FOR AGENDA

EBS/83/216

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October 4, 1983

To: Members of the Executive Board

From: The Secretary

Subject: Upper Credit Tranche Stand-By and Extended Arrangements Approved in 1981

The attached report provides background material for the Board discussion of the paper on a review of upper credit tranche arrangements approved in 1981 and of some issues related to conditionality (EBS/83/215, 10/4/83) scheduled for Friday, November 4, 1983.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Gerhard, ext. 74987.

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

Upper Credit Tranche Stand-By and Extended Arrangements Approved in 1981

Prepared by the Exchange and Trade Relations Department

(In consultation with other departments)

Approved by C. David Finch

October 3, 1983

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I. Introduction

This paper examines the experience with upper credit tranche stand-by and extended arrangements that were approved in 1981, based on data available as of end-June 1983. The last general review of upper credit tranche stand-by and extended arrangements was held in July 1982, when the Executive Board reviewed stand-by arrangements approved in 1980 and extended arrangements approved in 1978, 1979, and 1980. 1/ At that time, it was decided that a further review of stand-by arrangements and the extended Fund facility should be undertaken not later than December 31, 1983 (Decision No. 7157-(82/93), July 7, 1982). The present survey, accompanying a paper entitled "Review of Upper Credit Tranche Arrangements Approved in 1981 and of Some Issues Related to Conditionality" (EBS/83/215, 10/4/83), is intended to serve as background material for that review. As was the case in previous years, this paper does not survey all aspects of Fund arrangements, but rather attempts to focus on those matters that have been of special importance in the recent past.

Because of the diversity of the countries under review and the special factors that affect the sustainability of the balance of payments in each individual situation, it has been found useful to examine many issues regarding program assumptions, design, targets, and achievements at the level of individual cases. The differences and similarities among individual country experiences are illustrated with scatter diagrams and are discussed extensively in qualitative terms, but the use of general averages has deliberately been de-emphasized. In this respect, the present approach differs from that followed in previous papers which had focused to a greater degree on issues related to the design and monitoring of adjustment programs that lend themselves well to generalizations. Accordingly, earlier surveys made greater use of general averages and often compared situations before and after implementation of an adjustment program with developments in countries not undertaking an arrangement with the Fund. The focus of the present paper on the sources of payments imbalances, the selection and implementation of policy measures that are appropriate in specific situations, and the factors influencing progress toward viability of the balance of payments in individual countries, makes necessary a more disaggregated analysis. In adopting this approach, the staff has sought to take into account observations made by Executive Directors during previous reviews.

1/ The following documents provided background material for the discussion: "Review of Extended and Upper Credit Tranche Stand-By Arrangements," (EBS/82/97, 6/9/82); "Supplementary Material for Review of Recent Extended and Upper Credit Tranche Stand-By Arrangements," (EBS/82/97, Supplement 1, 6/10/82), and "Adjustment Programs--Broad Design and Key Indicators," (EBS/82/98, 6/9/82).

It will be noted that the present paper does not attempt to analyze the experience with one-year stand-by arrangements separately from that with multiyear stand-by or extended arrangements. A number of the factors that previously distinguished the different lengths and forms of arrangements have become relatively less important in recent years, owing to the increased emphasis on framing policies within a medium-term context and the greater reliance on supply-side measures in all adjustment programs supported by arrangements with the Fund, including one-year stand-by arrangements. Although countries that are in a position to make a longer term commitment to a particular adjustment path have continued to make frequent use of multiyear arrangements, this is apparently not due to fundamental differences in the kinds of problems that are addressed. Rather it more often reflects the value to the particular country of the assurance of an extended period of access to Fund resources and the administrative and political capacity of the country to make meaningful multiyear commitments.

The assessments in this paper should be regarded as preliminary and tentative in light of the short period that has elapsed since the programs under review were initiated. Insufficient time has passed for the full effects of some of the measures undertaken in many programs to be realized, and further policy changes are being implemented in connection with a number of multiyear arrangements that have not yet expired.

The following sections of the paper (II and III) survey the amount of resources involved in arrangements approved during 1981, and provide a summary of developments in the international economic environment during the period preceding approval of the arrangements. Sections IV and V describe the economic problems faced individually by the countries under review and the adjustment strategies adopted to address these problems. Sections VI and VII summarize the policy content of adjustment programs and the monitoring techniques used by the Fund to ensure that its resources are being used appropriately. Finally, Section VIII attempts to assess the extent to which the objectives of programs have been met and to evaluate the amount of adjustment remaining to be accomplished to reach balance of payments viability. Data for individual countries are presented in Appendix A and developments in other countries with programs beginning in 1981 under arrangements approved previously are discussed in Appendix B. Other appendices include a survey of the use of particular policy instruments in adjustment programs (Appendices C and D); and an analysis of the components of changes in the external current account balance of the countries under review (Appendix E).

II. Commitments and Use of Fund Resources

Twenty-seven arrangements for use of Fund resources in the upper credit tranches were approved in 1981, four more than in the preceding year (Table 1). 1/ Of these 10 were arrangements under the extended Fund facility, 4 were stand-by arrangements covering more than one year and the other 13 were one-year stand-by arrangements. The total amount of commitments was SDR 14.6 billion, of which SDR 5.2 billion (36 percent) was to be provided from ordinary resources and SDR 9.4 billion (64 percent) from borrowed funds. 2/ Some two thirds of the total commitments (SDR 9.9 billion) were for arrangements approved under the extended Fund facility. Amounts approved under extended arrangements averaged 365 percent of quota and ranged from 215 percent of quota for Pakistan to 450 percent of quota for Costa Rica; annual access for all extended arrangements averaged some 129 percent of quota. 3/ About one fourth of the total commitments (SDR 3.6 billion) was in respect of amounts approved under the four multiyear stand-by arrangements. The annual access provided in these arrangements averaged 121 percent of quota, or slightly less than in the extended arrangements. The 13 one-year stand-by arrangements accounted for SDR 1.1 billion, less than 8 percent of the total commitments in arrangements approved in 1981. Approved amounts varied from less than 25 percent of quota for Burma to 225 percent of quota for Korea, with the average being about 108 percent.

None of the extended arrangements approved in 1981 has yet expired, but those with Costa Rica, Morocco, Sierra Leone, Zaire, and Zambia were canceled in 1982. The other five are still in effect. Total purchases to date under the ten arrangements are SDR 4.8 billion, with the undrawn balance for uncanceled arrangements amounting to SDR 2.8 billion. The three-year stand-by arrangements with Romania and Yugoslavia are also still in effect. The two-year stand-by arrangement with Togo expired in February 1983 but purchases were interrupted early on and not resumed. The two-year stand-by arrangement with Thailand was canceled in 1982 and replaced by a one-year arrangement for a smaller amount after purchases of slightly less than half of the approved amount were made. The one-year stand-by arrangements with Burma, Ethiopia, Korea, Liberia, Mauritania, Mauritius, Senegal, Somalia, and Uganda expired as scheduled after full purchase of the approved amounts.

1/ There were 12 multiyear upper credit tranche arrangements approved in prior years for which approval of a second- or third-year economic policy program was required during 1981. Six of these were extended arrangements and the remaining six were stand-by arrangements. Economic developments in these countries during 1981 were described in the previous Review Paper (EBS/82/97, 6/9/82), and are summarized in Appendix B. A more detailed report on each individual case has been provided to Executive Directors in connection with the reviews of each of these arrangements.

2/ The average share of borrowed resources was about 60 percent for extended arrangements and one-year stand-by arrangements, and about 75 percent for multiyear stand-by arrangements.

3/ Excluding the arrangement for Pakistan, which replaced a previous extended arrangement for technical reasons, the smallest arrangement in relation to quota was for India (291 percent).

Table 1. Extended Fund Facility Arrangements and Stand-By Arrangements in the Upper Credit Tranches Approved in 1981

Country	Date of Approval	Expiration Date	Amount of Arrangement: Millions of SDRs: Approved	Amount of Arrangement: Millions of SDRs: Drawn 1/	Amount of Arrangement: Percent of Quota: Approved	Amount of Arrangement: Percent of Quota: Drawn 1/
Extended Fund Facility Arrangements						
Costa Rica	6/17/81	6/16/84 2/	276.75	22.50	450	37
Dominica	2/6/81	2/5/84	8.55	7.12	295	246
India	11/9/81	11/8/84	5,000.00	2,700.00	291	157
Ivory Coast	2/27/81	2/22/84	484.50	330.60	425	290
Jamaica	4/13/81	4/12/84	477.70 3/	365.40	430	329
Morocco	3/9/81	10/7/83 4/	817.05	136.50	363	61
Pakistan	12/2/81	11/23/83	919.00	730.00	215	171
Sierra Leone	3/30/81	2/22/84 5/	186.00 3/	53.60	400	115
Zaire	6/22/81	6/21/84 6/	912.00	175.00	400	77
Zambia	5/8/81	5/7/84 7/	800.00	300.00	378	142
Multiyear Stand-By Arrangements						
Romania	6/15/81	6/14/84	1,102.50	633.90	300	172
Thailand	6/3/81	3/31/83 8/	814.50	345.00	300	127
Togo	2/13/81	2/12/83	47.50	7.25	167	25
Yugoslavia	1/30/81	12/31/83	1,662.00	1,433.00	400	345
One-Year Stand-By Arrangments						
Burma	6/12/81	6/11/82	27.00	27.00	25	25
C.A.R.	4/10/81	12/31/81	10.40	8.00	43	33
Ethiopia	5/8/81	6/30/82	67.50	67.50	125	125
Grenada	5/12/81	5/10/82	3.43	2.90	76	64
Korea	2/13/81	2/12/82	576.00	576.00	225	225
Liberia	8/26/81	9/15/82	55.00	55.00	99	99
Madagascar	4/13/81	6/26/82	109.00 3/	39.00	213	76
Mauritania	6/1/81	3/31/82	25.80	25.80	101	101
Mauritius	12/21/81	12/20/82	30.00	30.00	74	74
Senegal	9/11/81	9/10/82	63.00	63.00	100	100
Solomon Islands	5/29/81	5/28/82	1.60	0.80	50	25
Somalia	7/15/81	7/14/82	43.13	43.13	125	125
Uganda	6/5/81	6/30/82	112.50	112.50	150	150

Source: Fund documents.

1/ As of June 30, 1983.
2/ Canceled and replaced by new stand-by arrangement on 12/20/82.
3/ Augmented to amount shown.
4/ Canceled and replaced by new stand-by arrangement on 4/26/82.
5/ Canceled on 4/6/82.
6/ Canceled on 6/21/82.
7/ Canceled on 7/3/82.
8/ Canceled and replaced by new stand-by arrangement on 11/17/82.

The arrangement with the Central African Republic expired before observance of the performance criteria for the last test data could be ascertained; subsequently, having observed all performance criteria, the Central African Republic was allowed to draw the balance remaining under the arrangement as an outright purchase. There were only three arrangements (Grenada, Madagascar, and the Solomon Islands) in which less than the full approved amount was purchased. Total drawings under one-year stand-by arrangements were some 94 percent of the approved amount. This proportion is considerably higher than has been the experience with one-year arrangements covered in previous reviews.

Upper credit tranche arrangements had been approved in previous years for 19 of the 27 countries for which such arrangements were approved in 1981. 1/ The previous arrangements with Burma, India, and Romania for use of resources in the upper credit tranches had all expired two years or more before the 1981 arrangement was approved. The arrangements approved were consecutive, in the sense that they were initiated within six months or less after the expiration or cancellation of a previous upper tranche arrangement in 16 cases; in 3 other countries (the Central African Republic, Grenada, and Uganda), the arrangements were consecutive to a previous use of Fund resources in the first credit tranche. As of the end of 1982, net use of Fund credit had been outstanding for more than 15 years for 2 of the 27 countries under review and for more than 10 years in 7 cases.

Many of the countries for which use of Fund resources in the upper credit tranches was approved during 1981 also made use of Fund credit under other facilities. Thailand made a purchase equivalent to 6 percent of quota under the buffer stock financing facility in October 1982. In addition, 21 of the 27 countries made purchases under the compensatory financing facility during 1981-82, in most cases shortly before or during the program period covered by the upper credit tranche arrangement. 2/ Amounts purchased ranged from 23 percent (Burma) to 105 percent of quota (Morocco, which made use of the cereals provision), and averaged about 56 percent of quota during the period. 3/

In addition to the use of Fund resources, IBRD/IDA credit in the form of a structural adjustment loan was granted during 1981-82 to 7 of

1/ The eight countries which had not previously made use of Fund resources in the upper credit tranches were the Central African Republic, Dominica, Ethiopia, Grenada, Ivory Coast, the Solomon Islands, Thailand, and Uganda. In four cases (Jamaica, Morocco, Pakistan, and Senegal), the previous use of resources had included an extended arrangement.

2/ The six countries under review that did not make purchases under the compensatory financing facility during 1981-82 were India, Mauritania, Sierra Leone, Somalia, Togo, and Yugoslavia.

3/ The smallest compensatory financing facility purchase by the countries under review during the period was by Liberia for 13 percent of quota, but Liberia subsequently made a second purchase which raised its total purchases during the period to 63 percent of quota.

the 27 countries under review. Three of these countries had extended arrangements with the Fund (Ivory Coast, Jamaica, and Pakistan), one had a multiyear stand-by arrangement (Thailand) and three had one-year stand-by arrangements (Korea, Mauritius, and Senegal). The amounts approved under the structural adjustment loan ranged from the equivalent of 33 percent of Fund quota (Pakistan) to 132 percent (Ivory Coast), and averaged 74 percent of Fund quota. Average approved access to Fund credit under the concurrent arrangement with the Fund was 253 percent of quota for these seven countries.

III. The Program Countries and the World Economic Environment

The 27 countries that entered into stand-by or extended arrangements with the Fund in 1981 were all developing countries that are net oil importers; 13 of these countries are classified by the World Bank as low-income countries, 1/ and 14 as middle-income countries. 2/ This group of 27 countries is more heavily weighted with low-income countries than the overall group of Fund members that are net oil importers.

In the aggregate, the economic situation of the 27 countries under review had worsened considerably after 1978. The annual rate of output growth declined by an average of 4 percentage points from 1977-78 to 1980, while the rate of inflation (as measured by the increase in consumer prices) rose by 6 percentage points during the same period. The ratio of the external current account deficit to exports of goods and services, which had already increased significantly in 1977-78, rose sharply in 1979 and remained high in 1980 (Table 2).

The deterioration of economic conditions in the countries under review can be related to a significant extent to economic developments in the rest of the world, mainly the slowdown in growth in the industrial

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1/ Low-income countries are countries whose per capita GDP, as estimated by the World Bank, did not exceed the equivalent of US$350 in 1978. The program countries in this group are Burma, the Central African Republic, Ethiopia, India, Madagascar, Mauritania, Pakistan, Senegal, Sierra Leone, Somalia, Togo, Uganda, and Zaire.

