DOCUMENT OF INTERNATIONAL MONETARY FUND AND NOT FOR PUBLIC USE

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CONFIDENTIAL

September 15, 1983

To: Members of the Executive Board

From: The Secretary

Subject: Liberia - Stand-By Arrangement

Attached for the records of the Executive Directors is the text of the stand-by arrangement for Liberia agreed at Executive Board Meeting 83/139, September 14, 1983.

Att: (1)

<u>Liberia - Stand-By Arrangement</u>

Attached hereto is a letter dated July 14, 1983 from the Minister of Finance and the Governor of the National Bank of Liberia requesting a stand-by arrangement and setting forth the objectives, policies, and measures that the authorities of Liberia intend to pursue for the period of this stand-by arrangement.

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

1. For the period from September 14, 1983 to September 13, 1984 Liberia will have the right to make purchases from the Fund in an amount equivalent to SDR 55.0 million, subject to paragraphs 2, 3, 4, and 5 below, without further review by the Fund.

2. (a) Purchases under this stand-by arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 14.0 million until December 15, 1983, the equivalent of SDR 28.0 million until March 15, 1984, and the equivalent of SDR 42.0 million until June 15, 1984.

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

3. Purchases under this stand-by arrangement shall be made from borrowed resources only, provided that any modification by the Fund of the proportions of ordinary and borrowed resource shall apply to amounts that may be purchased after the date of modification.

4. Liberia will not make purchases under this stand-by arrangement that would increase the Fund's holdings of Liberia's currency in the credit tranches beyond 25 pecent of quota or increase the Fund's holdings of that currency resulting from purchases of supplementary financing or borrowed resources beyond 12.5 per cent of quota:

(a) during any period in which the data at the end of the preceding period indicate that

(i) the limit on the National Bank of Liberia's net domestic assets described in paragraph 27 and further specified in Schedule A of the attached letter, or

(ii) the limit on net credit of the banking system to the public sector described in paragraph 27 and further specified in Schedule A of the attached letter, or

(iii) the limit on net credit of the banking system to the Government described in paragraph 27 and further specified in Schedule A of the attached letter, or

(iv) the limit on external arrears described in paragraph 21 and further specified in Schedule B of the attached letter is not observed; or

(b) if Liberia fails to observe the limits on authorization of new public and publicly guaranteed foreign indebtedness described in paragraph 22 of the attached letter; or

(c) during any period after December 14, 1983 until Liberia and the Fund review the progress of rescheduling of payments due on public debt to official creditors, and if any understandings are reached pursuant to this review, while any such understandings are not being observed; or

(d) during any period after March 14, 1984, until the Fund review mentioned in the last sentence of paragraph 29 of the attached letter is completed and any appropriate understandings are reached on budget performance (referred to in paragraph 13), the reschedulings of public debt (referred to in paragraph 19), and the operation of the petroleum sector (referred to in paragraph 25); or

(e) during the entire period of this stand-by arrangement, if Liberia

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

(ii) introduces multiple currency practices, or

(iii) concludes bilateral payments agreements which are inconsistent with Article VIII, or

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

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

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

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

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

8. Liberia shall pay a charge for this stand-by arrangement in accordance with the decisions of the Fund.

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

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

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

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

11. In accordance with paragraph 29 of the attached letter Liberia will consult with the Fund on the adoption of any measures that may be appropriate at the initiative of the Government or whenever the Managing Director requests consultation because any of the criteria in paragraph 4 above have not been observed or because he considers that consultation on the program is desirable. In addition, after the period of the arrangement and while Liberia has outstanding purchases in the upper credit tranches, the Govenment will consult with the Fund from time to time, at the initiative of the Government or at the request of the Managing Director, concerning Liberia's balance of payments policies.

ATTACHMENT

Monrovia, July 14, 1983

Mr. Jacques de Larosière
Managing Director
International Monetary Fund
Washington D.C.

