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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 84/4

3:00 p.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
	N. U. Haque, Temporary
T. Hirao	T. Yamashita
	I. R. Panday, Temporary
	D. I. S. Shaw, Temporary
	J. R. N. Almeida, Temporary
	W. Moerke, Temporary
	C. P. Caranicas
	A. S. Jayawardena
	E. M. Ainley, Temporary
	M. Eran, Temporary
A. R. G. Prowse	K. G. Morrell
G. Salehkhou	
	M. Camara, Temporary
M. A. Senior	
	A. K. Juusela, Temporary
	C. M. Hull, Temporary
Zhang Z.	

A. Wright, Acting Secretary
S. J. Fennell, Assistant

Also Present

B. Legarda, Consultant. Asian Department: H. C. Kim, R. H. Nord, T. Yanagita. Exchange and Trade Relations Department: D. K. Palmer, Associate Director; C. Atkinson. External Relations Department: Z. Zhang. Legal Department: Ph. Lachman. Advisors to Executive Directors: H.-S. Lee, Y. Okubo. Assistants to Executive Directors: H. Alaoui-Abdallaoui, I. Fridriksson, V. Govindarajan, D. Hammann, M. J. Kooymans, M. Rasyid, Shao Z.

1. SOLOMON ISLANDS - 1983 ARTICLE IV CONSULTATION, REVIEW UNDER STAND-BY ARRANGEMENT AND MODIFICATIONS OF PERFORMANCE CRITERIA

The Executive Directors considered the staff report for the 1983 Article IV consultation with Solomon Islands, together with a review under the stand-by arrangement and a request for modifications of performance criteria (EBS/83/261, 12/2/83; and Cor. 1, 1/4/84). They also had before them a report on recent economic developments in Solomon Islands (SM/83/251, 12/14/83; and Cor. 1, 1/4/84).

Mr. Prowse stated that both he and the Solomon Islands authorities considered that the staff report was excellent in terms of analysis and of understanding of the economy. Solomon Islands had a small tropical island economy, some characteristics of which--summarized in Mr. Legarda's recent paper on small tropical island countries (EBD/83/325, 12/19/83)--were relevant to consideration of the authorities' macroeconomic policy. Solomon Islands had a small domestic market and no export base. The economy was sensitive to external conditions and, therefore, to volatility in its terms of trade, which had declined by 40 percent in 1981 and 1982. The problems of such a relatively newly independent island economy stemmed from the external situation. Nevertheless, Solomon Islands had come through a difficult period in reasonable shape as a result of good management by the authorities and sound policy, reflecting in part the advice of the Fund staff.

From pages 38 and 39 of Mr. Legarda's paper (EBD/83/325) it was clear that the Solomon Islands authorities had made good use of the islands' facilities and resources, Mr. Prowse observed. The external situation, and not the authorities' policies, had led to the breach of the credit ceiling, partly because aid donors had changed the arrangements for disbursing aid and concessional assistance; instead of disbursing resources in advance of expenditure, the aid donors were disbursing after expenditure. The change in disbursement arrangements would obviously create ongoing problems, and when considering the request for a waiver, that background should be borne in mind. The staff had suggested that the aid donors should maintain revolving funds with the Central Bank.

In spite of the problems of aid disbursement, concessional assistance was vital for economic development in Solomon Islands, Mr. Prowse went on. Official aid and grants had declined by about one third between 1970 and 1982, but the authorities remained committed to maintaining a current account surplus in the budget, despite a budget deficit in the previous year. The importance of external assistance in the economy should be kept in mind when considering macroeconomic policy--for example, when determining what could be a tolerable deficit in the budget and balance of payments. The staff had suggested that a current account deficit of about 4 percent of GDP might be viable in the medium term. Substantial reductions in the budget and external current account deficits had been made in the period since independence; the external policy of such a small economy was exemplary. Of course, the debt service ratio was low, reflecting in part the favorable terms of foreign assistance.

Commenting on a policy area for which responsibility could be taken more directly by the authorities, the exchange rate had been well managed, Mr. Prowse pointed out. Indeed, there had been a significant decline in the real effective rate against the basket of currencies. The effectiveness of the exchange rate policy could be seen in the growth of reserves from SDR 18 million, or 2.5 months' imports, in 1981 to SDR 41.2 million, or 5 months' imports, by 1983. Reserves equivalent to 5 months of imports was not excessive in an economy that was so subject to volatile movements in the external environment. However, it was a strong enough position for the authorities to indicate that they did not intend at the present stage to make further drawings under the stand-by arrangement.