2/ Two of the middle-income countries (Korea and Yugoslavia) are major exporters of manufactures. The rest, which export mainly primary commodities, are included in the group designated "other net oil importers"; program countries in this group are Costa Rica, Dominica, Grenada, Ivory Coast, Jamaica, Liberia, Mauritius, Morocco, Romania, the Solomon Islands, Thailand, and Zambia.

countries after 1979 1/, the 1979-80 world oil price increases, and the rise in international interest rates. The quality of domestic economic policies was also an important factor accounting for the deterioration in the economic performance of the countries under review, as described in subsequent sections.

Table 2. Economic Indicators in Program and Industrial Countries, 1977-82

(In percent)

	1977	1978	1979	1980	1981	1982
Program countries						
Rate of growth of output 1/	6.0	6.6	2.2	2.5	4.0	2.9
Rate of inflation (CPI) 1/	10.7	8.0	12.3	16.5	17.3	13.0
Current account deficit/exports of goods and services 2/	12.1	16.5	26.3	26.3	23.0	16.9
Industrial countries						
Rate of growth of real GNP 1/	4.0	4.1	3.4	1.3	1.2	-0.3
Rate of increase of the GNP 1/ deflator	7.5	7.6	8.0	9.0	8.6	7.2
Interest rates (three-month LIBOR in percent per annum)	6.1	8.8	12.1	14.2	16.8	13.2

Source: Fund staff estimates.

1/ Average weighted by GNP in U.S. dollars in 1975. This measure has been used for purposes of comparability with data derived in the World Economic Outlook exercise, which is the source of the information on industrial countries. Averages in other sections of this paper are unweighted arithmetic averages for the countries under review.

2/ Average weighted by contemporaneous exports of goods and services.

1/ For a general discussion of the link between growth in the developing countries and economic activity in the industrial countries, see Goldstein and Khan, Effects of Slowdown in Industrial Countries on Growth in Non-Oil Developing Countries, IMF Occasional Paper, No. 12 (August 1982). This issue is examined empirically in Khan and Knight, "Determinants of the Current Account Balances of Non-Oil Developing Countries in the 1970s: An Empirical Analysis," DM/83/48, 6/28/83.

A flare-up of inflation in 1979 (partly associated with the international oil price increases) had led to a drastic tightening of monetary policy in a number of industrial countries and to a significant slowdown in economic activity. Short-term interest rates, which had begun to rise in 1978, increased sharply in 1979-80, and the rate of output growth in the industrial countries dropped by about 3 percentage points from 1978 to 1980. These developments were associated with sharp movements in the prices of internationally traded goods that resulted on balance in a drastic deterioration in the terms of trade of the countries under review. The terms of trade of these countries as an aggregate fell in each of the years after 1978, particularly following the 1979-80 oil price increases (Table 3). The terms of trade of low-income countries and of middle-income countries exporting mainly commodities (other net oil importers) broadly followed the variations in the price of non-oil primary commodities relative to oil prices over this period. Similarly, the terms of trade of the two exporters of manufactures moved roughly in line with the prices of manufactures relative to the price of oil.

Table 3. Terms of Trade of Program Countries

(Percentage change)

	1977	1978	1979	1980	1981	1982
Terms of trade of program countries	5.2	-0.3	-6.9	-9.0	-6.1	-1.2
Of which:						
Low-income countries	9.3	-1.6	-9.1	-8.2	-6.6	-2.9
Exporters of manufactures	2.8	4.4	-2.7	-10.1	-1.5	2.8
Other net oil importers	4.3	-2.7	-8.3	-8.8	-8.9	-2.8
	(Percentage changes in U.S. dollar terms)					
Memorandum items:						
World trade prices for major commodity groups						
Oil	9.3	0.1	48.7	62.0	10.1	-4.6
Non-oil primary commodities	20.7	-4.7	16.5	9.7	-14.8	-12.1
Manufactures	9.0	14.7	15.3	10.5	-5.1	-2.0
Non-oil primary commodities/oil	10.4	-4.8	-21.7	-32.3	-22.6	-7.9
Manufactures/oil	-0.3	14.6	-22.1	-31.8	-13.8	2.7

Source: Fund staff estimates.

Export market growth (a weighted average of the growth of non-oil import volumes of major trading partners) of the countries under review declined from an average of 6 1/2 percent a year in 1977-79 to less than 4 percent a year in 1980-81 (Table 4). This slowdown was broadly in line with the weakening of non-oil import demand by industrial countries, but with some delay that reflected continuing strong import demand by the oil exporting and non-oil developing countries in 1980-81 after the slowdown in the industrial countries had already begun. A further adverse exogenous shock of importance for the countries under review was the marked increase in international interest rates during 1978-1980. This was reflected in a sharp increase in the ratio of interest payments to exports after 1977, and an associated rise in the debt service ratio. The higher interest rates affected the middle-income program countries most severely; their interest payments increased from around 6 percent of exports in 1977 to 13-15 percent in 1982. The interest payments ratio for the low-income countries grew more moderately, rising from 7 percent to 8 1/2 percent over the same period, owing to the much smaller proportion of the debt of such countries that bear market-related interest rates. The countries under review were also adversely affected by the generally slow growth of concessional aid flows during much of this period and the decline in such flows after 1981.

Table 4. Export Market Growth of Program Countries

	1977	1978	1979	1980	1981	1982
			(Percentage changes in volume)			
Export market growth	6.1	7.5	6.1	3.7	3.8	-0.3
Non-oil imports of industrial countries	4.0	7.3	8.9	1.2	-0.1	1.2
Imports of oil exporting countries	16.0	4.8	-12.3	15.3	19.9	5.1
Imports of non-oil developing countries	7.2	8.5	10.3	4.7	2.6	-7.7

Source: Fund staff estimates.

IV. External Imbalances of Program Countries 1/

1. Indications of external imbalance

All of the countries under review exhibited balance of payments positions during the year preceding the program which were not viable in the medium to long run. In most cases the external current account deficit was clearly too large to be sustainable in light of the level of indebtedness, productive capacity and export prospects, and the likely ability to obtain capital inflows. There were also several instances in which the level of imports associated with a sustainable external current account deficit was insufficient to enable economic growth to be maintained at a satisfactory level; nevertheless, the country was unable to attract adequate foreign capital to finance a larger deficit. In many cases, short-term pressures had also emerged that resulted in a depletion of international reserves and/or an intensification of trade and payments restrictions (often an accumulation of external payments arrears). Several countries had had recourse to large-scale commercial borrowings beyond prudent limits or had obtained exceptional ad hoc external financing to finance the deficit. 2/ The external imbalances were often accompanied by high inflation and low or negative real economic growth. Although the adjustment process had already begun in a number of the countries under review, frequently in conjunction with a previous arrangement for use of Fund resources, 3/ a considerable amount of adjustment generally needed to be accomplished at the beginning of the 1981 arrangement. This reflected, inter alia, the additional need for adjustment imposed by adverse exogenous developments (e.g., the 1979-80 oil price increase, the prolonged period of slow growth in the industrial countries), and the lack of adequate policy change or limited success rate of adjustment measures included in programs initiated during the preceding period (see EBS/82/97, 6/9/82, pages 25-27).

1/ A more detailed survey of developments under adjustment programs adopted by certain of the countries under review is provided in Zulu and Nsouli, "Adjustment Programs in Africa: The Recent Experience, 1980-81," (DM/83/54, 7/13/83).

2/ Exceptional external financing is often difficult to distinguish from other borrowings and is frequently not identified separately in balance of payments statistics.

3/ See Section II, p. 5.

The severity of balance of payments difficulties varied considerably among the countries under review. 1/ Foreign exchange crises during the years prior to the program had resulted in the abrupt imposition of extensive trade and exchange controls and/or the accumulation of substantial arrears in several countries. Direct controls had been imposed in this manner in five cases (Costa Rica, Jamaica, Somalia, Uganda, and Zambia). An accumulation of arrears had taken place in 12 countries, the amounts ranging from the equivalent of 8 percent of Fund quota (Senegal) to 460 percent of quota (Costa Rica). More moderate balance of payments difficulties, generally involving a prospective financing gap and/or a substantial loss of reserves, had developed in the other 15 countries under review. In most cases, balance of payments difficulties had been in existence for three years or more prior to the arrangement.

Balance of payments difficulties were often compounded by an inadequate level of international reserves, which in several cases reflected delayed policy adjustment and the previous financing of an excessively large external current account deficit. Thirteen of the 27 countries under review held reserves at the beginning of the program period that were equivalent to five or fewer weeks of imports, and another four countries held reserves that were less than the equivalent of ten weeks of imports. 2/ In seven countries, the cumulative decline in gross reserves during the period 1978-80 exceeded the equivalent of five weeks of imports. The very low level of reserves clearly implied a vulnerability to even minor and temporary adverse developments, particularly in light of the excessively high level of short-term debt in several countries. In some cases the low level of reserves raised doubts, both domestically and in the world financial community, whether the economic policy mix was appropriate to maintain a viable external position.

1/ During the year prior to the initiation of the adjustment program, the ratio of the overall balance of payments deficit to Fund quota was 150 percent on average for the countries under review, reflecting 6 cases of surplus and 21 of deficit. However, this indicator may understate the severity of balance of payments difficulties because some countries were in such a difficult position that they were unable to finance the imbalance through an overall reserve loss and instead limited the amount of outflows by imposing or intensifying exchange and trade restrictions or accumulating external payments arrears.

2/ The appropriate level of gross or usable international reserves would vary considerably among the countries under review. In most of these cases, it could be argued that reserves equivalent to ten weeks of imports would probably not be considered an adequate or comfortable level.

2. Problems underlying balance of payments difficulties

An unsustainable external imbalance implies a corresponding inequality between domestic supply and demand that cannot be financed by normal capital inflows. The origins of such a disequilibrium are sometimes extremely difficult to identify. In some cases, it is possible to attribute the emergence of an imbalance primarily to an upsurge in demand (or maintenance of demand at levels that are too high in light of altered circumstances) or primarily to an inadequate response of supply. However, problems in one area often give rise to difficulties in the other, and it may be difficult to ascertain the original cause of an imbalance. For example, although the existence of excess capacity is a clear indication of supply problems, they may have emerged as a result of difficulties in obtaining imported inputs under a system of exchange and trade controls imposed to deal with a problem of excessive demand.

a. Problems of excessive demand

Excessive demand frequently emerged when expenditure levels were not reduced or declined too slowly after exogenous developments that called for adjustment. In several of the cases under review, public and private income and expenditures had expanded in response to the commodity booms of the early and mid-1970s. When commodity prices weakened demand was not reduced sufficiently, resulting in unmanageable budget and external current account deficits. 1/ Problems of excessive demand sometimes developed after exogenous shocks such as climatic disasters, crop failure, civil and military disturbances, or a decline in export demand associated with the world recession. The imbalances arising from such causes were sometimes so large that it became necessary to reduce rather than merely finance the disequilibria, even though they may have seemed temporary.

Excessive demand also developed as the unforeseen consequence of a deliberate policy to stimulate general economic activity or a particular sector, or to enlarge public sector participation in economic activity (e.g., Costa Rica, Jamaica, and Thailand). It also sometimes arose during periods of political disruption or of changes in leadership when control over public spending was less strict than during other periods (e.g., Liberia and Uganda).

Situations of excessive demand were often accompanied by structural problems. For example, the policy response to the 1979-80 oil price increase was inordinately slow in a number of countries; expenditure levels were not adjusted adequately, and in many cases domestic energy prices were not increased sufficiently, leading to both excessive

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1/ This pattern was exhibited by Costa Rica and the Ivory Coast (coffee), Morocco and Togo (phosphate), Mauritius (sugar), Liberia (iron ore), and Zambia (copper and cobalt).

demand and an inappropriate structure of relative prices. Inappropriate measures adopted to deal with severe problems of excessive demand sometimes had an adverse effect on supply conditions. For example, in Costa Rica, Jamaica, Somalia, Uganda, and Zambia, controls aimed at containing demand had led to an inappropriate structure of relative prices and adversely affected the allocation of resources. In some cases the problem of excessive demand was exacerbated by an inappropriate allocation of spending between consumption and investment as well as the poor quality of certain investments (e.g., the Central African Republic, Ivory Coast, and Sierra Leone).

Countries in situations of excessive demand were commonly characterized by large fiscal deficits which resulted in high rates of credit growth to the public sector and/or large external borrowings. In some but not all cases there was an acceleration in inflation accompanied by a real appreciation of the currency. In several instances, these developments contributed to other problems, e.g., a crowding out of the private sector owing to appropriation by the government of scarce real and financial resources, difficulties in servicing external debt, and a loss of competitiveness and consequent slowing of export growth.

b. Problems of supply

The countries under review faced multiple supply-side problems, many of which required detailed attention at the microeconomic policy level. Such problems may be described as the inability of the domestic productive sector to supply and export goods and services consistent with the full potential of the economy, defined in terms of the resource base and technological capabilities. 1/ The two basic categories of supply problems that were addressed in adjustment programs were the inefficient use of available resources (i) among the sectors of an economy; and (ii) with regard to intertemporal allocation (e.g., the level of consumption relative to investment and savings). In a number of instances, policy weaknesses in a particular area had contributed to supply difficulties in both categories (e.g., the underdevelopment or disfunction of financial intermediation or of the exchange system).

Resource misallocation among sectors stemmed from many causes. Inadequate infrastructure, high levels of tariff protection (usually intended to promote import substitution), and other tax and pricing policies had sometimes contributed to the development of export sectors characterized by an inadequate resource base, virtually no diversification, and unacceptably low rates of growth. In several countries, taxation, subsidy and pricing policies, combined with inefficient public management of many of the means of production, had led to a

1/ Supply-side policies were defined in a staff paper on "Supply-Oriented Adjustment Policies," (SM/81/78, 4/6/81), as "measures designed to increase directly the incentive or ability of the domestic productive sector to supply real goods and services at a given level of aggregate nominal domestic demand."

level of aggregate supply that was well below the potential of the economy (e.g., India, Jamaica, Korea, Morocco, and Pakistan). Continued dependence upon one or two export products had made some countries inordinately vulnerable to changes in external market conditions for one or a few commodities, (e.g., Mauritius (sugar), Senegal (groundnuts), and Zambia (copper and cobalt)). Finally, real wage increases in excess of productivity growth in key sectors had impaired profitability or external competitiveness in a large number of cases, thus lowering production and reducing future output potential as a result of the associated disincentives to investment. 1/

Most of the countries under review were at a stage of development in which they could benefit significantly from further expansion of the capital stock, but some faced special circumstances which necessitated an immediate and substantial redirection or strengthening of the investment effort. There were two cases (Dominica and Grenada) in which hurricane damage had resulted in the need for a massive rebuilding effort. In many instances, the policies or exogenous events which made sectoral reallocation of resources necessary also required a reorientation and increase in investment. In India and Pakistan, reorientation of investment was expected to facilitate an increased level of participation in world trade and a corresponding increase in welfare. In several instances, the level of investment was too large to be consistent with the absorptive capacity of the economy, and some reduction and reorientation was necessary (e.g., Ivory Coast, Liberia, and Togo).

The goal of higher investment generally made the achievement of higher domestic savings an important objective, often because concessional aid flows were stagnant or falling. Low levels of domestic savings tended to affect investment adversely owing to the associated need to adjust expenditure to the availability of resources. Because creditworthiness is closely related to overall macroeconomic indicators, the inadequacy of savings also tended to raise capital costs and limit commercial borrowing opportunities (e.g., Jamaica).