Dear Mr. de Larosière:

1. This urgent appeal for assistance is sent to you on behalf of the Liberian People at a moment of unprecedented hardship which is largely due to external conditions beyond our control and which our utmost efforts and sacrifices alone cannot overcome. Since 1980 our aggregate production has fallen sharply. Unemployment, especially in urban areas has, reached exceptionally high levels. The revenue base of the public sector has rapidly weakened, and we have been unable to bring the budget deficit down to levels which could be soundly financed. As a result, the heavy borrowing of the public sector in a financial market constrained by the sizable deficit in current external payments and by capital flight has contributed to the curtailment of productive activity and investment. The external debt burden of the public sector, in spite of important rescheduling, has in recent months exceeded our modest means. After two and a half years of serious adjustment effort supported by Fund stand-by programs, we are determined to continue along the way we have charted toward stability and revival, but, more acutely than ever, we need the support of the Fund, other international organizations, and friendly governments.

2. The Government of Liberia's 1982/83 economic program, which was supported by a Fund stand-by arrangement, was prepared at a time when the outlook in the world markets for iron ore and rubber, Liberia's major exports, was promising. Unfortunately, the demand for and prices of these commodities continued to decline with pronounced adverse consequences for Liberian output, employment and government revenues. In 1982/83 real GDP is estimated to have declined by 4 per cent, mainly reflecting a fall in export volume estimated at 11 per cent.

3. In the face of the unfavorable trends in world markets, the Government of Liberia found it necessary to implement measures additional to those outlined in our July 21, 1982 letter to you, with the aim of keeping the adjustment program on track. These measures were outlined in the supplemental Letter of Intent dated December 9, 1982. The most important measure was a 16-2/3 to 25 per cent progressive reduction in wages and salaries effective January 1, 1983. The proposals for these measures were prepared and their implementation followed up by the Economic and Financial Management Committee, which was established early in the fiscal year. We believe that, despite adverse circumstances, the 1982/83 program has yielded important results.

4. Specifically, government expenditures were cut by 10 per cent from the previous year. Recurrent expenditures, which had increased rapidly in the preceding fiscal years, were reduced by $26 million, or by 12 per cent.

The central government wage bill was reduced by 13 per cent, reflecting cuts in wage rates and employment. The cut in public sector salaries effected on January 1, 1983, represents a cut of 22 per cent in a full fiscal year.

Due to improved enforcement, revenues from the personal income tax have achieved their projected levels despite the decline in taxable incomes.

5. The overall deficit on a check issued basis was reduced by $19 million, or from $118 million (10.6 per cent of GDP) in FY 1981/82 to $99 million (8.7 per cent of GDP) (preliminary) in FY 1982/83. This reduction would have been significantly greater but for a $23 million decline in revenues, due to external factors and lower foreign grant aid.

In the external area, despite a reduction in export receipts by 8 percent in 1982/83, the current account deficit of the balance of payments is estimated to have been reduced from $92 million (8.2 per cent of GDP) in 1981/82 to $74 million (6.5 per cent of GDP) in 1982/83.

6. Cost reduction measures in both public and private sectors have improved significantly the potential competitiveness of Liberian exports in world markets. While the public sector cut salaries, major private corporations curbed costs by laying off personnel--in one major case one-third of the work force--and contractual wage awards in the private sector contained little or no increase in nominal wages.

7. In the area of foreign payments, the limited reserves of the National Bank of Liberia and its resulting chronic inability to make timely payments on external financial obligations were felt as a severe problem throughout the year. Nevertheless, the Government managed, not without difficulty, to keep its external payments current until the last quarter of the fiscal year, when a carefully prepared effort to settle all due offshore payments had to be postponed because of unforeseen problems with the oil import credit facility. The debt rescheduling under the London Club was concluded in December 1982.

8. Despite the positive measures and accomplishments of the past year, the Liberian economy and the country's financial system remain in a most difficult situation. We have had serious problems in containing domestic bank financing of the government deficit in the 1982/83 program. Such

bank financing reached $78 million, which includes a $16 million reduction in check float and domestic arrears. This compares with an increase in the check float and domestic arrears of $26.8 million in fiscal year 1981/82.