In his budget speech in November 1983, the Finance Minister of Solomon Islands had dealt with wages policy, Mr. Prowse went on. He had said that "in 1984, pay increases will have to be held below the change in retail prices. Thus they might be in the range of 5-7 percent, but no provision is being made in the budget for wages and salary increases. If and when such increases are agreed, they will have to be financed from additional revenues; and if no additional revenue is available, then any increase of expenses for wages and salaries must be financed from existing allocations by means of an across-the-board general reservation of the appropriations," as indeed had been done in 1983.

On the monetary side, it was most reassuring that interest rates were positive in real terms and that the Central Bank was well administered, Mr. Prowse stated. On the matter of interest rates, the staff made an interesting observation in their report that "there has as yet been no clear sign indicating the impact of the interest rate adjustments on the growth of domestic financial savings." The Executive Board had had discussions over the past three years on that long-standing issue, which had not yet been resolved. It would be interesting on the occasion of the next Article IV consultation with Solomon Islands to see whether empirical results would shed more light on the issue. In his view, the development of the financial infrastructure was more important than the particular level of interest rates.

In the previous year, policy objectives had been sound, policies had been well implemented, and the performance of the economy had been good, Mr. Prowse considered. Table 3 of EBS/83/261 illustrated the authorities' achievements and the objectives for 1984. In all the key variables--the GDP deflator, overall budget deficit, and current account deficit--there had been major improvements, as was evident from the revised estimates. The objectives for 1984 were to further reduce inflation and the fiscal deficit, to maintain a flexible exchange rate and positive real interest rates, and to limit credit growth; the overall objective was to bring about a recovery in investment and economic growth. Perhaps the one disappointment in 1983 had been that the suggested recovery in investment had not materialized. For 1984, however, the authorities were hoping for a real growth rate of about 5 percent.

Addressing the decision to be taken, Mr. Prowse commented that in a formal sense the waiver was retrospective; but it was merely the outcome of mechanical and programming problems, none of which could be attributed to the authorities. The breach of the credit ceiling for the public sector could be justified in the present case because of the particular causes. Finally, the authorities had no intention at present of making further purchases under the stand-by arrangement because of the strong external position and progress of the economy. They did, however, have every intention of implementing the program and meeting the performance criteria; indeed, the action of Solomon Islands in the present case was something of a model.

The authorities were satisfied with the proposed timetable for the next Article IV consultation, Mr. Prowse concluded.

Mr. Hirao indicated his agreement with the staff appraisal and the proposed decision. The authorities should be commended for taking important adjustment measures under the program. As was typical in small economies, Solomon Islands had been affected by external developments in which the terms of trade had deteriorated by as much as 40 percent in the past three years. Nevertheless, considerable progress had been made in many areas. The current account deficit had been lower than projected and the overall balance was estimated to be in surplus for 1983. Inflation had also been reduced markedly during the course of the year.

The ceiling on net credit to the Government had been exceeded by a considerable margin in September, Mr. Hirao noted. The staff had attributed that breach to an overrun in current expenditures, to problems associated with the changeover of the management of external aid flows, and to a shift in financing from foreign to domestic sources. Nevertheless, the performance criterion for total domestic credit had been met, and measures to reduce government borrowing from the banking system had been taken. The authorities intended to strengthen fiscal discipline in 1984. In view of the circumstances, he could go along with the modifications of the performance criteria.

In spite of the progress being made, there remained some areas of concern, particularly with respect to public finances, Mr. Hirao considered. The overall budget deficit would still remain high in 1984, although he noted Mr. Prowse's remarks that efforts had been made to reduce it. He was especially concerned about the change in composition of spending; current expenditures had been higher than programmed and capital expenditures were expected to fall. That change seemed to reflect potential problems in coordinating and monitoring project implementation, rather than efforts to control expenditure. The authorities were aware that there might be some room for tightening control over current expenditures and improving the implementation of capital projects, and he hoped that with the introduction of various measures, including revenue efforts, the Government would be able to achieve a current budget surplus equivalent to about 1 percent of GDP.