The financial system was the locus of a broad array of structural problems. Inadequate intermediation, which hinders both savings and investment and directly reduces growth prospects, occurred in several cases where the amount or quality of financial services was low due to undeveloped banking services (e.g., Dominica), inadequate or negative real interest rates (e.g., Dominica, Jamaica, and Thailand), or extensive sectoral credit allocation requirements (e.g., Korea and Mauritius).

In several of the countries under review, the longstanding use of an extensive network of exchange and trade controls to constrain imports

1/ Relatively high wage increases were a problem in Costa Rica, Dominica, Jamaica, Korea, Mauritius, Morocco, Romania, Thailand, and Yugoslavia. Excessive wage growth generally arose due to widespread indexation of wages, labor militancy, or direct government policy.

to levels that could be financed had resulted in the emergence of inappropriate incentives to producers, and a reduction in the contribution of international trade to growth and welfare (e.g., Burma, India, Jamaica, Pakistan, Romania, and Uganda). When controls were used as an alternative to needed exchange rate action, export profitability suffered, thereby reinforcing the shortage of foreign exchange and unduly limiting the potential for economic growth. Administrative delays associated with these schemes also led in several instances to shortages of necessary inputs and consequent production problems.

V. Adjustment Objectives and Strategies

Fund resources are used to support adjustment programs that have as their primary objective the achievement of a viable balance of payments position. Such programs also generally aim at reducing inflation and establishing improved conditions for economic growth. In selecting an adjustment strategy to achieve these objectives in the cases under review, the causes of existing external and internal imbalances had to be identified and a view taken as to the balance of payments position that would be sustainable and appropriate in the circumstances of the individual member country. To this end, the current and projected level and composition of expenditure had to be compared with current and potential productive capacity, taking into account the consequences of the level and terms of indebtedness. 1/ On this basis, an appropriate path for domestic expenditure and the external current account deficit was to be derived.

Although precise estimates of such future trends are not feasible, judgments about the sustainable level of the external current account deficit necessarily influence the formulation of adjustment programs. For example, among the countries under review, relatively large reductions in the external current account deficit were considered to be necessary to reach a sustainable position in some cases (e.g., the Central African Republic, Dominica, Madagascar, Mauritius, Senegal, and Somalia) while in others (e.g., Ethiopia, Pakistan, and Thailand) a smaller decrease was deemed appropriate. Current account reductions were not considered to be necessary for all countries; in several cases (e.g., Burma and India), an increase in the deficit was believed to be both feasible and desirable as part of the process of increasing domestic production and the involvement of the country in international trade. In most of these cases the programmed initial increase in the deficit was to reflect higher imports of essential inputs and investment goods (often in conjunction with a liberalization of exchange and trade restrictions) that were expected to lead to a stronger balance of payments, not always within the period of the arrangement, but certainly over the medium term.

1/ A more complete discussion of factors affecting sustainability of the balance of payments is found in "Adjustment Programs - Broad Design and Key Indicators," (EBS/82/98, 6/9/82).

Once a judgment about a sustainable position has been made, the desirable speed of adjustment must be selected, combining policy changes and financing in such a way as to balance the costs and benefits of prompt action against those of delay. The programs under review typically envisaged a multiyear framework for adjustment, even in many cases in which a one-year arrangement was approved. In general, early policy action was stressed so as to hasten the rebuilding of confidence, both internally and externally, and avoid any further deterioration in the underlying situation. Early action was especially important for those policies that influence the balance of payments only after some time lag, so as to ensure that the benefits of the policy change would not be unduly delayed.

The strategies that were adopted to move the economy toward balance of payments viability varied according to the policy problems that had given rise to the existing payments imbalance. Nine of the 27 countries under review (the Central African Republic, Costa Rica, Ethiopia, Liberia, Madagascar, Senegal, the Solomon Islands, Thailand, and Togo), faced balance of payments difficulties mainly because demand was excessive when compared with available resources. 1/ The adjustment strategy in these cases accordingly aimed at restoration of external and internal balance mainly through the tightening of demand management policies. For these "demand restraint" programs structural policy measures were of secondary importance and were usually limited to the correction of relatively minor distortions in pricing and trade policies. Lower credit growth and the reduction of government claims on financial resources were the policy instruments most commonly employed in such programs. The restoration of balance of payments viability was commonly expected to be reflected in an improved current account position in the short term; an average reduction of about 1 1/2 percentage points was targeted in the ratio of the external current account deficit to GDP during the first program year (Table 5). An adequate reserve level was typically an objective of the program; reserves were equivalent to less than five weeks of imports in three of the nine cases at the outset of the arrangement. The targeted reserve movement varied from an expected decline equivalent to five weeks of imports in the case of the Solomon Islands to a targeted increase of five or more weeks for several countries in this category; on average reserves were expected to be approximately maintained as a proportion of imports. In the six cases where external payment arrears had emerged, the overall balance of

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1/ It should be emphasized that balance of payments problems stem from many causes, including in any individual case factors that may be identified as related to excessive demand and also problems stemming from supply difficulties. A successful adjustment strategy would incorporate elements designed to address both sources of problems. The distinction drawn between types of adjustment strategies is based on the relative importance of different sources of disequilibria and is therefore judgmental to some extent.

payments target was consistent with their reduction and eventual elimination. In none of the cases under review was the total elimination of arrears expected during the first program year.

Table 5. Targeted Developments in Selected Indicators for Program Countries 1/

(In percent)

	Demand Restraint Programs	Supply Oriented Programs	Mixed Strategy Programs
Ratio of external current account balance to GDP 2/			
Prior year	-15.2	-4.1	-12.4
Target	-13.6	-4.3	-12.8
International reserves 3/ (weeks of imports)			
Prior year	10.0	11.9	6.7
Target	9.9	10.8	6.3
Real growth rate			
Prior year	0.7	5.3	-0.2
Target	4.2	5.2	3.7
Rate of inflation 4/			
Prior year	14.8	16.2	26.0
Target	12.3	14.7	18.2

Source: Staff estimates.

1/ This table presents arithmetic averages of selected variables for all of the programs for which data are available.
2/ Excludes Dominica and Grenada.
3/ Reserve data refer to the end of the indicated period.
4/ Excludes Costa Rica and Uganda.

In eight countries (Burma, Dominica, Grenada, India, Korea, Pakistan, Romania, and Zaire), balance of payments difficulties were seen to have arisen primarily, though not necessarily exclusively, because of the inadequate growth of supply due to structural inadequacies. Adjustment programs were therefore oriented mainly toward correction of structural weaknesses. In these "structurally oriented" cases, the policies adopted aimed mainly at an improved investment and savings performance and a sectoral reallocation of resources, rather than at the restraint of demand. Policy changes were intended to improve growth and export prospects and to strengthen the capacity to service debt, thereby contributing to balance of payments viability. In four of these cases, inadequate past investment or damage from natural disasters required a large investment effort (Burma, Dominica, Grenada, and India). In six instances, a reallocation of resources among sectors was envisaged as a way to boost the value of tradable goods production (Burma, India, Korea, Pakistan, Romania, and Zaire). When the protection of local producers had led to a severe sectoral misallocation of resources, as in the cases of Burma, India, and Pakistan, a liberalization of the exchange and trade system was planned to improve the structure of incentives and promote greater efficiency. Increased investment and imports were expected in several cases to lead to quite large external deficits in the short term; in Dominica and Grenada, current deficits equivalent to over 25 percent of GDP were targeted to help repair hurricane damage and begin ambitious development programs. 1/ For the other six cases, little change was expected on average in the external current account balance as a percentage of GDP during the program period. Inflation targets varied from case to case, reflecting the relative importance of adjustment of pricing policies and taxes, which were often expected to have a substantial one-time effect on the price level.

For the remaining ten countries under review (Ivory Coast, Jamaica, Mauritania, Mauritius, Morocco, Sierra Leone, Somalia, Uganda, Yugoslavia, and Zambia) imbalances were attributable to problems of both excessive demand and inadequate supply and adjustment programs accordingly placed about equal emphasis on demand restraint and structural adjustment. The adjustment programs in these cases of "mixed" strategy were more complex and the objectives more heterogeneous. The need for demand restraint coincided in the cases of Jamaica and Uganda with the intention to reduce the role of the public sector in the economy; in Jamaica, with the need to reallocate resources away from the protected import-competing sector; and in the Ivory Coast, Mauritania, Mauritius, and Zambia, with the need to diversify the export sector. The multiplicity of objectives does not lend itself well to generalization except that in these cases the composition of expenditure, both at the government level and for the economy as a whole, was more the focus in the short run than the overall government deficit or external current account balance.

Several of the countries adopting such a mixed strategy were cases in which excessive demand had contributed to a shortage of foreign exchange that had led to the imposition of extensive trade and exchange

1/ For Dominica, this represented a decline from an even larger deficit in the prior year when unusually large capital inflows were registered, including substantial emergency aid.

controls. In several instances, the system of controls had in turn caused other more serious structural problems. The adjustment program for most of these countries included elements of demand restraint along with a reform of the trade and exchange system intended to revive the external sector, eliminate distortions, and restore confidence. Liberalization of controls was accompanied in some cases by a relatively large devaluation aimed at reduction of the foreign exchange shortage. Since an immediate elimination of the shortage was often difficult, a smaller devaluation was sometimes accompanied by the replacement of quantitative controls with tariffs or by the temporary establishment of a parallel exchange market. Such schemes implied a slower adjustment process than would have been associated with the alternative of a more drastic devaluation, but this was considered necessary in order to mitigate the economic and social disruption that might have resulted from more rapid relative price change. Such schemes also permitted the partial restoration of the price mechanism in the external sector and a diminution of administrative discretion which at times had proved to be arbitrary and had led to misallocation of resources.

In cases of this sort, the objectives of adjustment programs differed substantially from those of simpler cases of demand restraint. For example, when the overall level of imports had been severely constrained by quantitative barriers and the composition of imports distorted, a period of higher imports was typically necessary to overcome production bottlenecks and redress sectoral misallocations. In such cases, a higher current account deficit was sometimes targeted. At the same time, measures were generally taken to lower government deficits and diminish credit growth in order to reduce underlying aggregate demand to levels consistent with a sustainable balance of payments. In some cases, the program also envisaged an increase in the officially measured rate of inflation; such an increase generally occurred in situations in which domestic price controls had repressed prices of a number of commodities during the period of the foreign exchange shortage.

VI. Policy Content of Programs

1. Demand-management policies

As noted in the preceding section, objectives and adjustment strategies showed wide variation among programs, a diversity that was reflected in the relative importance attached to different policy instruments in adjustment programs. When excessive demand was the primary source of external and internal imbalance, adjustment programs were composed mainly of measures to restrain aggregate demand to levels compatible with the availability of resources. Even those programs with the most pronounced structural orientation generally included at least some actions aimed at containing domestic demand, although these were not the primary focus of policies in such cases.

a. Fiscal policies

In most cases the thrust of fiscal policies was directed toward reducing the disequilibrium in public sector finances. With the exceptions of the supply oriented programs of Burma, Grenada, Romania, and Zaire and the demand restraint program of the Solomon Islands, all of the cases under review targeted a reduction in the ratio of the budget deficit to GDP (Table 6). Even in those programs in which an increase in the budget deficit was projected, specific measures were generally to be taken to raise revenues and/or reduce some categories of outlays. The targets for the overall fiscal deficit as a percent of GDP were not met in a majority of the countries under review, although the deviation from the target was not large in most programs. 1/ However, a substantially higher ratio of the government deficit to GDP than targeted was registered in several cases (e.g., Costa Rica, Liberia, Madagascar, Morocco, Togo, and Zambia).

Almost all of the programs under review envisaged some increase in budgetary revenue, in most cases by a significant amount (the average projected increase was almost 20 percent). The sole exception was Romania, where the absence of planned revenue increases (and expenditure cuts) reflected not only stabilization objectives but also a shift of expenditure responsibilities from the budget to enterprises. This was to some extent attributable to the projected growth of nominal income, but in 19 cases the impact of discretionary measures to increase revenue was expected to be a major contributing factor. Higher indirect tax rates (usually import duties or domestic sales taxes), increases in prices of goods sold by the government, or lower transfers to public enterprises were the most common policy changes. Higher taxation of petroleum and other energy products was also frequently intended. Even though some changes in tax policy were required prior actions in 11 arrangements, revenue raising measures were implemented fully in accordance with plans in only 5 programs. In these cases the revenue targets were either surpassed or met, with the exception of the first year of the Ivory Coast extended arrangement, when the fall in coffee and cocoa prices had a negative influence on government receipts. There were substantial shortfalls in government revenues from the program projections in 13 of the 27 programs under review, frequently as a result of incorrect projections of underlying macroeconomic variables (e.g., economic growth, and export and import values). Not surprisingly, those countries in which implementation of programmed revenue measures was the most limited (the Central African Republic, Grenada, and Sierra Leone) were among those with severe revenue shortfalls.

1/ In several instances absolute magnitudes of the deficit were close to targeted levels, but a lower than projected growth of nominal GDP meant that the target for the overall deficit as a percent of GDP was not achieved.

Table 6. Targeted and Actual Developments in Credit and Public Sector Balance Ratios 1/

(In percent)

	Demand Restraint Programs	Supply Oriented Programs	Mixed Strategy Programs
Overall credit growth ratio 2/			
Prior year	23.3	25.5	33.5
Target	25.8	22.7	27.4
Actual	26.9	20.9	30.1
Public sector credit growth ratio 2/			
Prior year	11.7	8.8	26.3
Target	13.3	12.3	17.6
Actual	15.5	14.3	22.7
Ratio of government overall balance to GDP			
Prior year	-8.7	-6.1	-10.4
Target	-6.3	-7.5	-8.0
Actual	-8.4	-7.0	-9.5

Source: Staff estimates.

1/ This table presents arithmetic averages of selected variables for all of the programs for which data are available.
2/ Absolute change in credit outstanding relative to stock of broad money at beginning of period. Overall credit excludes Uganda.

Even though specific actions to reduce the growth of public sector outlays were to be an integral part of demand-management efforts in 20 programs, in only very few instances (Ivory Coast, Madagascar, Mauritania, Mauritius, Romania, and Zambia) was the required degree of restraint such that a reduction in real levels of spending was planned. Cuts in nonwage current outlays (often to be achieved through lower transfers to nonfinancial public enterprises) and a reduced rate of growth in wages were the most common measures planned. Reductions in the public investment program were less frequent although it was decided not to introduce new projects in several cases. Of the 12 annual programs in which total government expenditures were projected to rise by more than 15 percent, one half belonged to the structurally oriented group. Only three arrangements (Costa Rica, Sierra Leone, and the

Solomon Islands) having demand management as the main orientation provided for a comparable increase in public sector outlays. In general, aggregate expenditure targets were met reasonably well, with the growth of public sector outlays exceeding the targeted growth rate by more than 10 percentage points in only two instances (Morocco and Zaire).