The Government of Liberia recognizes the importance of continuing its efforts to reduce external and internal imbalances and to promote confidence at home and amongst the international financial community. The Government has therefore adopted a new economic and financial program covering 1983/84, which will focus on a reduction in domestic bank credit to the Government and on a strengthening of the external position of the National Bank of Liberia. Assuming a partial recovery in world markets for Liberia's main export products and continued restraint on aggregate domestic demand, the program aims at a further reduction in the current account deficit of the balance of payments in 1983/84. The specific measures and policies to be pursued during FY 1983/84 are summarized below and deal with the following areas: fiscal policy, public corporations, external policies and financial policies. In support of this program the Government of Liberia requests a further one-year stand-by arrangement from the International Monetary Fund in an amount of SDR 55 million, and it requests the cancellation of the existing stand-by arrangement for 1982/83.

Fiscal Policy

9. Given a large public sector imbalance at the outset and the institutional characteristics of the Liberian economy, the main thrust of the adjustment process necessarily consists of measures to curb the Government's total deficit and to reduce the level of domestic credit to Government. Adjustment in FY 1983/84 includes both expenditure reductions and revenue increases.

10. Initial estimates for the fiscal year 1983/84 (beginning July 1, 1983) indicate that without additional measures revenue would increase only moderately. Due to an expected upturn in the export sector in the second half of fiscal 1983/84 and because of our efforts to improve enforcement and collect existing taxes (1983 was proclaimed as "the year of rigid enforcement of tax collection"), we should be able to increase revenue, especially in the second half of the fiscal year. In FY 1983/84 a concerted effort will also be made to increase collections of customs duties.

11. The Government has implemented several measures to generate additional revenues amounting to $16.9 million (estimated yield shown in millions of dollars).

a.	An increase in the excise tax on gasoline from 32 to 92 cents per gallon	12.1
b.	An increase in the tax on bills of entry for duty-free goods processed by concessions (stamp tax for each $100 or fraction thereof) from 25 to 75 cents	1.0
c.	An increase in the consular fee on transshipment goods from 2.5 to 7.5 per cent	3.4
d.	Imposition of excise tax on goods sold by military PXs at 50 per cent of the normal rate for beer, stout, soft drinks, and domestic spirits and tobacco, and custom duties at 25 per cent of the normal rate for imported spirits and tobacco	0.4
	Total	16.9

As a result of these measures the level of revenue in FY 1983/84 is expected to exceed the previous year's level by 11 per cent.

12. To curtail expenditures, the Government has cut sharply some budgeted items and reallocated other items within their expenditure categories to minimize outlays.

a. Any effort to reduce significantly the level of recurrent expenditures necessarily involves a reduction in the cost of personnel services. We have therefore taken additional steps to fully maintain the salary and employment freeze in the central government and in the public corporations.

b. Vacant posts will not be filled except in the case of transfers within each agency or from other agencies. We will continue to review carefully all departmental employment rolls, eliminating vacant posts and making some positions redundant. We are being assisted in our efforts by a consulting team, which is doing a physical payroll audit. These efforts will result in a further cut in personnel costs. The wage bill for FY 1983/84 represents a reduction from 1981/82 outlays of 22 per cent.

c. The sale of government cars will generate annual savings in expenditure for gasoline and repairs of approximately

$750 thousand. Savings of $2 million will be made on foreign travel expenditures by the introduction of a voucher system. A reclassification results in an apparent increase in subsidies, but actual subsidies to public corporations will be kept within previous overall limits.

d. Concerning the development outlays, priority will be given to projects nearing completion, projects with a high rate of return, and projects with maximum foreign financing. Locally financed development expenditures will be held slightly below the level budgeted in FY 1982/83.

We have requested the support of the UNDP, IBRD, other international institutions, and bilateral donors in organizing an aid donors' conference which is scheduled to take place before the end of 1983.

13. As regards non-budgetary expenditure, including encumbrances, we have taken the measures required to bring these items under budgetary control. Encumbrances have been abolished in FY 1983/84. The Economic and Financial Management Committee (EFMC) will authorize non-budgetary expenditure only to the extent that equivalent cuts are made elsewhere, and that revenues are at or above target levels.

The budgetary costs of support to the National Iron Ore Company will be examined in the context of the mid-term review with the Fund.

14. The Government estimates that the overall budgetary deficit, defined in accordance with the usual IMF presentation, will not exceed $42.4 million in FY 1983/84 compared with $99.0 million in FY 1982/83. Bank financing of the deficit will be reduced from the $78 million noted above in FY 1982/83 to $30 million in FY 1983/84.