On the external side, the medium-term analysis of the balance of payments was informative, Mr. Hirao stated. The debt service burden was expected to remain modest over the medium term, given the concessional aid inflows. He hoped that the authorities would continue to pursue a prudent debt management policy, as they might have to borrow at higher interest rates in the future. The authorities' intention to continue pursuing a flexible exchange rate policy was welcome, as was the continued adherence to a liberal trade system. Finally, he commended the authorities' intention to refrain from using additional Fund resources under the stand-by arrangement in light of the favorable balance of payments prospects and sound reserve position. He saw no difficulty in holding the next Article IV consultation in March-April 1985.

Mr. Shaw said that he supported the staff appraisal and the authorities' request for modification of the performance criteria on net credit to the Government. The authorities had effectively implemented the adjustment program on which they had embarked six months previously; the economy had been successfully turned around.

The authorities were meeting the basic objectives of the program under the stand-by arrangement, Mr. Shaw considered. The modification of the ceiling on net credit to the Government was justified because circumstances had been mainly beyond the control of the authorities. The shortfall in aid financing had required an increase in domestic financing and, hence, an increase in credit to the Government. Although the overall fiscal deficit was within the program target, there had been some slippage on current expenditures, and the authorities had compensated for that slippage by reducing capital expenditures.

With respect to the shortfall in aid financing, the problem of mobilizing external financing had been evident at the time of the Executive Board discussion of the stand-by arrangement in June 1983, Mr. Shaw recalled. At that meeting several Directors, including himself, had welcomed the re-creation of the Central Planning Office as an important step in alleviating the problem. He urged the authorities to put increasing emphasis on improving their administrative capabilities in that respect. He was concerned that the Central Planning Office had not yet provided "a significant improvement in coordination and monitoring of project implementation" (page 9, EBS/83/261). Nevertheless, his constituency was well aware that administration was a problem in small tropical island economies. Had any technical assistance been provided by such financial institutions as the World Bank and Asian Development Bank, or even bilateral donors?

In its letter of intent, the Government had requested that bilateral donors set up revolving funds in Solomon Islands to help speed aid disbursements, Mr. Shaw noted. That method of disbursing aid had been used in previous years, but the problems had emerged after the donors had stopped using that method.

The staff paper was not explicit regarding the views of the World Bank on the investment program of Solomon Islands, Mr. Shaw remarked. Could the staff indicate whether missions by the World Bank were envisaged in the future and whether there had been any recent missions that had reviewed the investment program?

He commended the authorities' decision to treat the arrangement on a truly stand-by basis, Mr. Shaw went on. The authorities did not intend to draw the balance of the amount available under the program, and he was therefore not as concerned as he might have been about the retrospective nature of the modification of performance criteria. He understood that there had been administrative reasons for delaying until 1984 the present review and the request for modification. In all probability the resources of the Fund were more expensive than the resources being made available by aid donors.

As for the Article IV consultation, it was encouraging to note that the fiscal deficit was expected to meet the program targets of about 10 percent of GDP in 1983, and that the authorities were expected to reduce the deficit further to 7.9 percent of GDP in 1984, Mr. Shaw considered. While that deficit was high, it seemed to be financeable given the foreign assistance available to Solomon Islands. The commitment of the authorities to maintain a flexible exchange rate policy and thereby prevent erosion in the competitiveness of exports was commendable. The authorities should also ensure that wages did not decrease the competitiveness of the export sector, and in that respect he was somewhat worried about the wage increases in 1983, which could offset the competitiveness of the export sector if they resulted in higher factor costs. The 9 percent increase for nonestablished workers and 10 percent increase for teachers were above the estimates for the increase in the 1983 consumer price index. While there might be some justification for catch-up provisions, he urged the authorities to monitor the situation closely when looking at wage settlements for 1984.

Strengthening the administrative capacity to manage external aid was crucial, as the staff of the Fiscal Affairs Department had recommended in its review, Mr. Shaw remarked. Increased cooperation and coordination with donors, both multilateral and bilateral, and technical assistance from both the World Bank and the Asian Development Bank would help in that respect. Had either the World Bank or the Asian Development Bank investigated the possibility of directing aid to energy projects?

He commended the authorities for reducing inflation to 8 percent in 1983 and to a projected 6 percent in 1984, Mr. Shaw continued. The policy of maintaining positive real interest rates was appropriate, although there was as yet no evidence that such a policy would provide sufficient incentives for savings.