In summary it appears that fiscal adjustment in the programs under review relied on a more balanced approach of both raising revenue and slowing the growth of expenditures than the arrangements covered in last year's review, where fiscal improvements were expected mainly from reductions in expenditure. 1/ Although the spending targets were met to a reasonable extent, revenues fell considerably short of expectations. This frequently reflected incorrect assumptions about economic growth or adverse developments outside the control of the authorities (e.g., lower than expected export growth), but also resulted in some cases from the delayed or incomplete implementation of programmed revenue measures. However, although it might be expected that such events would also create pressures for additional government expenditures in some areas, they did not result in substantial departures from planned expenditure levels. Because there is a general tendency for revenue targets to be set conservatively, the results indicate that it may be easier to reduce the growth of government spending to conform to changing circumstances than it is to raise government revenues significantly within a given fiscal year.

b. Other demand-management policies

A number of other types of measures were frequently to be employed to reduce the level of aggregate demand. With a view to reducing consumption and improving the public sector financial performance, tariffs charged by nonfinancial public enterprises (NPEs) were to be raised in 15 programs. In a number of cases these price changes were essential because the imbalances of public enterprise finances were a major drain on budgetary resources (e.g., Burma, Senegal, and Zambia), or because there was considerable potential otherwise for mobilizing resources from this sector (e.g., India). Hence measures to raise NPE tariffs were also frequently stipulated as prior actions to be implemented before formal consideration of the request for use of Fund resources (see discussion in Section VII). Twelve programs contained higher interest rates as part of the policy package, although in most the primary purpose of the increase was not so much to control aggregate demand as to reduce financial repression and improve resource allocation. In addition, several programs contained other demand restraining measures such as general wage restraint (e.g., Dominica, Ethiopia, Senegal, and Uganda). As the policies to raise interest rates and NPE

1/ EBS/82/97 (6/9/82), p. 13. See also a recent detailed study of fiscal adjustment under arrangements approved in 1980, Lubin K. Doe, "Fiscal Policy and Adjustment in the 1980 Fund Financial Programs," DM/83/52, 6/30/83, p. 8.

tariffs often involved once and for all type actions which do not involve major difficulties in implementation, and were in any case frequently specified as prior actions, they tended to be implemented to at least a moderate degree. The same was true for the other policies in this group. There were a few notable exceptions to this general pattern (e.g., Costa Rica, Sierra Leone, Zaire, and the third-year program for Jamaica), where the degree of implementation was limited.

A noteworthy feature of the programs under review is the infrequent reliance on restraint of the growth of private sector credit. Measures aimed specifically at limiting the expansion of credit to the nongovernment sector were used in only seven programs; in all of these the degree of restraint was rather moderate. In a large number of cases, program design was apparently based on the view that the public sector was a principal source of the imbalances in the economy. Accordingly, policies were formulated with primary emphasis on overcoming weaknesses in this area. Sometimes in connection with this effort, but often also independently, the relative prices in the economy were to be changed in a manner which tended to reduce real private consumption (e.g., tax increases, cuts in subsidies, interest rate policy, etc.), thereby reducing the overall domestic financial imbalances. The use of overall credit ceilings as performance criteria in programs (which together with a subceiling on government credit implies a limit on private sector credit) was apparently intended mainly to be a mechanism for monitoring the evolution of the economy during the program period, rather than as a means to control private expenditures; the implicit limit involved with such a ceiling often provided for some acceleration of private sector credit in the programs under review. 1/

2. Structural policies

For purposes of analysis structural adjustment policies may be classified into three main categories: those to expand production of tradable goods, those intended to augment growth of potential output, and those with other objectives. In general any policy action tends to have a number of functions and a precise classification of these as primary or secondary is often not possible. The following discussion of the various structural measures used in the programs under review illustrates the diversity of approaches to solving structural problems facing member countries.

a. Policies to expand production of tradable goods

Policies to expand production of tradable goods can be further subdivided into those that directly improve the competitiveness of domestically produced goods (i.e., exchange rate actions and containment of costs), and those that otherwise seek to provide adequate incentives

1/ Actual developments in the major monetary aggregates that were subject to performance criteria are reviewed in Section VII.

for domestic production (e.g., increases in producer prices). A depreciation of the currency was frequently an integral part of the policy package adopted by the countries under review. About one half of the 27 programs explicitly included an adjustment of the exchange rate either as a prior action or as a measure to be taken during the program period. By comparison exchange rate actions were included in about one third of the core group of programs covered in the last review paper (EBS/82/97, 6/9/82) and about one half of the 1978-79 stand-by arrangements reviewed in EBS/81/52 (7/14/81).

The use of the exchange rate as a principal policy instrument was most common in countries following a structurally oriented or mixed adjustment strategy; exchange rate actions were taken less frequently in pure demand-management programs, with only three out of nine such arrangements containing a depreciation (see Appendix C). Four of the programs approved in 1981 that contained a currency depreciation were part of a structurally oriented adjustment strategy, and the change in the exchange rate in these programs was aimed at solving specific structural problems. None of the programs designed around large investment efforts (Burma, Dominica, Grenada, India, and Pakistan) contained a large initial exchange rate change, although some additional flexibility in managing the exchange rate or some subsequent adjustment was involved in several of these cases. In contrast, all of those predominantly structural programs whose main strategy was to effect a shift of resources between sectors (i.e., Jamaica, Korea, Romania, and Zaire) relied to some extent on exchange rate adjustment to help achieve program objectives. Currency depreciation was used in all but two (Ivory Coast and Zambia) of the programs in the mixed strategy group. Implementation of the intended exchange rate action was less than envisaged in several cases, but in only two instances (Costa Rica and Mauritania) did the adopted policy changes fall far short of the stated intentions.

Six programs included a general policy of wage restraint as a means to improve competitiveness as opposed to being primarily a part of demand-management efforts. In most cases (Dominica and Mauritania being the only exceptions) where wage restraint was part of the policy program, it was coupled with exchange rate depreciation for maximum effect. Increases in agricultural producer prices were another frequent component of structural policies; eight programs containing significant efforts in this area had a very good record of implementation.

b. Policies to augment growth of potential output and improve efficiency

Higher and more efficient investment is perhaps the most obvious means of raising the potential output of the economy. Four of the programs under review had a large-scale public sector investment effort as the central element of their adjustment strategy. Investment policies, often elaborated with the assistance of the IBRD, were also an important aspect of other programs; 18 of the cases under review contained significant measures in this area. Ten of these envisaged an increase in the nominal value of capital formation during the program period. Implementation of investment policies tended to be somewhat disappointing when compared with other measures as most countries had only moderate or limited success in this respect. For a number of countries this reflected in part changes in external circumstances during the program period (e.g., Senegal, Sierra Leone, and Zaire). Since investment plans require a given level of resources and can be carried out only over a considerable period of time, their implementation was often adversely affected by reductions in resource availability during the program period.

Policies to improve the functioning of the financial system to promote savings and hence expand the scope for capital formation were a feature of eight programs. In general the magnitude of planned increases in administratively controlled interest rates as well as other measures in this category were rather moderate. The effectiveness of these policies was often further impaired by a less than complete implementation of planned policy changes.

The role of policies to liberalize and rationalize the trade and payments system appears to have been relatively more prominent in programs approved in 1981 than in those covered in past reviews. In some programs (e.g., Burma, Pakistan, and Romania) changes in the form or intensity of exchange and trade controls were central to the adjustment strategy of the country in question. In other cases (e.g., India and Somalia) the role of such measures was less central but still an important part of the overall policy package. Such measures were of relatively minor importance in several other instances (e.g., Thailand). The most frequently specified policies in this area included liberalization of imports (e.g., Burma, Pakistan, and India) and rationalization of the exchange system through simplification of multiple exchange rate systems, usually in connection with a devaluation of the currency (e.g., Jamaica, Romania, Somalia, and Uganda).

c. External debt policies

The external debt service burden posed a significant constraint on policy formulation in several of the countries under review. 1/

1/ The ratio of debt service payments to exports of goods and services exceeded 25 percent in the year prior to the program in ten cases and generally showed a rising trend among most of the countries under review. Although this ratio is not entirely satisfactory as a measure of the debt service burden (e.g., because interest on short-term debt is often excluded and because there are sometimes other reliable sources of foreign exchange earnings such as worker remittances), difficulties involving debt service are common and in several cases have intensified among the countries under review.

Accordingly, efforts were made to alter the composition of external debt toward more reliance on loans with concessional terms and to limit recourse to new borrowing from nonconcessional sources. Several countries implemented new procedures for the monitoring and control of new external borrowing commitments, and the planned reduction in the overall public sector deficit was often associated with an expected decline in overseas borrowing on nonconcessional terms.

Rescheduling of external debt was envisaged at the time the adjustment program was elaborated in 12 of the 27 programs under review (see Appendix D). The rescheduling included only official debt in six cases and involved both official and commercial debt in five other instances; nine of the negotiations involving official debt were undertaken on a multilateral basis and two were undertaken on a bilateral basis. Rescheduling included only commercial debt in the remaining case. The amount of official debt service payments that was postponed ranged from 2 percent of total outstanding debt in the case of Pakistan to 44 percent for the Central African Republic. As a percentage of the external current account deficit, it varied from 13 percent in the case of Uganda to 189 percent in the case of Togo. The actual amount of debt service payments postponed fell considerably short of expectations only in the cases of Pakistan and the Central African Republic. For all of the other countries under review the amount and terms of the rescheduling were broadly in accordance with what was expected at the time the adjustment program was formulated. 1/

d. Other policies

The structural elements of the programs under review also included other policies, often dealing with specific problems and tailored individually to the institutional arrangements of the country in question. Energy conservation policies were an important element of most of the programs under review; domestic petroleum product prices were expected to remain significantly below import cost in only two cases (Burma and Romania). The maintenance of domestic energy prices at levels in excess of import cost (in many cases through the imposition of taxes on petroleum and other energy products) was a component of policy in most countries and energy price increases were explicitly included in a number of programs (e.g., Costa Rica, Dominica, Liberia, Mauritius, Morocco, Pakistan, Senegal, and Sierra Leone). In Senegal, administrative units were created to rationalize policymaking in several key areas, including budgetary control, wage policy, and economic and financial coordination.

1/ A suggested approach for cases in which debt rescheduling is envisaged is outlined in "Fund Policies and External Debt Servicing Problems," SM/83/45, 3/8/83, pp. 26-28.

VII. Monitoring of Policy Implementation--Prior Actions and Performance Criteria

1. Prior actions 1/

In committing its resources to support the adjustment efforts of members, the Fund needs to be assured that the adjustment program is being implemented as fully as possible. Actions taken before the request for the arrangement can serve to demonstrate that policies are in place which are likely to result in the achievement of program objectives. In particular, actions that imply a basic change in the direction of economic policy and that would require separate decisions to be reversed or voided are suitable for this purpose. Adjustments of the exchange rate, interest rates, the cost of energy, and prices of widely used consumer goods generally fall into this category as would significant institutional changes such as the removal of restrictions, multiple currency practices, or price controls. Introduction of new taxes or modification of existing rates of taxation are also examples of this type of change.

Prior actions were an important component of the policy package in most of the upper credit tranche arrangements approved in 1981. In only one instance (Togo) was a program approved without an understanding that significant prior policy changes would be made. In two other cases (Morocco and Pakistan), the 1981 programs replaced previous extended arrangements for technical reasons; although the identification of prior actions is difficult in these cases, implementation of a number of policy changes preceded the approval of the new arrangement. In the case of India, the government budget contained important pricing policy changes and other adjustment measures that were clearly necessary before the arrangement could be approved, but was passed well in advance of the major negotiations.

The most frequent prior actions in the countries under review were those relating to the tax system; 11 programs included the introduction of new taxes and/or a change in existing tax rates or coverage. Prior changes were also frequently stipulated in expenditure policies and public enterprise tariffs, frequently in the form of measures to reduce or eliminate subsidies and price distortions. The prevalence of prior actions related to public finance is perhaps to be expected, since typically final negotiations on programs cannot be concluded before the

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1/ It is not clear how long before approval of the program a policy measure can be taken and still be called a prior action. Generally, this paper has defined prior actions to include all policy measures of the kind described that were taken between the start of negotiations and final approval of the program. However, with the often continuous contacts between the authorities and the staff, pinpointing the start of negotiations may not always be without an element of arbitrariness as well.

government budget is known in some detail and hence measures taken within the budget often are implemented in advance of the formal approval of the program. A depreciation of the currency preceded approval of eight programs in 1981 with the magnitude of the change ranging up to 90 percent (in domestic currency terms). Other frequent prior actions were measures relating to interest rates, producer prices, and liberalization of the exchange and trade system.

2. Performance criteria

Even with the strongest possible measures taken before program inception, the general thrust of policies can always be altered or made inappropriate by offsetting changes in other policy variables or by unforeseen exogenous developments. For example, currency depreciation may be partly offset by an export tax and import subsidy, and one kind of tax increase can be neutralized by a tax reduction elsewhere. Similarly, an unanticipated decline in export volumes or other adverse development affecting assumptions underlying the design of the program may mean that the initial policy stance is no longer sufficient to achieve the planned objectives. In addition, some types of policies (e.g., expenditure control) are by nature subject to frequent review. There is therefore a need for continuous monitoring of policy implementation and appropriateness on the part of both the authorities and the Fund. Two basic monitoring techniques have evolved with experience. The most common is to set limits in advance for certain key variables for the duration of the arrangement or some subperiod of it. Alternatively, or most often in addition to such limits, there may be periodic reviews of economic developments and policies to ensure that policy implementation remains consistent with the original program objectives.

a. Quantitative performance criteria

With two exceptions, every program approved in 1981 contained quantitative limitations on overall credit expansion in the form of ceilings on net domestic assets of either the banking system or monetary authorities. The exceptions were Dominica and Grenada, both of which are members of a currency union; the main instrument of control available to the authorities in these cases is the central government budget. Accordingly, a ceiling on appropriately defined measures of the budget deficit was the main aggregate performance criterion for each of the programs. All of the arrangements containing limitations on overall credit expansion employed a subceiling on recourse to the domestic banking system by either the central government or the public sector. In the case of Jamaica, the overall ceiling was on credit extended by the monetary authorities, whereas the limitation on public sector credit was on that extended by the entire banking system. For Zambia there was also a subceiling on credit from the monetary authorities to the government-owned mining companies. In addition to the two credit ceilings, the Costa Rica and Somalia programs had ceilings on the overall government deficit including external financing, and the arrangement with Togo had a ceiling on domestic government arrears.

For a few cases in which there was substantial uncertainty with regard to a major economic variable at the beginning of the program period, provision for automatic adjustment of performance criteria relating to credit was incorporated into the program. In three instances (the Central African Republic, Mauritania, and Morocco), higher than projected external financing was to be reflected in a commensurate reduction in the rate of credit expansion under the overall and government ceilings. In four other cases (Jamaica, Pakistan, Senegal, and Uganda), the adjustment was symmetrical (sometimes within specified limits) so that domestic credit ceilings would be raised or lowered depending on whether external financing was lower or higher, respectively, than the projected amounts. For the Ivory Coast, a partial upward adjustment of the overall credit ceiling was to be allowed in the event that financing needs related to the accumulation of coffee stocks were higher than expected.

