984, provided that the Fund may extend this period.

(b) The Fund will review Decision No. 6783-(81/40) not later than December 31, 1984, and annually thereafter as long as the Decision remains in effect, in order to consider the future of the Policy on Enlarged Access in the light of all relevant factors, including the magnitude of members' payments problems and developments in the Fund's liquidity.

Decision No. 7599-(84/3), adopted
January 6, 1984

Guidelines on Access Limits

(a) Access by members to the Fund's general resources under Decision No. 6783-(81/40) on the Policy on Enlarged Access during the period ending on December 31, 1984 shall be subject to annual limits of 102 or 125 percent of quota, three-year limits of 306 or 375 percent of quota, and cumulative limits of 408 or 500 percent of quota net of scheduled repurchases, depending on the seriousness of the member's balance of payments needs and the strength of its adjustment effort. The annual and triennial access limits shall not be regarded as targets. Within these limits, the amounts of access in individual cases will vary according to the circumstances of the member in accordance with criteria established by the Executive Board. The Fund may approve stand-by or extended arrangements that provide for amounts in excess of these access limits in exceptional circumstances.

(b) The guidelines will be reviewed before the end of 1984 at the time of the annual review of the Decision on the Policy on Enlarged Access.

Decision No. 7600-(84/3), adopted
January 6, 1984

Use of Ordinary and Borrowed Resources

The Fund, having reviewed the proportions of ordinary and borrowed resources to be used under a stand-by or extended arrangement approved under Decision No. 6783-(81/40) on the Policy on Enlarged Access, decides that:

1. The proportions after the effective date of this decision will be as follows:

(a) Under a stand-by arrangement, purchases will be made with ordinary and borrowed resources in the ratio of 2 to 1 in the first credit tranche, and 1 to 1 in the next three credit tranches. Thereafter, purchases will be made with borrowed resources only.

(b) Under an extended arrangement, purchases will be made with ordinary and borrowed resources in the ratio of 1 to 1 until the outstanding use of the upper credit tranches and the Extended Fund Facility equals 140 percent of quota. Thereafter, purchases will be made with borrowed resources only.

2. In accordance with subparagraph 8(d) of Decision No. 6783-(81/40), the proportions in (1) above shall apply to amounts that may be purchased under existing arrangements after the effective date of this decision on the basis of the member's quota at the time the arrangement for the member was approved.

Decision No. 7601-(84/3), adopted
January 6, 1984

Access Limits Under Special Facilities

(a) In paragraph 3 of Decision No. 6224-(79/135) "100 percent" shall be changed to "83 percent."

(b) The following changes shall be made in paragraphs 9 and 14(a) of Decision No. 6860-(81/81):

(i) "125 percent" shall be changed to "105 percent"; and

(ii) "100 percent" shall be changed to "83 percent."

(c) In paragraph 2 of Decision No. 2772-(69/47), as amended, "50 percent" shall be changed to "45 percent."

(d) The new percentages of quota under (a), (b), and (c) above shall be reviewed not later than December 31, 1984 and annually thereafter in the light of all relevant factors, including the magnitude of members' payments problems and developments in the Fund's liquidity.

Decision No. 7602-(84/3), adopted
January 6, 1984

5. RATE OF REMUNERATION

Rule I-10 shall read as follows:

(a) The rate of remuneration shall be equal to 85 percent of the rate of interest on holdings of SDRs under Rule T-1 (hereafter referred to as the "SDR interest rate"). The relationship of the rate of remuneration to the SDR interest rate will be referred to as the "remuneration coefficient."

(b) Beginning April 30, 1984, the remuneration coefficient during each quarter shall be at the level determined under (1), (2), (3), and (4) below, but no higher than permitted by Article V, Section 9(a):

(1) During the period May 1, 1984 to April 30, 1987, the remuneration coefficient shall be the higher of (i) or (ii) below:

(i) The remuneration coefficient in effect on January 1, 1984 increased by 3.33 percentage points in each of the three financial years beginning May 1, 1984, May 1, 1985, and May 1, 1986;

(ii) The remuneration coefficient in effect on January 1, 1984, increased or decreased on the first day of each quarter by 1 percentage point for each 1/6 of 1 percentage point that the SDR interest rate on the day before the beginning of the quarter is below or above the SDR interest rate in effect on April 30, 1984, provided that the remuneration coefficient in any quarter in each of these three financial years shall not be more than 2.5 percentage points above the amount of the coefficient for that year as determined under (i) above.

(2) Following the adjustment in the remuneration coefficient on May 1, 1986, the rate of remuneration shall be reviewed before May 1, 1987. This review shall be conducted in the light of all the relevant considerations, including, in particular, the SDR interest rate and the rate of charge.

(3) Beginning May 1, 1987, the remuneration coefficient shall be the higher of (i) or (ii) below:

(i) The remuneration coefficient existing at the end of the preceding financial year;

(ii) A remuneration coefficient of 95 percent, increased or decreased on the first day of each quarter by 1 percentage point for each 1/6 of 1 percentage point that the SDR interest rate on the day before the beginning of a quarter is below or above the SDR interest rate on April 30, 1987, provided that the remuneration coefficient in any quarter of a financial year shall not be more than 2.5 percentage points above the level at the end of the preceding year.

(4) The rate of remuneration, while less than 100 percent of the SDR interest rate, shall be rounded to the nearest two decimal places.

(c) The operation of (b) above shall be reviewed on the occasion of the reviews of the rate of charge under Rule I-6(4) and the SDR interest rate under Rule T-1(d).

(d) If the rate of charge on holdings specified in Rule I-6(4) should exceed the SDR interest rate, the Executive Board shall review the remuneration coefficient, and, in particular, will consider whether the remuneration coefficient should be set, within the range in Article V, Section 9(a), at such a level as would permit the rate rate of charge to be set under Rule I-6(4)(a) or (b) at the same level as the SDR interest rate referred to above and still meet the target amount of net income for the financial year.

Decision No. 7603-(84/3), adopted
January 6, 1984

6. INDONESIA - TECHNICAL ASSISTANCE

In response to a request by Indonesia for technical assistance, the Executive Board approves the proposal set forth in EBD/83/340 (12/29/83).

Adopted January 6, 1984

7. APPROVAL OF MINUTES

The minutes of Executive Board Meetings 83/102 and 83/103 are approved. (EBD/83/336, 12/28/83)

Adopted January 4, 1984

8. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors as set forth in EBAP/84/1 (1/4/84) and EBAP/84/3 (1/5/84) is approved.

APPROVED: May 22, 1984

LEO VAN HOUTVEN
Secretary