He assumed from the staff papers that Solomon Islands would be on an 18-month cycle for future Article IV consultations, Mr. Shaw said. While he agreed with an 18-month cycle for Solomon Islands, he did not go along with the reason put forward by the staff on page 22 of EBS/83/261 relating to the general elections. If Article IV consultations were dependent upon elections, consultations with some members might never take place. The surveillance function of the Fund should not depend on the election process in a member country. In any case, Article IV consultations reviewed the performance of the economy since the previous consultation and made general policy recommendations to the authorities that could be useful to either a continuing or a new administration.

Mr. Salehkhou indicated his broad concurrence with the staff appraisal and his support for the proposed decision. The overall performance of the economy since the adoption of the current stand-by arrangement had been satisfactory and the authorities' decision to continue with and strengthen the adjustment policies despite an improvement in their balance of payments position was commendable. The economy had benefited from favorable external developments, including a welcome improvement in the terms of trade that had reversed a deteriorating trend of several years. However, the achievement of the 1983 program objectives for the current account of the balance of payments, for inflation, and for real economic growth was to a large extent due to the successful implementation of the measures and policies under the stand-by arrangement. Those policies included, in particular, a substantial depreciation of the currency and a flexible exchange rate policy, which had greatly improved the country's export competitiveness.

It was encouraging that the authorities did not intend to make further purchases under the program, Mr. Salehkhou went on. Could the staff or Mr. Prowse indicate whether there were any plans for early repurchases in view of the improvement in the balance of payments?

Although the authorities should be commended for the progress achieved thus far, he noted that performance in the fiscal area was less than satisfactory, Mr. Salehkhou continued. A projected current account budget surplus had not materialized because current expenditures had not been contained and government revenues had been less than expected. Similarly, the implementation rate of development projects was not likely to be increased to 65 percent, despite the re-establishment of the Central Planning Office in early 1983 to coordinate and monitor project implementation. Furthermore, the ceiling on domestic borrowing by the Government had been breached in the early months of the program, and total domestic credit from the banking system would remain within the ceiling only because of more sluggish economic activity than projected. While he could go along with the authorities' request for modifications of performance criteria, more effort on their part was needed if the new performance criteria were to be met, particularly with respect to the control of current expenditures and implementation of development projects.

Balance of payments developments in 1983 seemed to be more favorable than envisaged under the program, although the improvement in the current account deficit was partially related to a significantly lower than expected level of imports of investment goods and to below-target economic activity, Mr. Salehkhou commented. While he could understand the authorities' and the staff's optimism regarding the sustainability of the unusually large current account deficit in view of the high level of foreign grants and concessional assistance, some caution would be advisable as foreign assistance was subject to fluctuations that could seriously affect the domestic and external position of Solomon Islands. It would therefore seem desirable to strengthen further the level of external reserves.

Mr. Ainley said that he could agree with the main points in the staff appraisal and that he could support the proposed decision. In general, performance under the 1983 program had been good. But there had been a few disappointing developments: the strong recovery in investment activity envisaged under the program had not materialized, current expenditures had risen markedly, and domestic bank borrowing by the Government had exceeded the program limits. The additional measures recently taken by the authorities to keep the program on track were therefore welcome. The move to control current expenditures was particularly appropriate, and the continuing efforts to stimulate private investment through fiscal and other incentives were commendable. As Mr. Hirao had said, it would be important to speed up the implementation of capital projects. The new arrangements to improve the management of foreign aid flows should help in that regard. The measures introduced seemed well designed to reduce the fiscal deficit and limit government borrowing from the banking system. He could therefore support the proposed modifications in the credit ceilings for the last quarter of 1983. He noted that the authorities were asking for a reduction in the overall credit ceiling, which was a rare occurrence in Fund programs.

He could also support the proposed monetary program for the first half of 1984, and he hoped that the authorities would continue to develop the financial infrastructure that should help to mobilize domestic savings, Mr. Ainley remarked. The authorities should be commended for pressing ahead with adjustment, even though they did not intend to make further purchases under the stand-by arrangement. That intention demonstrated that the authorities were extremely serious about adjustment, and it augured well for the economy's prospects over the medium term. Solomon Islands was a small island economy with a narrow export base, and despite its successful diversification efforts, the country remained highly vulnerable to external developments. By continuing to adjust even when external conditions were improving, the authorities were providing some important room for maneuver when or if they became less favorable. Finally, he looked forward to the forthcoming discussion of Mr. Legarda's paper on small tropical island countries.