Nearly all of the programs under review contained limitations on external debt as performance criteria. The most common ceilings applied to the contracting or guaranteeing of public debt in the maturity ranges of 1-10 or 12 years, with a subceiling on debt in the maturity range of 1-5 years. Normally the ceilings referred to public and publicly guaranteed debt, but private sector debt was included in the case of Korea. The stand-by arrangement with Romania was the only one in which a separate debt ceiling covering short-term debt was specified, but the overall debt ceiling in the arrangement with Costa Rica was defined to include debt with original maturity of less than one year. 1/

For Costa Rica, Jamaica, and Yugoslavia, which undertook to follow a flexible exchange rate policy, a lower limit was placed on the net foreign asset position of the monetary authorities in order to ensure that the exchange rate would respond flexibly to unforeseen adverse developments in a manner consistent with the degree of adjustment intended in the program. There was provision for automatic adjustment of the limit in the Jamaica program in the event of a deviation from the projected amount of external borrowing. In the case of Romania, another form of a balance of payments test, namely a lower limit on gross reserves, was used in conjunction with minimum levels of the trade balance in convertible currencies. Twelve countries with arrangements approved during the period under review had external payments arrears at the inception of the program and hence performance criteria were established on the reduction and eventual elimination of the arrears. A specification of the amount of arrears to be settled through cash payments or rescheduling was included in some cases (e.g., the Central African Republic, Madagascar, and Zaire). All of the programs also had the standard restrictions clause as a performance criterion.

1/ Fund policies on external debt limitations in connection with use of Fund resources, including the programs approved in 1981, are more fully discussed in SM/83/45 (3/8/83), and SM/83/46 (3/9/83).

b. Other performance criteria

In addition to the standard categories of quantitative performance criteria, a number of arrangements contained performance criteria applying to variables reflecting specific institutional features of individual countries. The Somalia program contained the introduction of a dual exchange rate system as an important part of the policy of moving toward a realistic exchange rate. As a way of ensuring that only a limited value of transactions would be effected at the more appreciated exchange rate, ceilings were placed on the foreign exchange losses incurred by the monetary authorities as a result of the operation of the dual exchange rate system. Adherence to a schedule of reductions in the number of multiple exchange rates was a performance criterion in the Romania program, and in Zaire understandings on exchange rate issues in connection with annual reviews were specified as performance criteria.

As in previous years, annual reviews were stipulated in the 1981 programs whenever performance criteria were to be set for second- or third-year programs within multiyear arrangements. The difficulties of projecting the values of financial variables beyond a period of twelve months make such reviews essential. Mid-term reviews to set ceilings within annual programs were also specified for ten programs. In some cases quantitative performance criteria were not set for the entire year because the program period did not correspond with the financial year, so that for example precise targets for the second half of the year could be agreed only after the budget had been passed. In five instances, reviews were scheduled to confirm that the policies being followed remained adequate for the objectives of the program, but performance criteria for the period had already been established. In such cases, the reviews sometimes concentrated on particular aspects of policy, such as exchange rate action or price changes, but their scope was not strictly limited to such special issues. There is little difference in practice between the two types of review, since it would not in general be desirable to alter policies significantly without some corresponding adjustment of performance criteria. Similarly, the setting of performance criteria at the time of a mid-term review would presumably be done in the context of any policy changes made necessary by changing circumstances. In fact, there were only two instances in which performance criteria had been established for the duration of the annual program, but a review was held to discuss specific policy actions. 1/

The use of review clauses was much more widespread in the 1981 arrangements than in previous years. Arrangements in which reviews were

1/ In Romania this was to ensure that envisaged price changes had been made and that rescheduling negotiations had proceeded in a satisfactory manner. The February 1982 mid-term review of the Pakistan extended arrangement was to discuss macroeconomic policies including the exchange rate.

subject to a performance clause (for the purpose of either setting at least one specific performance criterion within an annual program or reaching understandings concerning further policy actions) constituted between one third and one half of total arrangements during the 1970s, with no perceptible trend over time. By contrast, review clauses were used as performance criteria within annual programs in two thirds of the arrangements approved in 1981. The implications of such an increase are not entirely clear, since the flexibility of the review clause could allow considerable differences in the manner in which it was used in various arrangements. For example, performance criteria for a subperiod of a program could be set in such a way that no new policy measures would be necessary, or the occasion of review discussions could be used to agree on important changes in the direction of economic policy. In the latter case, the review clearly would be more far-reaching and the relative importance of the review clause as a performance criterion much greater, even though the two cases are identical in a formal sense.

3. Observance of performance criteria

All performance criteria had been observed in 8 of the 27 arrangements under review at the time of this writing. One of these is an extended arrangement still in effect (India) and the other seven are one-year stand-by arrangements that expired during 1982. Purchases have been interrupted in each of the multiyear stand-by arrangements. In general, more than one performance criterion was breached in arrangements with interruptions, indicating the degree of interdependence among various targets and policy instruments.

Nonobservance of one or more performance criteria occurred in the remaining arrangements under review. Ceilings on bank financing of the government deficit were breached in 10 cases. A breach of the overall credit ceiling was associated with nonobservance of the subceiling on public sector credit in all but two of the programs incorporating limits on both overall and public sector credit (the Solomon Islands and Thailand). There was only one instance (Yugoslavia) in which total credit exceeded the ceiling while the government remained within the established limitations on credit from the banking system or monetary authorities. Most frequently, incomplete implementation of policies was clearly a causative factor, although it was not always easy to determine the precise extent to which incomplete policy implementation caused departure, since the specific policy actions expected to be necessary to enable performance criteria to be met were not explicitly described in some cases. In several instances, a lack of adjustment of policies to respond to unanticipated exogenous factors also played some role. There were several cases in which the nonobservance of performance criteria was temporary and in which credit levels for subsequent dates were within the established limits (e.g., Dominica and Yugoslavia).

After credit policy, nonobservance of performance criteria was most frequent in respect of limits on external payments arrears, where breaches occurred in 6 out of 12 programs having such ceilings. The nonobservance of limits on arrears was associated with a considerably less favorable than envisaged overall balance of payments outturn in all but two cases. In Madagascar the overall deficit was reduced as were arrears, and the breach of the ceiling was temporary. The overall deficit was also reduced in the Central African Republic; a waiver of the criterion was granted in this case because the problem was due to some underestimation of the initial stock of arrears that became evident only after the program had been approved. The extent to which the widespread nonobservance of criteria on arrears was a symptom of inadequate policy implementation rather than exogenous developments is difficult to determine, but, in most of the cases in which the limits were not observed, the degree of policy change was also less than had been anticipated.

The standard restrictions clause was breached in four programs: in Jamaica, Romania, and Yugoslavia because external payments arrears were incurred after the program was approved, in Yugoslavia because of a tightening of limits on exports and imports of domestic bank notes, and in Costa Rica and Yugoslavia because of the introduction of a multiple currency practice. The balance of payments test was not met in the programs of Costa Rica and Jamaica. External debt ceilings were exceeded only in the cases of Morocco and Sierra Leone.

There was considerable variation in the manner in which performance criteria on reviews were formulated, making it difficult in some cases to determine precisely when the criteria were not observed. 1/ In this paper, a nonobservance of the review clause is considered to have taken place if a delay in the review caused a postponement or rephasing of purchases or if an annual review clearly took place later than was necessary for technical reasons. In practice, this would be defined as a delay of three months or more. Failure or delay in conducting scheduled reviews occurred in eight programs (Costa Rica, Grenada, Mauritius, Morocco, Pakistan, Romania, Sierra Leone, and Uganda). In three cases (Costa Rica, Morocco, and Sierra Leone), the failure to complete reviews was associated with a substantial departure from the planned policy program and purchases were not resumed. In Grenada, new understandings were reached so close to the end of the program period that it was

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1/ A common way of formulating the review clause is to establish an outside limit for the date for the Board discussion to complete the review. In other instances, particularly in those cases in which other performance criteria are to be decided either in connection with reviews to establish annual programs or within such programs, no explicit date is set but further purchases are contingent on the review. In such circumstances, the phasing itself would be agreed at the time of the review. While any delay beyond the specified date constitutes nonobservance of the performance criterion in the first type of review, it is not as straightforward to determine when a review clause of the latter type has been breached.

decided to cancel the arrangement and replace it with a new one. In the other instances, purchases were resumed after a delay once the review was completed.

4. Waivers and modifications

Flexibility in monitoring program implementation may be achieved through the modification of performance criteria in response to changed circumstances. A waiver of particular quantitative or other limits may also be granted if it is considered that further purchases are warranted despite nonobservance of one or more criteria, but that the criteria themselves should not be changed. Certain types of performance criteria are formulated in such a manner that they are not subject to modifications, and only a waiver is possible in these cases.

The most frequently waived ceilings in the programs under review were those on external payments arrears. Such waivers were approved for three programs (the Central African Republic, Romania, and Zambia) of the six in which arrears ceilings were broken. For the Central African Republic, the stock of arrears outstanding on the base date had been underestimated and the ceilings were therefore waived and correspondingly modified. In Romania the inability of the authorities to conclude the expected rescheduling agreements with private suppliers led to the incurrence of arrears and prevented their elimination although the program was otherwise being implemented as agreed. In Zambia, much lower than expected export prices made it difficult for the authorities to achieve the targeted reduction in arrears. The waiver was accompanied by a modification of ceilings for subsequent periods. Credit ceilings were waived on only three occasions (in Sierra Leone, to allow for higher credit to finance purchases of unexpectedly large coffee and cocoa crops, and in Jamaica and Yugoslavia, because the excess was small and additional policy measures were implemented). 1/ The only other waivers in the programs under review were those applying to the restrictions clause in Jamaica, Romania, and Yugoslavia and the ceiling on domestic arrears in the Ivory Coast. The incurrence of external payments arrears in Jamaica, Romania, and Yugoslavia after approval of the arrangement meant that any further purchases under these programs had to be accompanied by a waiver of this criterion. Temporary approval of the restriction on export and import of bank notes in Yugoslavia was granted and a waiver was also given. For the Ivory Coast a waiver of the domestic arrears ceiling was granted because new information showed that the base figure had been significantly underestimated.

There were relatively few modifications of performance criteria in the 1981 arrangements. Ceilings on overall credit expansion were modified in only five programs. The changes were mainly of a technical nature in three cases (the Central African Republic, Ivory Coast, and Uganda) and in two others (Mauritania and Romania) involved downward revisions of ceilings to keep domestic liquidity from expanding too

1/ Pakistan 1980/81 waived de facto by new arrangement.

rapidly in the face of a better than expected net foreign asset position. Arrears ceilings were modified in the Zambia program as described above. In the case of Somalia there was a modification of the ceiling relating to exchange losses of the monetary authorities resulting from the dual exchange rate system. Romania was unable to meet the end-1982 target on gross international reserves because of reduced availability of external financing, and the performance criterion was modified accordingly.

The relative infrequency of waivers and modifications in the 1981 programs is in contrast with earlier experience in respect of upper tranche arrangements. 1/ Waivers were granted in 9 of the 31 programs in the core group covered by the last review paper; in some cases more than one waiver was given (Guyana, Malawi, and Sudan). Moreover, waivers involved credit ceilings in all but one of the nine programs, often reflecting a considerable deviation from the originally intended adjustment effort. 2/ In contrast, credit ceilings were waived only twice in arrangements approved in 1981, and other waivers were in respect of performance criteria that were more subject to influences beyond the control of the authorities. The experience with modifications does not appear to be markedly different from that in the programs covered by the last review. Seven of the 31 programs in the core group contained modifications of performance criteria compared with 6 of the programs approved in 1981. The modifications in the 1981 programs were largely technical in nature whereas modifications involving substantive differences in policy impact were more common in the core group of the previous review.

VIII. *Attainment of Program Objectives*

Programs supported by the use of Fund resources may be evaluated in terms of the success in achieving the short-term objectives that were defined at the time the set of adjustment measures was elaborated. They may also be judged according to the progress made toward the medium-term objective of the achievement and maintenance of a viable balance of payments position. The degree of success in implementation of planned policy measures and in achievement of the short-term objectives of the program are principal considerations in this regard, but an assessment of the amount of adjustment remaining to be accomplished is perhaps of even greater importance. 3/ In this connection, developments in a broad range of economic indicators were analyzed for countries adopting

1/ "Waivers and Modifications of Performance Criteria: Upper Credit Tranche Arrangements--Fund Experience, 1974-80" (EBS/81/70, 3/23/81).

2/ EBS/82/97, 6/9/82.

3/ Developments under a Fund-supported program could also be evaluated by comparison with the alternative adjustment path that would have been followed in the absence of the program and associated financing. However, given the nonobservability of the results of adjustment strategies that have not been pursued, the possible scope of such an examination is limited.

adjustment programs supported by use of Fund resources during the period under review. Special attention was paid to the current account of the balance of payments and to the rates of inflation and economic growth, as well as to savings, investment, the public sector deficit, monetary developments, and the evolution of relative prices.

1. Immediate objectives of programs

Countries following adjustment programs supported by the use of Fund resources typically establish targets for the balance of payments, output growth, and inflation during the period covered by the arrangement. These goals, which can be defined as the immediate objectives of programs, may fall short of the full adjustment required to achieve a viable medium-term balance of payments position. They thus measure the amount of adjustment that is judged to be appropriate within the period of the arrangement, but do not necessarily represent a sustainable equilibrium. 1/ Performance with respect to these objectives is discussed in this section.

The evolution of the current account of the balance of payments was broadly as expected for the countries under review. The ratio of the external current account deficit to GDP was smaller than projected for about half of the cases, and there were relatively small excesses over the planned ratio in all but a few of the remaining programs. The average external current account deficit/GDP ratio for all countries was slightly smaller than the target, and developments in this regard did not differ markedly between structurally oriented and demand restraint programs (Table 7). However, performance was somewhat better for countries with one-year programs than for those with multiyear arrangements, apparently reflecting the higher degree of implementation of planned policy measures in most one-year programs (whether demand restraint or structurally oriented) than in a number of multiyear stand-by and extended arrangements.

A striking feature of the programs under review is the generally poor performance of exports, which grew on average by 11 percentage points less than anticipated. The shortfall affected all but five of

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1/ Two further considerations should be taken into account in evaluating achievements with regard to short-term objectives. Firstly, for cases in which the structure of the economy is inappropriate, examination of the extent of implementation of certain key policy changes may provide a better indicator of the short-term achievements of a program. For example, a smaller than projected external current account deficit may reflect less than envisaged progress in liberalizing the exchange and trade system, and would not indicate achievement of program objectives in such a case. Secondly, it is possible that the short-term targets in a program may be extremely ambitious and difficult to achieve, so that failure to reach the targets may not necessarily mean that progress toward balance of payments viability was not made.

the arrangements under review. 1/ It was more pronounced in countries following demand restraint programs than in those pursuing structurally oriented policies. The causes of the poor export performance are diverse, but reflect lower than expected international prices for primary commodities, 2/ the prolonged period of slow economic growth in industrial countries, production bottlenecks, and other supply problems within the program countries themselves.