15. With the aim of maintaining all payments on a current basis, the Government has made some progress in FY 1982/83 in reducing domestic arrears. The Government will ensure that on June 30, 1984, its domestic arrears shall not exceed the level of June 30, 1983. In addition, arrears in payments to be made by public corporations will be progressively reduced.

Public Corporations

16. The Government intends to implement the project recently agreed upon with the World Bank to rationalize the public corporations. This project includes the possible sale of some of these corporations to the private sector either in full or in joint venture.

External Policies

17. The Government is acutely aware of the need to further improve competitiveness of Liberia's export products. Given the linkage of the domestic currency to the U.S. dollar, the persistent strength of the latter over the past year has made any net improvement in international price competitiveness extremely difficult to achieve. Nevertheless, actions have been taken by both private and public sectors to enhance competitiveness. Layoffs by firms holding concessions in the iron ore, rubber and timber industries have reduced their wage bills and, together with the wage developments in the public sector, have minimized pressures for wage increases. In the event of world market price increases for these products as the result of the anticipated general economic recovery, these firms are positioned to realize significant productivity gains and to compete vigorously for enlarged market shares. Continued strong cost-cutting measures are necessary throughout the Liberian economy to enable our country to attain a sustainable external position.

18. With further actions it has introduced to contain and to reduce the domestic financing gap of the public sector, the Government of Liberia continues to emphasize the importance of strengthening the country's external payments position. Despite the decline in exports from $509 million in 1981/82 to an estimated $469 million in 1982/83, the current account deficit is projected to be reduced from $92 million in 1981/82 to $74 million in 1982/83, due to an even larger fall in imports. Prices for rubber and timber have increased modestly, but prices for iron ore are not likely to rise until the recovery has achieved broad momentum throughout the industrialized world and until steel production has increased. With a projected increase in exports of 12 per cent in 1983/84 to $527 million, the program aims at a further reduction of the current account deficit to $50 million. This further improvement assumes a modest increase in imports contained by restrictive budgetary policies and the effect on interest payments of additional debt relief which is being negotiated. Wage cuts, layoffs, and pervasive consequences of the fourth successive year of decline in economic activity, including stagnant investment, are currently limiting imports.

19. The timely settlement of external financial obligations and especially meeting current payments continued to prove difficult in 1982/83. Essential ingredients of managing Liberia's external debt service obligations during 1983/84 are a further Paris Club rescheduling of principal and interest payments due on public debt to bilateral creditors and another London Club refinancing of principal repayments due on public sector obligations to private banks. Contacts for these reschedulings have been initiated. We will use our best efforts to reach agreement before end-November 1983.

20. To help regularize the payment of public debt service and to help budget the limited foreign exchange resources of the Government, we have requested an expert advisor in debt management under the technical assistance of the Fund. He will undertake a complete census of the external debt of the Government and public corporations and will initiate a regular scheduling of debt service payments. By being able to anticipate service payments more precisely in advance, the Government will be able to budget its external accounts and foreign exchange resources more effectively.

21. At the end of June 1982, the public sector arrears with respect to current foreign exchange payment obligations were virtually eliminated. However, towards the end of the 1982/83 financial year new arrears of $14 million were incurred. We intend to ensure that, not later than May 31, 1984, in accordance with Schedule B attached hereto, external arrears--excluding the oil facility--shall be fully paid off. As for the oil facility, we have requested a refinancing on London Club terms.

22. Throughout 1983/84 strong efforts will be maintained to prevent the emergence of new arrears; no purchase will be made from the Fund if new arrears on public debt service occur. The Government intends to accumulate gross foreign exchange reserves held by the National Bank of Liberia of at least $10 million by end-June 1984. Our foreign borrowing policies will continue to be extremely cautious, and the balance of payment consequences of any additional public sector foreign debt will be carefully evaluated in a written analysis. A copy of any and all such analyses will be supplied to the Fund. During the period of the stand-by arrangement, the Government will not contract more than $5 million of new public sector or Government-guaranteed external debt on commercial terms with maturities of one to twelve years (excluding use of Fund resources and rescheduling of existing liabilities).