Mr. Williams indicated his support for the proposed decision. Indeed, there was much that he liked in the program. It was particularly encouraging that the authorities intended to keep the existing arrangement in place, but on a truly stand-by basis, for the remainder of the program period. That approach seemed to be a pragmatic way for the Fund to assist the Solomon Islands authorities in the pursuit of their adjustment and development objectives.

Since August 1982 the authorities had pursued an appropriately flexible exchange rate policy aimed at preserving the profitability of the islands' exports and the competitive position, Mr. Williams observed. He encouraged them to continue pursuing a flexible policy in the future and welcomed the fact that the Central Bank would maintain key interest rates positive in real terms.

His only area of concern was with respect to fiscal policy, but even there he was encouraged by the authorities' intention to implement the recommendations of the recent Fiscal Affairs Department technical assistance mission, Mr. Williams said. He urged the authorities to resolutely adopt and implement such measures as might be necessary to achieve the fiscal element of their adjustment program in 1984.

Finally, the external current account deficit was considered sustainable by the authorities, Mr. Williams remarked, and the financing mix to support that deficit seemed appropriate. The overall debt service burden was clearly manageable and obligations to the Fund seemed to be within acceptable limits.

Mr. Hull said that he agreed with the remarks made by most of the previous speakers, particularly on the importance of treating the program on a truly stand-by basis. He endorsed the staff appraisal and supported the proposed decision. In the medium term, Solomon Islands needed development assistance, not balance of payments support.

The staff representative from the Asian Department commented that the Solomon Islands authorities shared the concern expressed by some Directors about fiscal developments in 1983 and possible prospects for 1984. They fully recognized the difficulties encountered in restraining current expenditures in 1983, and they intended to improve their performance in the financing and implementation of capital expenditures in the present year, as was clearly indicated in the letter of intent. In 1983 the authorities had introduced a number of measures to improve administration of capital expenditures; they had restored the Central Planning Office and had hired more expatriates. Although those measures had not immediately improved the implementation of capital projects, the authorities expected that some improvements would be evident in the coming year. The authorities had also asked a number of international organizations for technical assistance. In August 1983, staff from the Fiscal Affairs Department had visited the country to examine the financial operations of the Government. The staff had made three major recommendations to the authorities, including the strengthening of administrative capabilities to manage external aid and the timely monitoring of fiscal developments.

With regard to World Bank activities in Solomon Islands, in October 1983 a basic economic survey mission had visited the country, the staff representative said. The World Bank staff had used the answers to the questionnaire carried out by the Fund mission, and the basic economic report would be completed soon. However, he did not know to what extent the mission had investigated the investment priorities of the Government.

The authorities were aware of the importance of restraining wages in 1984, in view of their experience in the previous year, the staff representative went on. They intended to limit the rise in wages and salaries to roughly the rate of inflation expected for 1984.

Before making any early repurchases, the authorities wished to see how the external situation developed, the staff representative from the Asian Department remarked. The short-term and medium-term balance of payments prospects appeared relatively favorable at present, but projections were subject to large margins of error. Furthermore, the authorities had a policy of maintaining their reserves at a level roughly equivalent to four-six months of imports of goods and services; reserves were currently about five months of imports. In conclusion, at the present juncture there was no clear indication that the authorities would make any early repurchases.

The Associate Director of the Exchange and Trade Relations Department agreed with Mr. Shaw that the wording in the last paragraph of page 22 of EBS/83/261 with respect to the next consultation was awkward. The Article IV consultation with Solomon Islands could be delayed beyond a year simply because, for the immediate future, balance of payments prospects were good. However, if there were a sudden and unexpected serious deterioration in the external situation, the management and staff could press for an earlier consultation.

Responding to a question by the Acting Chairman, the Associate Director explained that the staff would be visiting Solomon Islands in March-April 1985.

The staff representative from the Asian Department stated that the Solomon Islands Parliament would be dissolved in November 1984. At that time the Government would submit the budget for the following year. Elections would be held within 90 days of the dissolution of Parliament, after which a new government would be formed. The authorities considered that a staff visit on the 12-month cycle would be inappropriate for discussing meaningful budget policy for 1985.

The Acting Chairman commented that although the staff's reason was appropriate in the case of Solomon Islands, Mr. Shaw was right in cautioning the staff not to use elections as a reason to delay Article IV consultations.