Table 7. Developments in Selected Indicators for Program Countries 1/

(In percent)

	Demand Restraint Programs	Supply Oriented Programs	Mixed Strategy Programs
Ratio of external current account balance to GDP 2/			
Target	-13.6	-4.3	-12.8
Actual	-12.5	-4.3	-12.6
International reserves 3/ (weeks of imports)			
Target	9.9	10.8	6.3
Actual	8.6	10.6	6.2
Real growth rate			
Target	4.2	5.2	3.7
Actual	0.4	4.7	1.5
Rate of inflation 4/			
Target	12.3	14.7	18.2
Actual	15.0	11.7	21.7

Source: Staff estimates.

1/ This table presents arithmetic averages of selected variables for all of the programs for which data are available.
2/ Excludes Dominica and Grenada.
3/ Reserve data refer to the end of the indicated period.
4/ Excludes Costa Rica and Uganda.

1/ Twenty-one of the countries under review also requested use of Fund resources under the compensatory financing facility during 1981-82.
2/ An index of market prices for primary commodities exported by primary producing countries fell by 15 percent in 1981 and by a further 12 percent in 1982.

Given the large shortfall on exports, the relatively small deviations from the external current account target by most of the program countries implied a slower than anticipated growth of imports. 1/ Imports rose on average by about 9 percentage points less than expected, in part due to more favorable than projected international price developments. However, 16 of the countries under review experienced a decline in import volumes; imports fell in terms of nominal SDRs in 10 of these cases. In only three countries (Burma, Jamaica, and Mauritania) was there a significant increase in real import levels. As might be expected, the reduction in imports from planned levels was relatively larger among countries with programs oriented around measures to restrain demand. In several instances, it reflected deliberate policy actions to restrain demand more than planned initially. Demand was further reduced by lower producer incomes stemming from the poorer than expected export performance and also by the restraining effect of generally higher real interest rates on borrowing to finance imports. In some instances, the impact of trade liberalization on imports was considerably less than had been expected (e.g., Pakistan). There were also a number of cases in which the lower import level was associated with the adoption of a more restrictive exchange and trade system. The latter course of action tended to be more common among countries where implementation of the original adjustment program did not take place as planned (e.g., Costa Rica, Sierra Leone, Togo, and Zambia).

The overall balance of payments outcome was better than anticipated in the majority of program countries, reflecting higher than expected capital inflows associated mainly with increased external borrowing (notwithstanding the observance of ceilings on contracting of external debt by most countries); as noted above, the current account result was broadly as projected. In several of the cases in which the outcome was less favorable than expected, special factors had caused a large shortfall on net capital inflows due to delays in anticipated aid receipts (the Solomon Islands), speculative outflows (Korea), or a sharp reduction in access to commercial markets (Romania and Yugoslavia). In other instances, the deterioration was associated with a failure to implement the planned adjustment policies and the consequent emergence of severe pressure on international reserve levels; these cases were often marked by a rapid accumulation of payments arrears or a failure to achieve the planned reduction in such arrears (e.g., Costa Rica, Sierra Leone, Togo, Zaire, and Zambia).

There was some increase in the ratio of gross international reserves to imports in about one third of the countries reviewed, although the rise was less than anticipated in several cases. A decline in the ratio of reserves to imports was experienced in the remaining countries. Although a reduction in the ratio had been planned in a

1/ An analysis of the components of changes in the external current account balance of the countries under review is provided in Appendix E.

number of cases, it was sometimes considerably larger than anticipated. Reserve levels remained low in several countries at the end of the period under review, amounting to the equivalent of five weeks or less of imports in 11 cases (compared with 13 such cases at the beginning of the program period).

A notable feature of the countries under review is the general rise in external debt service payments. An increase in the ratio of debt service outlays (including amounts owed to the Fund) to exports of goods and services was experienced by 21 of the 27 countries; on average, a rise in the ratio of about 4 percentage points was recorded. The deterioration of the external debt position reflected the slow growth of exports, sharply higher international interest rates during the period, and the rapid expansion of foreign borrowing on commercial terms in immediately preceding years. 1/ In several cases, the rise in the debt service burden was a matter of serious concern; debt service payments exceeded one third of export earnings in six of the countries under review (Costa Rica, Morocco, Sierra Leone, Togo, Uganda, and Zambia), and an additional five countries had debt service ratios higher than 25 percent. Discussions aimed at a rescheduling of obligations were under way in most of these cases, as well as in a number of the other countries under examination.

The rate of inflation was approximately on target or lower than expected for about half of the countries in which a reduction in the rate from previous levels had been planned (about two thirds of the cases under review). The lower rate of price increase was partly due to the impact of a lower than expected rise in import prices, but also reflected to some extent the moderating effect on prices of domestically produced goods of the low level of capacity utilization in several countries. Substantially worse than projected inflation was experienced by six of the countries in this category; two of these (Madagascar and Togo) were cases marked by a failure to implement adjustment measures and an early departure from the planned adjustment program. In one other instance (Uganda), the price projections included in the program had been made under conditions of great uncertainty and some departure was not unexpected.

Some rise in inflation had been anticipated in the remaining one third of the countries under review. The planned increase was relatively modest except in the case of Costa Rica, which was in the process of realigning prices following a large exchange rate adjustment. In most of the remaining cases, a correction of price distortions was an

1/ Staff estimates indicate that a rise in the debt service ratio of only about 1 percentage point would have occurred if the originally expected export growth had been realized. The general experience of developing countries with respect to external debt and debt service payments in recent years is described in detail in "External Debt and Debt Service of Developing Countries," (SM/83/49, 3/8/83).

important component of the adjustment program (e.g., Burma, Romania, and Zambia). The actual increase in prices was less than assumed in the program for most of the countries in this category, due in part to the impact of falling inflation abroad. In several cases, it also reflected a failure to adjust administered prices to the extent envisaged and may therefore be viewed as the result of a departure from the planned policy program.

The rate of real economic growth, which was targeted to increase sharply for the countries under review, was less favorable than expected, with an average rise in the growth rate of only about one percentage point being recorded. 1/ This result was partly attributable to the impact of depressed international economic conditions on the performance of exports. Most countries with structurally oriented programs or with policies that combined structural and demand restraint elements achieved or exceeded the targeted rate of growth, notwithstanding a substantial shortfall on exports in several cases. However, the average improvement for all of the countries in this category was less than expected, reflecting mainly the poor performance of a relatively few countries. By contrast, the average rate of growth showed little change in countries with programs centered around measures to restrain demand. This represented a considerably worse performance than the substantial improvement that was projected at the beginning of the program period, and was undoubtedly related to the relatively pronounced shortfall of exports experienced by a majority of these countries. Although the performance of most of the members of this group was below expectations, the extent of the deterioration was particularly large for several countries where implementation of adjustment measures was quite poor and negative rates of growth were recorded.

In summary, the external current account deficit was approximately on target for the countries under review, as lower than expected export growth was compensated by a reduction in imports below projected levels. There was considerable success in reducing inflation, but economic growth rates increased by less than expected and were below program targets. On balance, success in achieving the immediate objectives of programs was mixed. There were several cases where implementation of the program was very poor and where achievements were well below targeted performance. However, most countries were successful in implementing at least some of the envisaged adjustment measures and achieved or exceeded one or more of the immediate objectives of the program.

1/ Because real economic activity can generally be expected to respond to new policy initiatives only with some time lag, variations in the rate of economic growth during a program are often linked to a considerable extent to developments in exogenous factors. In addition, it should be noted that the national accounts data available for most of the countries under review are often subject to wide margins of error. Projections of economic growth are particularly difficult to make with precision under these circumstances.

2. Adjustment remaining to be accomplished

It is normal to expect that at any given time there would be some degree of external and internal imbalance in most countries (including those without arrangements with the Fund) and some corresponding need for adjustment of economic policies. As long as the required adjustment is not unduly large, it would not normally pose any serious difficulty to economic policy formulation.

At the time of approval of an arrangement for use of Fund resources, all of the countries under review were facing a need for adjustment that was large enough to present problems in this regard. The extent to which developments during the period of the arrangement contributed to a reduction in the adjustment remaining to be accomplished to amounts that could be addressed without a major reformulation of policies is critical to a determination of whether significant progress was achieved toward balance of payments viability. Such developments could take the form of either explicit policy changes or a fundamental and enduring improvement in exogenous economic circumstances. To a considerable degree, an assessment of progress in this sense goes beyond the question of the extent to which the immediate objectives of a program were achieved.

An attempt was made to quantify the amount of adjustment remaining to be accomplished at the end of the program period (or, for countries where multiyear arrangements remain in force, as of the latest period for which data are available) for the 27 countries under review. 1/ The objectives of external and internal balance were defined, respectively, in terms of (1) an external current account deficit that was judged to be sustainable for each country in light of its individual balance of payments position and prospects, 2/ and (2) a level of domestic inflation approximately equal to that prevailing in the principal industrial trading partner countries during the period. The existence of significant exchange and trade restrictions or extensive price controls, which may be used to repress the symptoms of financial imbalance, was considered to demonstrate the need for substantial further adjustment. 3/

The assessments in this section are based on the views of the staff regarding the medium-term balance of payments prospects of the

1/ The analysis included in this paper is based on data that were available as of June 1983.

2/ The external current account objective has been expressed in percent of GDP for the purposes of this exercise. It should be recognized that this measure is highly sensitive to changes in the real exchange rate. For example, during a period in which lower domestic inflation results in a real depreciation, the same external current account deficit/GDP ratio may involve a progressively lower absolute level of the deficit.

3/ Other possible indicators of imbalances within the economy (e.g., chronically low economic growth) could also be used to supplement these data, but have not been incorporated into the present analysis.

countries concerned. Subjective elements of judgment are an unavoidable part of such assessments and precise quantification of the remaining adjustment is not feasible in most cases. However, it is possible to draw certain broad conclusions about the relative magnitude of the policy problems that remained to be addressed in different countries at the end of the period under review.

In interpreting the results of the analysis, two considerations should be taken into account. Firstly, the above indicators may diverge from levels that are judged to be sustainable over the medium term either because of temporary factors or alternatively because there is a need for more fundamental policy change. In certain cases, the divergence may even stem from an element of the policy program (e.g., the movement in the price index stemming from the elimination of a subsidy). Even if temporary factors are the primary cause of the problem, there may be a need for significant policy change; for example, a fall in the price of a key export commodity may be self-reversing, but the fact that it has a severe impact on the balance of payments may indicate the need for strong policy action to promote the diversification of exports and reduce the vulnerability of the economy over the medium term. Secondly, the present analysis is based on judgments as of mid-1983 about the sustainability of the balance of payments for the countries under review; these assessments are not necessarily the same as those that were made when adjustment programs were being formulated by these countries. A position that was considered to be sustainable in the set of circumstances prevailing at that time may no longer be viable if underlying conditions have changed substantially. This is clearly the case for countries with heavy reliance on international capital markets where conditions have become more difficult (e.g., Korea, Romania, and Yugoslavia). By contrast, the recent decline in oil prices and moderation of interest rates may reduce the need for adjustment of policies in some countries.

The adjustment that remained to be accomplished at the end of the period under review was relatively small in several cases (e.g., Korea, Mauritius, and Thailand), and was not expected to require a major reformulation of economic policies, but rather could be brought about largely through the sustained implementation of policies already in place. A somewhat larger amount of adjustment was indicated for several additional countries (e.g., the Central African Republic, Liberia, Senegal, and Somalia); some of these faced severe short-term liquidity constraints and a potentially difficult external debt situation. Certain of the countries under review (e.g., Dominica and the Solomon Islands) had relatively large imbalances that were associated with adverse weather conditions and were expected to be self-correcting to at least a certain degree. The amount of adjustment that needed to be effected through new measures was relatively small in these cases. A somewhat similar situation prevailed in Grenada, where much of the imbalance stemmed from a large investment project that was expected to be completed in the near future.

There were a number of cases in which the external current account deficit and rate of inflation were broadly acceptable in numerical terms, but where significant exchange, trade, and price controls remained in place (e.g., Burma, Ethiopia, Pakistan, and Romania); considerable further adjustment would be required for all of these countries if administrative restrictions were to be removed. 1/ Such countries could clearly benefit from the adoption of measures to eliminate the underlying imbalances, improve the allocation of resources, and establish the conditions for higher economic growth. In several other countries (e.g., Jamaica, Madagascar, Morocco, Yugoslavia, Zaire, and Zambia), the external current account deficit and/or rate of inflation were unacceptably large at the end of the period under review, in spite of the existence of extensive exchange and trade restrictions and/or price controls. The amount of additional adjustment required in these cases was accordingly quite large.

The amount of remaining adjustment was also large in several countries not making use of extensive administrative restrictions. In one instance (Uganda), many of the adjustment measures needed had already been implemented, but the full impact had not yet been realized. In others (e.g., Costa Rica, Ivory Coast, Mauritania, Sierra Leone, and Togo), substantial further measures would be necessary. Some of these countries, as well as several making use of extensive administrative restrictions, were cases in which the policy program supported by use of Fund resources had been implemented to only a limited extent.

The need for a number of the countries under review to pursue a set of economic policies aimed at substantial adjustment in addition to that already accomplished under the program reflects a number of factors. Firstly, the large size of the initial imbalance made it desirable to phase the adjustment over a period longer than one year in several cases. This was explicitly recognized in several programs that were supported by multiyear arrangements. Even in those cases where a one-year arrangement was used, a longer adjustment horizon was often foreseen; six of the one-year programs under review were followed within six months by a new arrangement. 2/ Secondly, some countries with large payments imbalances had aimed at adjustment through the adoption of supply-oriented policies which require more time to be effective; 16 of the countries under review were pursuing an economic strategy in which such structural adjustment policies either constituted the principal focus of the program or played an important supporting role. Thirdly, the international economic environment was worse than expected during the period under review; the slow growth of the industrial countries and the impact of other adverse exogenous developments

1/ In several of these cases, the process of liberalization has continued beyond the period under review, in some instances under a policy program supported by the use of Fund resources.

2/ In addition, five of the multiyear arrangements were followed within six months by new arrangements, in most cases after the 1981 arrangement had been canceled prior to the original expiration date.

clearly posed additional policy problems for several of the countries under examination. Finally, incomplete implementation of the planned policy program resulted in the persistence or aggravation of large imbalances in a number of cases. There were also some instances in which incorrect underlying assumptions or smaller than expected response to policy changes contributed to the achievement of less progress during the program period than had been anticipated. These and other factors influencing the progress of the countries under review toward a viable balance of payments position are discussed more fully in the accompanying paper (EBS/83/215, 10/4/83).

Summary Data for Individual Countries

The data that form the basis for much of the quantitative discussion in this paper are summarized in the attached Tables A1-A6. Data are provided on the targeted and actual outcomes for several important variables for each year in which an economic and financial program was established in connection with the 27 arrangements under review. The information covers the principal items for which program objectives were established (inflation, real growth, the ratio of the external current account balance to GDP, the overall balance of payments, and the level of international reserves), as well as projected and actual values of several variables that have served as indicators of policy implementation (the growth ratios of overall credit and credit to the government or public sector, and the ratio of the fiscal deficit to GDP). The differences and similarities among the data for individual countries are illustrated in Charts 1 - 7 for most of these variables. These charts appear at the end of the paper.

