

**FOR
AGENDA**

EBS/83/154
Supplement 1

CONFIDENTIAL

August 23, 1983

To: Members of the Executive Board
From: The Secretary
Subject: Somalia - Review of Stand-By Arrangement

The attached supplement to the paper on a review of the stand-by arrangement for Somalia has been prepared on the basis of additional information. This subject has been scheduled for discussion by the Executive Directors tomorrow, Wednesday, August 24, 1983.

Att: (1)

INTERNATIONAL MONETARY FUND

SOMALIA

Review of Stand-By Arrangement - Supplementary Information

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

(In consultation with the Fiscal Affairs Department)

Approved by J.B. Zulu and W.A. Beveridge

August 23, 1983

At the request of the Somali authorities a Fund mission visited Somalia during August 6-15, 1983, to review the progress that has been made in preparing Somalia's medium-term recovery program (1984-86) and to hold preliminary discussions on a possible arrangement under the extended Fund facility to begin upon the completion of the current stand-by arrangement. The mission obtained the following additional information to that contained in EBS/83/154 (7/27/83) on recent economic and financial developments in Somalia.

1. Livestock exports: In mid-May 1983, after the discovery of rinderpest in some imported cattle, Saudi Arabia imposed an embargo on cattle imports from Africa and a number of other countries. The Somali authorities indicated early in June that an agreement had been reached to the effect that Somali cattle would be allowed into Saudi Arabia if they were vaccinated, quarantined at shipping points, and certified by the FAO to be free from rinderpest. While the Somali authorities have had a continuing dialogue with Saudi Arabia to seek that the ban be lifted temporarily pending Somalia's compliance with these requirements, Somali cattle exports, which account for about 30 percent of Somalia's export receipts, have come to a complete standstill since June. A high level Somali delegation headed by the Minister of Foreign Affairs, and including the Ministers of Finance, Commerce, and Livestock, as well as the Governor of the Central Bank, departed for Saudi Arabia on August 11, 1983 to discuss the matter further with the Saudi Arabian Government. In discussions with the staff on August 16 and 17, the Minister of Finance expressed optimism that Saudi Arabia would lift the ban on Somali cattle shortly. If the ban remains in force during the peak export season to Saudi Arabia, which begins in about a week and coincides with the pilgrimage season, Somalia could sustain a loss of up to about US\$35 million. In that event, Somalia would probably experience an export

shortfall which could qualify it for a compensatory financing drawing. The authorities have already expressed an interest in making such a drawing and are expected to provide the requisite data shortly.

2. Fiscal, monetary, and price developments: Fiscal and monetary developments during the first half of 1983 appear to be generally in line with program targets. Somalia has met all the performance criteria for end-June 1983. The Government reduced its net indebtedness to the banking system during the first half of 1983 by 6 percent, compared with the programmed reduction of 5 percent. The growth of domestic credit was, therefore, contained to 2 percent instead of a program target of 3 percent. The net foreign assets of the banking system declined by more than projected due to some extent to the impact of the cattle embargo. Accordingly, domestic liquidity declined by about 9 percent, a substantially larger reduction than the 1 percent envisaged under the program. Notwithstanding this development, the rate of inflation, which had subsided during the first quarter of 1983, increased during the second quarter on the basis of preliminary data for the Mogadiscio consumer price index through end-May 1983. The Somali authorities maintain that this is due to transient factors, namely the delays in the seasonal rains in the regions, which slowed down the flow of agricultural produce into Mogadiscio, and temporary supply shortages caused by transportation and distribution bottlenecks. Furthermore, according to the Somali authorities, movements in the Mogadiscio consumer price index reflect to a great extent the urbanization pressures in the Mogadiscio area and not necessarily price developments in the country as a whole. They expected the rate of inflation in the Mogadiscio area to decline significantly during the rest of 1983.

3. Banking reform: In accordance with the intention expressed in the letter of intent of June 6, 1983, the Somali authorities signed in July 1983 a three-year advisory assistance contract with Midland Bank to provide banking and financial advice to enhance the effectiveness of Somalia's commercial banking system. In September 1983, Midland Bank is expected to start with a study to determine how to improve the operations, management, and accounting procedures of the Commercial and Savings Bank of Somalia.

4. Employment policy: Until recently the Government of Somalia had a system of guaranteed employment in the public sector for all secondary school and university graduates. While the Government had not been enforcing this system of automatic employment in recent years, it took a decision to discontinue it officially at the beginning of August 1983. Recruitment of university and high school graduates for positions in public schools, the military, or the civil service will be on a competitive

basis depending on the availability of vacancies. The Government has also decided to establish more vocational schools to meet the demand for skilled labor.

5. Medium-term recovery program: The Somali authorities have made considerable progress in the preparation of a medium-term recovery program for 1984-86. The core public investment program has been scaled down from about US\$1.5 billion to US\$1.2 billion by moving projects from the core program to the supplementary investment program. On the basis of present commitments, the foreign financing available amounts to US\$672 million. Domestic financing is estimated at US\$133 million. The unfinanced gap, accordingly, amounts to US\$427 million, the foreign component of which the Somali authorities hope to raise subsequent to the Consultative Group Meeting currently scheduled for October, 1983. In consultation with the Fund and the World Bank, the authorities have also prepared the macroeconomic framework and a policy action program. A draft of the medium-term recovery program is expected to be available for further discussion with the Fund and the World Bank in September.