Mr. Shaw said that he was satisfied with the staff's answer. With respect to technical assistance from development banks, did the Asian Development Bank or the World Bank have facilities to provide technical assistance for the management of projects, and project implementation and monitoring in the same way as the Fund? A number of small island economies in his constituency worked closely with both the Caribbean Development Bank and the Inter-American Development Bank in areas of technical assistance.

The Acting Chairman indicated that he did not have any specific knowledge with regard to Solomon Islands, but it was his impression that a great deal of the technical assistance of the World Bank and perhaps other development banks was provided under contract in connection with lending for substantive projects.

Mr. Jayawardena noted that it appeared to be the staff position that a current account deficit of about 12-14 percent of GDP was sustainable if it was matched by aid inflows. He agreed with the staff's approach, but he was concerned that the principle should be applied evenhandedly to all countries. In three earlier cases when the staff had been critical of large current account deficits, he had invited attention to matching aid and grant inflows; but, on those occasions, he had not heard a chorus of approval, as he had today.

The Acting Chairman commented that it was difficult to generalize, and that each case should be considered separately. The critical factor in the case of Solomon Islands was that the internal grants and concessional loans to the Government were expected to be sustained in the medium term.

The Associate Director of the Exchange and Trade Relations Department agreed with the Acting Chairman. Solomon Islands had a special aid relationship with a wide range of donors and institutions, and the total grants allowed were projected to be forthcoming for a number of years. The staff looked at a country's situation on its individual merits.

Mr. Prowse commented that where assistance was available on a concessional and sufficiently stable basis, a country that was short of resources and capital should make use of that sort of financing. In fact, Solomon Islands had the problem of absorbing available financing; the amount of resources could be greater if the capacity to utilize them properly were greater. Nevertheless, the authorities recognized the importance of using such resources efficiently.

On the matter of the timing of the next Article IV consultation, although informally adopted guidelines did specifically mention that elections should not be a reason for deferring consultations, it was sensible to recognize that the capacity of a country to deal with a staff visit for a consultation was limited by the approach of an election and the drawing up of an annual budget, Mr. Prowse went on. The alternative to holding the consultation in early 1985 would be to have the staff visit before the end of 1984, which was clearly not appropriate. The timing suggested by the staff was a practical response to the circumstances, and Solomon Islands was not in a situation where frequent Article IV consultations were necessary. Nevertheless, he was surprised to hear the suggestion that Solomon Islands might consider making early repurchase.

As for technical assistance, the Central Banking Department had provided technical assistance to Solomon Islands in connection with the development of banking legislation and infrastructure, Mr. Prowse continued. The Central Banking Department had also been providing the Central Bank with senior management officers since its inauguration. As to energy, there had been a World Bank energy assessment for Solomon Islands that included technical assistance for energy planning; the World Bank was still considering technical assistance for petroleum exploration. The Asian Development Bank (AsDB) had recommended in 1983 the development of a power station fueled by wood, and the project had gone ahead with assistance in its construction and supervision from the AsDB. A regional fuel consumption proposal was being considered by the relevant authorities. The World Bank had recently approved a rural services project for Solomon Islands of approximately US$3.5 million, mainly to assist smallholders, but also to help estates producing palm oil commercially. That proposal was the fourth World Bank project in the Pacific to be cofinanced by the AsDB and the World Bank, with the former taking the leading role. The World Bank would continue to participate through supervisory visits, however, as far as possible, the AsDB would be the primary coordinating authority for the AsDB and the World Bank in Solomon Islands.

Although there were problems for the authorities in dealing with numerous aid authorities, there were also some benefits, Mr. Prowse noted. The United Nations Development Programme maintained a large office in Western Samoa, and staff frequently visited Solomon Islands to assist with the supervision of projects. Most important, the bilateral aid donors provided extensive supervision in a consulting and management capacity. The provision of suitable personnel was one area in which the Fund could contribute to the development process, by providing the Government with statisticians and general administrators. Overall, a great deal of help was being provided both bilaterally and multilaterally.