23. During the period of the stand-by arrangement the Government of Liberia will not introduce new or modify existing multiple currency practices, impose new or intensify existing restrictions on payments and transfers for current international transactions, conclude any bilateral payments arrangements with Fund members, or impose new or intensify existing restrictions on imports for balance of payments reasons. The Government will continue to operate an open economy in order to obtain the full benefits of international trade in goods and services.

24. The Government of Liberia notes with satisfaction that all producer prices of public corporations have been brought into alignment with world market prices and intends to continue this policy. Likewise, consistent with present policy, the Government will not subsidize prices of any imported goods. The Government will eliminate and henceforth avoid

implicit subsidies to other public corporations via the failure of these corporations to pay the Liberia Petroleum Refining Company (LPRC) and the Liberia Electricity Corporation (LEC) currently and in full for any products and services received after the date of this letter. The elimination of these subsidies will make a major contribution toward better payment discipline generally and toward managing the scarce foreign exchange resources of the public sector.

25. To minimize the foreign exchange cost of purchasing, shipping, and financing petroleum products, the refining operations of the LPRC have been terminated and shall remain so during the stand-by period; the LPRC facility shall be used solely for the unloading, storage, and distribution of petroleum products imported by the LPRC itself or by leasees. All existing contracts with expatriate consultants to the LPRC have been terminated. The Government will publicly affirm that the LPRC has no monopoly on the importation and distribution of petroleum products and that private companies including concessions are permitted to import all such products in competition with each other and the LPRC.

Financial Policies

26. In order to strengthen the financial position of the National Bank of Liberia, to diminish the high level of excess reserves, and to limit potential pressure on foreign exchange resources, effective February 1, 1983, the monetary authorities raised the required reserve ratio of the commercial banks from 15 per cent to 30 per cent.

27. Consistent with the balance of payments targets, the Government intends in the course of FY 1983/84 to limit the increase in net domestic assets of the National Bank of Liberia to $30 million, which, with the projected net purchases from the Fund of $40 million, would allow gross reserves to increase by $10 million. In addition, the Government intends to limit the increase in net claims on public sector from the banking system to $36 million and, within this ceiling, to limit the increase in net credit of the banking system to the Government to $30 million in the 12 months ending June 30, 1984. The schedule of credit ceilings is contained in Schedule A.

28. In order to remain within the limits on net domestic assets, the National Bank of Liberia will closely monitor its net position with the commercial banks. In this context, the National Bank of Liberia will review the interest charges on its credits to the commercial banks. Similarly, the National Bank will not accept as eligible to meet reserve requirements commercial bank loans to the Government or to other public entities. The monetary authorities will review the reserve requirements for savings deposits, with a view to determining whether a reduction will

encourage domestic savings by enabling commercial banks to pay higher yields.

29. We believe that the policies and measures set forth in this letter are adequate to achieve the objectives of our adjustment program, but we will take any further measures that become necessary to achieve these goals. Liberia will consult with the Fund on the adoption of such measures in accordance with the policies of the Fund, and will provide the Fund staff with all relevant information in connection with the progress being made in achieving the program's objectives. In particular, the Liberian authorities will initiate immediate consultations with the Fund staff at any time revenue falls short of budget projections, or expenditures exceed budget levels. Also, Liberia will consult with the Fund staff in the event that net credit to the Government from the banking system, at the end of two consecutive months, exceeds the next limit to be observed. The Liberian authorities will review with the Fund the progress in the implementation of the program, not later than January 31, 1984.

Very truly yours,

Thomas D.V. Hanson
GOVERNOR, NATIONAL
BANK OF LIBERIA

G. Alvin Jones
MINISTER OF FINANCE

Schedule A: Credit Ceilings

(In millions of dollars)

	Net domestic assets of the National Bank of Liberia	Net credit to Government from banking system	Net credit to public sector from banking system 1/
June 30, 1983 2/	182	255	275
November 30, 1983	194	267	290
February 29, 1984	203	276	300
May 31, 1984	210	283	309
June 30, 1984	212	285	311
Total change	30	30	36

1/ Includes deposits of public corporations with banking system.
2/ Actual.

Schedule B: Limits on External Arrears

(In millions of dollars)

June 30, 1983	14
November 30, 1983	9
February 29, 1984	4
May 31, 1984	0
June 30, 1984	0