Several considerations need to be taken into account in making assessments on the basis of these data. Firstly, the information provided generally refers to calendar year developments, although many program periods do not coincide with the calendar year. The choice of appropriate periods that best reflect the prior and program years has been made on an individual basis, but there are several cases in which a mismatching of dates has occurred with possible bias to some of the results. Secondly, the data that are defined as targets in the tables refer to objectives established at the beginning of a program year. For the second and third years of multiyear arrangements, these may not necessarily be the same as the targets that were established at the beginning of the arrangement. Thirdly, although data have been selected with a view to achieving maximum comparability across countries, various definitional and other differences remain that reduce the usefulness of such comparisons. For example, variation among countries is particularly common with respect to the definition of the public sector, which is narrowly defined as the central government in some instances but is based on a more inclusive concept in others. Fourthly, credit growth ratios do not represent percentage changes but rather have been defined in terms of the stock of broad money at the beginning of the program period. Finally, all of the data provided must be regarded as preliminary and subject to revision in light of the short time that has elapsed since the end of the program period. Data referring to the later years of multiyear arrangements would be especially likely to be affected by such changes.

Table A1. External Current Account Balance, Inflation and Real Growth: One-Year Stand-By Arrangements, 1981

(In percent)

	External Current Account Balance/GDP			Inflation Rate			Real Growth Rate		
	Prior Year	Target	Actual	Prior Year	Target	Actual	Prior Year	Target	Actual
Burma	-3.9	-7.0	-7.3	-0.2	7.0	3.7	7.8	6.0	6.7
C.A.R.	-19.2	-22.0	-12.3	17.3	16.0	12.7	-3.9	3.0	-2.2
Ethiopia	-5.8	-6.2	-6.9	1.7	...	8.8	3.3	5.0	2.4
Grenada	-15.5	-28.9	-24.2	23.0	20.0	18.8	3.0	2.7	3.4
Korea	-9.4	-8.2	-7.5	44.2	24.0	11.8	-6.2	5-6	7.1
Liberia	-9.6	...	-8.3	10.0	8.5	7.0	-2.5	...	-2.0
Madagascar	-18.4	-11.8	-13.4	18.2	16.0	30.5	0.8	1.5	-9.2
Mauritania	-36.2	-45.3	-32.7	11.1	...	18.7	3.7	...	8.5
Mauritius	-16.5	-13.5	-6.0	26.5	25.0	13.4	-7.6	5.0	5.6
Senegal	-20.5	-16.2	-12.4	13.0	11.0	19.0	-2.4	9.2	9.8
Solomon Islands	-21.8	-26.4	-23.2	15.9	12-14	14.6	-5.5	4-5	0.6
Somalia	...	...	...	59.4	35.0	44.3	...	...	...
Uganda	-1.6	-4.0	-2.2	104.0	50.0	76.0	-8.4	9-10	10.0

Source: Staff estimates.

Table A2. Overall Balance of Payments and Gross Official Reserves: One-Year Stand-by Arrangements, 1981

	Overall Balance of Payments (millions of SDRs)			Gross Official Reserves (weeks of imports)		
	Prior Year	Target	Actual	Prior Year	Target	Actual
Burma	48.0	-70.0	-37.0	21.5	...	13.9
C.A.R.	-0.4	-17.3	-7.5	13.0	...	20.0
Ethiopia	-46.9	-66.7	-53.2	8.3	...	14.5
Grenada	0.1	-6.6	-6.4	13.0	10.0	9.4
Korea	-1,452.0	-807.0	-1,948.0	12.1	12.3	11.2
Liberia	-32.0	-55.0	-40.0	1.0	1.0	1.0
Madagascar	-183.2	-86.8	-74.5	2.0	...	3.0
Mauritania	-29.7	-18.0	28.7	25.7	18.8	24.1
Mauritius	-60.0	-30.0	-2.0	0.7	0.5	1.1
Senegal	-139.5	-82.0	-103.6	0.1	0.1	0.1
Solomon Islands	-5.2	-2.3	-10.3	20.0	22.1	15.0
Somalia	-21.5	-84.9	-11.0	3.9	...	10.7
Uganda	-129.0	-142.0	-96.9	1.8	...	12.0

Source: Staff estimates.

Table A3. Credit Growth Ratios and Overall Government Balance: One-Year Stand-By Arrangements, 1981

(In percent)

	Overall Credit Growth Ratio 1/			Government Credit Growth Ratio 1/			Overall Government Balance/GDP		
	Prior Year	Target	Actual	Prior Year	Target	Actual	Prior Year	Target	Actual
Burma	19.7	27.5	24.1	19.7	24.6	23.2	-7.8	-11.7	-14.1
C.A.R.	16.0	21.1	13.1	-12.9	13.1	10.5	-5.2	-3.3	-5.6
Ethiopia	8.0	13.3	10.6	6.6	11.7	3.5	-4.0	-2.5	-5.2
Grenada	5.3	0.4	2.3	-3.9	6.0	3.0	-0.7	-10.8	-9.5
Korea	50.1	56.3	45.3	4.0	6.1	8.1	-3.4	-2.9	-4.9
Liberia	10.9	...	63.3	47.0	34.3	40.4	-10.5	-6.0	-10.5
Madagascar	61.4	20.9	35.3	44.4	12.1	28.8	-18.4	-9.2	-14.7
Mauritania	30.4	36.7	26.1	12.8	22.6	9.9	-13.8	-8.4	-9.1
Mauritius	35.4	30.4	32.8	25.2	18.9	24.9	-13.9	-13.5	-12.9
Senegal	22.6	41.4	40.9	6.4	20.3	22.3	-13.4	-10.7	-7.0
Solomon Islands	14.5	26.8	21.2	-7.5	6.6	8.8	-14.3	-15.9	-12.6
Somalia	32.8	19.8	19.7	23.9	10.5	10.3	...	...	...
Uganda	72.7	114.0	103.8	65.5	55.0	61.7	-4.3	-2.6	-3.2

Source: Staff estimates.

1/ Absolute change in credit outstanding relative to stock of broad money at beginning of period.

Table A4. External Current Account Balance, Inflation and Real Growth: Multiyear Stand-By and Extended Arrangements, 1981

(In percent)

	Year	External Current Account Balance/GDP			Inflation Rate			Real Growth Rate		
		Prior Year	Target	Actual	Prior Year	Target	Actual	Prior Year	Target	Actual
Romania	1	-4.2	-3.0	-1.3	1.5	2.5	3.5	3.3	6.5	2.7
	2		-0.6	2.1		11.2	17.8		5.7	3.2
	3		1.4	...		7.0	...		3.8	...
Thailand	1	-6.2	-6.0	-6.9	20.0	15.0	12.0	5.8	7.3	7.0
	2		-5.6	-3.0		9.8	4.8		7.0	4.5
Togo 1/	1	-23.2	-16.5	-22.9	12.3	9.0	19.7	0.8	0.7	-4.8
Yugoslavia	1	-4.0	-2.5	-1.5	39.0	20.0	39.0	2.0	2.0	1.5
	2		-1.0	-2.5		15.0	31.0		2.5	1.0
	3		-1.0	...		36.0	...		-2.5	...
Costa Rica 1/	1	-14.4	-11.8	-11.7	18.1	40.0	37.1	0.8	--	-4.6
Dominica	1	-56.1	-26.0	-32.1	29.8	...	13.9	17.0	8.5	8.0
	2		-28.8	-18.5		...	4.4		2.8	3.3
	3		...	...		...	...		5.7	...
India	1	-1.6	-2.0	-2.1	15.8	11.0	2.4	8.0	4.8	5.2
	2		-2.1	-2.1		8.0	6.5		5.0	2.0
	3		-2.1	...		7.0	...		6.0	...
Ivory Coast	1	-16.0	-18.4	-14.4	14.7	...	8.8	6.3	-1.5	-1.3
	2		-15.6	-13.7		...	7.4		3.0	-1.8
	3		-11.1	...		...	...		3.0	...
Jamaica	1	-7.2	-9.9	-15.4	26.5	18.0	8.9	-4.6	3.8	1.2
	2		-14.2	-13.4		10.0	7.3		5.0	2.0
	3		-3.0	...		9.0	...		3.3	...
Morocco 1/	1	-8.0	-6.5	-12.6	9.4	11.0	12.5	3.7	4.5	-1.3
Pakistan	1	-3.5	-4.1	-5.3	13.9	10.0	11.5	6.4	6.1	5.6
	2		-4.5	-1.5		8.0	5.2		6.7	5.8
Sierra Leone 1/	1	-16.1	-11.5	-15.9	13.7	15.0	26.3	0.5	1.5	--
Zaire 1/	1	-6.7	-7.1	-13.1	46.7	45.0	35.4	2.5	2.0	2.4
Zambia 1/	1	-11.7	-11.3	-21.4	11.7	15.0	12.9	4.1	5.0	-0.7

Source: Staff estimates.

1/ No second-year program was established.

Table A5. Overall Balance of Payments and Gross Official Reserves: Multiyear Stand-By and Extended Arrangements, 1981

	Year	Overall Balance of Payments (millions of SDRs)			Gross Official Reserves (weeks of imports)		
		Prior Year	Target	Actual	Prior Year	Target	Actual
Romania 1/	1	-188	-131	-1,177	3.0	4.0	4.0
	2		771	720		5.0	6.0
	3		...	...		8.0	...
Thailand	1	210	-424	-20	16.0	19.0	15.0
	2		-429	110		12.0	14.0
Togo 2/	1	3	-27	32	11.0	...	24.0
Yugoslavia	1	-132	-297	-369	5.0	6.0	6.0
	2		-536	-1,427		5.0	3.0
	3		-460	...		5.0	...
Costa Rica 2/	1	-360	--	-400	7.8	5.5	6.3
Dominica	1	--	-4	-5	...	...	...
	2		-3	-3		...	...
	3		-2	...		...	...
India	1	-440	-1,683	-2,175	24.0	20.0	17.0
	2		-1,683	-1,280		15.0	19.0
	3		-1,497	...		19.0	...
Ivory Coast	1	-490	-440	-449	2.0	...	2.0
	2		-345	-134		...	0.4
	3		-372	...		...	...
Jamaica	1	-117	-15/31	33	4.0	5.0	4.0
	2		-12/41	-134		9.0	4.0
	3		111	...		11.0	...
Morocco 2/	1	-175	-344	-207	5.0	4.0	4.0
Pakistan	1	-19	-226	-510	10.2	9.2	7.6
	2		-234	668		8.3	16.1
Sierra Leone 2/	1	-119	-61	-120	0.7	...	0.5
Zaire 2/	1	-180	-450	-612	11.0	...	10.0
Zambia 2/	1	-213	-152	-327	3.1	2.5	3.5

Source: Staff estimates.

1/ Convertible currencies only.
2/ No second-year program was established.

Table A6. Credit Growth Ratios and Overall Government Balance: Multiyear Stand-By and Extended Arrangements, 1981

(In percent)

	Year	Overall Credit Growth Ratio 1/			Government Credit Growth Ratio 1/			Overall Government Balance/GDP		
		Prior Year	Target	Actual	Prior Year	Target	Actual	Prior Year	Target	Actual
Romania	1	42.5	32.4	20.5	...	...	...	0.2	--	1.0
	2		14.3	8.5		...	...		2.6	2.7
	3		7.2	...		...	...		2.4	...
Thailand	1	22.2	28.3	21.0	11.4	5.1	6.0	-4.8	-2.8	-3.1
	2		25.7	26.0		4.8	11.0		-2.7	-5.9
Togo 2/	1	9.5	20.0	10.1	-0.7	9.9	13.5	-2.2	-0.6	-5.6
Yugoslavia	1	36.9	27.7	29.2	...	...	...	-1.3	0.1	-0.1
	2		22.1	27.3		...	...		0.1	0.1
	3		...	...		...	...		--	...
Costa Rica 2/	1	34.6	34.7	63.8	16.7	15.3	10.1	-11.2	-9.0	-13.9
Dominica	1	14.2	15.6	25.4	-2.8	...	4.5	-24.3	-20.9	-15.3
	2		10.2	-3.1		...	-3.6		-21.1	-15.2
	3		...	...		...	...		...	...
India	1	26.2	21.8	21.0	14.1	9.4	9.0	-6.6	-6.2	-5.8
	2		22.3	20.6		8.9	7.4		-5.6	-6.3
	3		...	...		...	...		-6.5	...
Ivory Coast	1	44.5	42.3	34.6	23.6	20.2	19.2	-12.7	-12.5	-8.9
	2		34.1	11.1		3.5	4.0		-8.8	-8.8
	3		29.8	...		18.7	...		-6.2	...
Jamaica	1	36.2	23.4	24.4	28.9	8.0	7.9	-17.0	-13.3	-14.2
	2		14.6	33.1		5.2	28.3		-12.9	-15.7
	3		11.4	...		-3.1	...		-10.3	...
Morocco 2/	1	16.8	16.6	20.2	10.1	9.3	12.8	-10.3	-7.4	-14.7
Pakistan	1	14.6	17.3	16.5	6.0	6.0	6.5	-5.2	-5.1	-5.3
	2		15.8	17.0		5.7	8.0		-5.4	-7.0
Sierra Leone 2/	1	52.8	30.7	56.5	45.8	24.1	53.6	-11.5	-8.1	-10.2
Zaire 2/	1	50.4	38.6	51.9	12.8	25.2	43.2	0.2	-2.9	-5.9
Zambia 2/	1	28.0	30.2	46.1	26.7	16.5	17.4	-17.3	-8.2	-16.0

Source: Staff estimates.

1/ Absolute change in credit outstanding relative to stock of broad money at beginning of period.
2/ No second-year program was established.

Previous Upper Credit Tranche Arrangements Requiring Approval of Annual Programs in 1981

Twelve multiyear upper credit tranche stand-by and extended arrangements were initiated in prior years for which a second- or third-year annual program would normally have had to be approved during 1981. 1/ These arrangements have not been reviewed in the main text. All of these arrangements had expired or been canceled as of end-June 1983. Cancellation occurred prior to the original expiration date in four cases (Bangladesh, Guyana, Kenya, and Sudan). The full amount available was purchased in only three instances (the Philippines, Sri Lanka, and Turkey), while two countries (Gabon and Panama) made no purchases under the arrangement (Table B1).

The objectives and design of adjustment policies under the 12 arrangements were described fully in the previous Review Paper (EBS/83/97, 6/9/82). The policies adopted in five of these countries (Kenya, Malawi, Panama, Sri Lanka (1981 program year only), and Tanzania) were aimed mainly at restraint of demand, while those pursued in the remainder were considered to be primarily oriented toward structural adjustment (Bangladesh, Gabon, Guyana, Honduras, the Philippines, Sri Lanka (1979-80 program years only), Sudan, and Turkey). Implementation of planned policy changes was generally mixed, with only a few cases in which a majority of policies were implemented substantially as expected.

In addition to the usual quantitative performance criteria and reviews, there were also a number of performance criteria that reflected particular institutional features of the country concerned. The arrangement with Panama which uses the U.S. dollar as its domestic currency, did not include a ceiling on the expansion of overall domestic credit, but had a ceiling on the overall public sector deficit, including foreign borrowing. The arrangement with the Philippines included a limit on new private debt as well as the normal ceiling on contracting of nonconcessional loans by the public sector. Other performance criteria included, inter alia, a limit on transfers from the budget to state economic enterprises (Turkey), a minimum reserve requirement applicable to commercial banks (Turkey), and the termination of bilateral payments agreements (Sudan). In addition, the arrangement with Turkey specified as a performance criterion that the exchange rate continue to be adjusted sufficiently (as a minimum) to maintain external competitiveness.