A number of Directors had expressed concern about budget expenditure and the Government's finances, Mr. Prowse recalled. It was remarkable that in his budget speech in November 1983, the Minister of Finance had said "the main shortcomings during the year have been in the government sector where expenditure controls, particularly on wages, salaries and allowances, have not been fully effective. Revenue collection has been slow and the execution of the development budget has not improved as it should have done." The authorities had adopted the recommendations of the Fund staff in that area. The Minister of Finance had gone on to say that "all Ministries are required to ensure that their spending is kept within the amount of funds given to them and no more." The Minister had also said that "no expenditures would be incurred, for instance, against aid-funded projects where funds are not yet available. To ensure control I shall reserve all expenditure on development estimates...and accounting officers will not be allowed to incur expenditure against projects until I have specifically reserved the funds. Tighter control will apply to advances made to the provinces also; where provinces are not making any efforts to clear their advances, they will be offset against their annual grant." Finally, Solomon Islands authorities would continue to implement the program that it had so enthusiastically adopted, and would continue to strive for the kind of hard-nosed management approved by the Fund.

The Acting Chairman made the following summing up:

Executive Directors generally endorsed the appraisal on Solomon Islands. They commended the Solomon Islands authorities for the implementation of a flexible exchange rate policy, the adjustment of interest rates, and the maintenance of a liberal exchange and trade system. Directors noted that these measures, together with more favorable external developments, contributed to a reduction in the external deficit on current account and an overall surplus in 1983. Inflation had moderated more than anticipated, and there had been a resumption of real economic growth.

Directors endorsed the Government's economic and financial objectives of further reducing the external current account deficit and inflation while raising the rate of real economic growth, including growth of investment. Although recognizing that, in line with program objectives, the overall budget deficit in relation to GDP increased only slightly in 1983, Directors expressed concern about the deterioration in current fiscal operations. They emphasized that realization of the program objectives would, however, require a strengthening of the budgetary position, particularly through restraint in the growth of wages and salaries and an improvement in external aid inflows, so as to reduce the fiscal deficit and its financing from domestic sources. Administrative problems also persisted in the implementation of development projects and in obtaining external aid reimbursement. Directors also noted the importance of sustaining export profitability through exchange rate and wage policies. Maintaining key interest rates positive in real terms should assist in fostering the mobilization of financial resources.

Directors recognized the structural factors present in Solomon Islands and the progress made by the authorities and the economy in this respect. In the light of the improved balance of payments position and the expectation of another overall payments surplus in 1984, Directors warmly commended the present intention of the Solomon Islands authorities not to make use of additional Fund resources under the current stand-by arrangement, while nonetheless intending fully to implement the program.

It is expected that the next staff discussion with the authorities for the Article IV consultation with Solomon Islands will be held by April 1985.

The Executive Board then took the following decision:

Review Under Stand-By Arrangement and Modifications of Performance Criteria

1. Solomon Islands has consulted with the Fund in accordance with paragraph 3(b) of the stand-by arrangement (EBS/83/81, Supplement 1, 6/23/83) and paragraph 19 of the letter from the Minister of Finance and the Governor of the Central Bank of Solomon Islands dated April 21, 1983 attached thereto.

2. The letter from the Minister of Finance and the Governor of the Central Bank of Solomon Islands dated December 1, 1983 shall be annexed to the stand-by arrangement for Solomon Islands, and the letter from the Minister of Finance and the Governor of the Central Bank of Solomon Islands dated April 21, 1983 shall be read as supplemented and modified by the letter of December 1, 1983.

3. Accordingly, the limits on total domestic credit of the banking system and net credit to the Government for the period October-December 1983 shall be those referred to in paragraph 3 of the letter of December 1, 1983 in place of those referred to in paragraph 14 of the letter of April 21, 1983 and specified in the table attached to it.

Decision No. 7604-(84/4), 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/84/3 (1/9/84) and EBM/84/4 (1/9/84).

2. AUSTRALIA - CHANGE IN REPRESENTATIVE RATE FOR AUSTRALIAN DOLLAR

The Fund finds, after consultation with the Australian authorities, that the representative exchange rate for the Australian dollar against the U.S. dollar, under Rule O-2(b)(i), is the consensus market rate, as determined by the Reserve Bank of Australia. The Fund will be informed immediately of any change in the representative exchange rate. (EBD/84/2, 1/3/84)

Decision No. 7605-(84/4) G/S, adopted
January 9, 1984

3. SOMALIA - TECHNICAL ASSISTANCE

In response to a request from Somalia for technical assistance, the Executive Board approves the proposal set forth in EBD/84/1 (1/3/84).

Adopted January 9, 1984

APPROVED: May 22, 1984

LEO VAN HOUTVEN
Secretary