Economic developments in these 12 countries through the early part of 1982 were described in detail in the previous Review Paper. In all

1/ Prior multiyear arrangements requiring approval of an annual program in 1981 had also been initiated for Costa Rica, Korea, Liberia, Madagascar, Mauritania, Morocco, Pakistan, Senegal, and Yugoslavia. All of these were replaced during 1981 by arrangements that have been reviewed in the main text.

but three cases (Gabon, Guyana, and Turkey), preliminary data were presented at that time covering the entire period of the arrangement for which annual programs were ultimately approved. The most recent data available are provided in Tables B2 and B3, including estimates of the actual outturn during the entire period of the arrangement for those countries for which information had been incomplete. These data are broadly consistent with those provided earlier and do not support any significant change in the views about individual countries or overall performance that were offered at that time. A detailed analysis of individual cases is included in the periodic reviews that have been undertaken of each of these arrangements. A listing of the relevant papers containing the most recent reviews of each case is provided in the Annex to this Appendix.

There were four cases in which agreement between the staff and the authorities was not reached regarding the policy program scheduled to begin in 1981 (Bangladesh, Kenya, Sudan, and Tanzania). For practical purposes, the arrangement could therefore be considered as not operative during the period under review in the present paper. The lack of agreement on a set of adjustment policies generally reflected the fact that developments during the earlier year(s) of the arrangement had diverged widely from the original objectives, often as a result of poor implementation of the planned policy program.

The experience of the 8 countries for which annual programs were approved in 1981 generally parallels that of the group of 27 countries covered by the present review. In three instances (Guyana, Honduras, and Malawi), policy implementation lagged following approval of the program and the last Review Paper concluded that there was unsatisfactory progress toward the objectives of the arrangement. Progress toward balance of payments viability was judged to have been satisfactory during the 1981 program year in four cases (Gabon, Panama, Sri Lanka, and Turkey), but the outcome was mixed in the remaining arrangement (the Philippines).

Table B1. Upper Credit Tranche Arrangements Providing for 1981 Programs

Country	Date of Approval	Expiration Date	Amount of Arrangement: Millions of SDRs: Approved	Millions of SDRs: Drawn 1/	Percent of Quota: Approved	Percent of Quota: Drawn 1/
Extended Arrangements						
Bangladesh 2/	12/8/80	12/7/83	800.0	220.0	351	97
Gabon	6/27/80	12/31/82	34.0	--	113	--
Guyana 3/	7/25/80	7/24/83	100.0	51.7	400	207
Honduras	6/28/79	6/27/82	47.6	23.9	140	70
Sri Lanka	1/26/79	12/31/81	260.3	260.3	219	219
Sudan 4/	5/4/79	5/3/82	200.0	251.0	227	285
Stand-By Arrangements						
Kenya 5/	10/15/80	10/14/82	241.5	90.0	350	130
Malawi	5/9/80	3/31/82	49.9	40.0	263	211
Panama 6/	4/18/80	12/31/81	66.4	--	100	--
Philippines	2/27/80	12/31/81	410.0	410.0	195	195
Tanzania	9/15/80	6/30/82	179.6	25.0	327	45
Turkey	6/18/80	6/17/83	1,250.0	1,250.0	625	625

Source: Fund documents.

1/ As of June, 1983.
2/ Canceled on June 21, 1982.
3/ Augmented to SDR 150 million (400 per cent of new quota) in July 1981. Canceled on July 22, 1982.
4/ Augmented to SDR 427 million (323 per cent of new quota) in November 1980. Canceled on February 22, 1982.
5/ Canceled on January 8, 1982.
6/ Augmented to SDR 90 million in February 1981.

Table B2. External Current Account Balance, Inflation, and Real Growth: Prior Arrangements Providing for 1981 Programs

(In percent)

	Year	External Current Account Balance/GDP			Inflation Rate			Real Growth Rate		
		Prior Year	Target	Actual	Prior Year	Target	Actual	Prior Year	Target	Actual
Extended Arrangements										
Bangladesh 1/	1	-12.9	-13.1	-12.4	18.5	10.4	12.6	3.5	7.2	5.9
Gabon	1	5.7	18.0	13.1	7.3	10.0	11.0	-0.7	1.5	--
	2		9.7	11.6		12.0	9.5		4.9	-3.4
	3		1.9	11.1		10.0	14.0		-0.7	1.9
Guyana	1	-19.2	-18.3	-25.9	11.3	10.0	4.8	1.6	6.9	0.6
	2		-20.4	-36.9		10.0	16.9		5.6	-4.4
Honduras	1	-8.5	-12.5	-8.9	5.7	...	12.1	7.0	6.6	6.6
	2		-12.6	-12.6		...	18.1		6.0	2.6
	3		-12.0	-10.8		...	9.4		1.3	0.3
Sri Lanka	1	-5.5	-9.8	-11.1	8.3	16.0	19.0	8.2	5.8	6.3
	2		-16.5	-19.8		20.0	37.7		6.0	5.8
	3		-15.9	-13.3		19.0	23.9		5.5	5.8
Sudan 1/	1	-7.0	-6.5	-9.0	28.0	25.0	28.0	-5.0	4.0	-1.0
	2		-9.0	-9.0		17.0	31.0		5.0	5.5
Stand-By Arrangements										
Kenya 1/	1	-12.6	-10.0	-10.2	12.8	10.0	20.0	4.3	4.2	4.1
Malawi	1	-20.2	-15.3	-17.7	2.7	12.6	11.9	6.8	2.0	0.2
	2		-17.4	-12.5		10.6	19.8		3.0	0.1
Panama	1	-10.8	-10.2	-7.8	8.0	...	13.8	6.0	3.5	6.0
	2		-9.0	-11.0		...	7.3		5.5	4.3
Philippines	1	-5.3	-5.9	-5.8	18.8	15.0	17.6	6.8	6.0	4.4
	2		-6.4	-6.0		12.0	12.4		5.5	3.8
Tanzania 1/	1									
Turkey	1	-2.3	...	-6.3	63.0	...	101.0	-1.0	...	-1.0
	2		-4.5	-4.0		40.0	42.0		3.0	4.3
	3		-2.5	-2.0		25.0	27.0		4.5	4.5

Source: Staff estimates.

1/ No annual program was approved for 1981.

Table B3. Credit Growth Ratios and Overall Government Balance: Prior Arrangements Providing for 1981 Programs

		Overall Credit Growth Ratio 1/			Government Credit Growth Ratio 1/			Overall Government Balance/GDP		
	Year	Prior Year	Target	Actual	Prior Year	Target	Actual	Prior Year	Target	Actual
Extended Arrangements										
Bangladesh 2/	1	36.0	38.9	35.8	24.6	15.3	23.9	-12.6	-11.6	-11.4
Gabon	1	10.0	18.7	10.5	17.1	--	-5.1	5.1	6.1	7.9
	2		9.3	-1.5		-12.8	-19.9		10.4	10.0
	3		15.7	1.9		-3.5	-12.1		9.1	9.2
Guyana	1	63.0	18.9	32.7	52.9	8.1	24.6	-23.3	-20.2	-34.2
	2		26.6	39.6		20.3	35.2		-23.0	-40.2
Honduras	1	-5.4	14.6	3.1	22.5	27.7	28.3	-6.8	-7.3	-5.2
	2		14.1	48.8		14.1	50.1		-6.6	-9.0
	3		25.0	71.3		19.2	45.6		-7.3	-8.5
Sri Lanka	1	-1.6	43.1	29.4	-12.2	14.3	14.3	-13.8	-9.7	-13.9
	2		30.9	68.6		6.7	51.1		-12.7	-23.1
	3		34.7	29.4		23.1	20.8		-14.7	-15.5
Sudan 2/	1	34.0	23.0	30.0	22.0	20.0	16.0	-9.0	-7.0	-8.5
	2		30.0	57.0		12.0	28.0		-7.0	-10.0
Stand-By Arrangements										
Kenya 2/	1	12.4	20.3	21.7	-4.6	6.2	13.9	-12.6	-10.0	-10.2
Malawi	1	44.3	19.4	32.2	14.4	4.7	28.9	-9.6	-7.8	-11.1
	2		21.9	49.1		--	43.6		-6.8	-10.7
Panama	1	...	...	...	...	...	...	-11.5	-8.0	-5.2
	2		...	...		...	...		-5.8	-5.4
Philippines	1	20.4	26.8	24.1	0.8	5.2	3.4	-0.1	-1.3	-1.3
	2		13.2	22.2		...	8.2		-1.3	-4.0
Tanzania 2/	1	32.2	23.8	29.9	26.9	16.3	21.4	...	...	...
Turkey	1	58.7	83.6	64.1	48.9	41.1	46.1	-3.9	-1.7	-4.3
	2		55.1	44.3		31.0	26.3		-1.9	-0.3
	3		27.8	26.2		10.1	9.0		-1.5	-1.8

Source: Staff estimates.

1/ Absolute change as percent of broad money outstanding at beginning of period.
2/ No 1981 program was approved.

Papers Containing Reviews of Arrangements Providing for 1981 Programs

Extended arrangements

Bangladesh	Staff Report for the 1981 Article IV Consultation (SM/21/41, 2/23/82)
Gabon	Staff Report for the 1982 Article IV Consultation and Review of Extended Arrangement (EBS/83/42, 2/24/83)
Guyana	Staff Report for the 1982 Article IV Consultation (SM/82/201, 10/8/82)
Honduras	Staff Report for the 1982 Article IV Consultation (SM/82/151, 7/28/82)
Sri Lanka	Staff Report for the 1982 Article IV Consultation (SM/82/155, 7/30/82)
Sudan	Request for Stand-By Arrangement (EBS/82/7, 1/14/82)

Stand-by arrangements

Kenya	Request for Stand-By Arrangement (EBS/81/241, 12/10/81)
Malawi	Request for Stand-By Arrangement (EBS/82/126, 7/13/82)
Panama	Request for Stand-By Arrangement (EBS/82/47, 3/24/82)
Philippines	Request for Stand-By Arrangement (EBS/83/24, 1/31/83)
Tanzania	Staff Report for the 1982 Article IV Consultation (SM/82/154, 7/30/82)
Turkey	Staff Report for the 1983 Article IV Consultation and Request for Stand-By Arrangement (EBS/83/98, 5/20/83)

Exchange Rate and Interest Rate Actions in the 1981 Arrangements

Although a substantial degree of fiscal and monetary restraint is included in many adjustment programs supported by the Fund, reliance on demand reduction alone to bring about external adjustment would have a substantial cost in terms of slower economic growth and loss of potential income. Therefore, programs are generally designed with a view to reducing this cost by utilizing macroeconomic tradeoffs when they are present (such as allowing slightly more expansionary demand-management policies, with a possible adverse impact on inflation, in order to relieve some unemployment); by eliminating distortions or rigidities; and by utilizing intertemporal tradeoffs implicit in the investment possibilities of the country. The exploitation of such tradeoffs is often effected through changes in economy-wide prices, such as the exchange rate, wages, and the rate of interest, as part of a comprehensive policy package.

The 27 arrangements under review encompass a diversity of experiences in exchange rate management. Six of the countries are members of currency unions and use the U.S. dollar as legal tender; in these countries, the scope for exchange rate management, and to an extent interest rate management, is very limited. Two of the countries (Dominica and Grenada) belong to the East Caribbean Currency Authority (ECCA), whose currency has been pegged to the U.S. dollar at the same parity since mid-1976. The nominal effective exchange rate indices of these countries and Liberia (which also pegs to the U.S. dollar) have followed to a large extent the movements in the value of that currency, appreciating by over 20 percent (unweighted average) in both nominal real terms from December 1980 to December 1982. 1/ Three countries (Ivory Coast, Senegal, and Togo) use the CFA franc issued by the Central Bank of the West African States (BCEAO) and the Central African Republic uses the CFA franc issued by the Bank of the East African States (BEAC). The CFA franc issued by both banks has been pegged at the same parity for a number of years to the French franc, which depreciated in nominal effective terms (MERM weights) by 20 percent from end-1980 to end-1982. On average, the nominal effective exchange rate indices of these four countries also depreciated, but by only about 7 percent from end-1980 to end-1982. Their real effective exchange rate indices moved in dissimilar ways during 1981-82 (ranging from a real depreciation of

1/ The effective exchange rate indices used in this section are in all cases those calculated for the purposes of surveillance.

15 percent to an appreciation of 8 percent). Interest rate changes were not an important component of adjustment programs in any of the countries belonging to a currency union or in Liberia. 1/

Step depreciations of the currency were explicitly to be undertaken as part of the adjustment programs of Mauritius, Romania, the Solomon Islands, Somalia, Thailand, Uganda, and Zaire. In three other cases (Korea, Morocco, and Yugoslavia) a sizable depreciation had taken place in 1980 during the period covered by a previous arrangement with the Fund, and flexible exchange rate management was intended to prevent a deterioration of competitiveness in 1981; in fact, Yugoslavia undertook a significant further depreciation in the second half of 1981. Step depreciations were often accompanied by adoption of a more comprehensive basket peg, reform of the exchange and trade system, and/or wide-ranging changes in the price system. In several countries, the peg was changed from the U.S. dollar (or from a basket in which the U.S. dollar was preponderant) to a basket of currencies reflecting trade or settlement flows (Korea, Mauritius, Morocco, Pakistan, and the Solomon Islands), or to the SDR (Somalia). Appropriate adjustments in domestic relative prices were allowed to take place in most countries. In half of the cases this resulted in a substantial increase in domestic prices of internationally tradable goods. In one instance (Romania) the exchange rate change was accompanied by a substantial modification of the pricing system, including the tying of domestic prices of tradables more closely to world prices and the official exchange rate. 2/ In other cases, producer prices of import or export goods were raised, or price controls on these goods were relaxed.

The impact change in the real exchange rate after the depreciation ranged from less than 10 percent in some countries (Korea, Morocco, Thailand, and Yugoslavia (1981)) to close to 90 percent in Uganda (Table C1). Twelve months after the devaluation, some of the impact change in the real exchange rate had been reversed except in those countries that had continued to depreciate. In several cases (Korea, Morocco, and Yugoslavia (1981)), the twelve-month real depreciation was significantly larger than the impact effect, as the currency had continued to depreciate in nominal effective terms. In another instance

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1/ Interest rates in the ECCA countries are set collectively, and the Liberian central bank is not a bank of issue. In the BCEAO countries there is an official money market, with freely determined interest rates for maturities of up to three months. Other rates are set collectively by the BCEAO, in the context of policies which aim, among other things, to maintain domestic rates consistent with foreign rates. The Central African Republic has a little more independence in its interest rate policy. The BEAC sets the discount rate, but each member country establishes the differential between the discount rate and commercial bank lending rates.

2/ For an exposition of the role of exchange rates in centrally planned economies, see Allen, "Prices, the Exchange Rate and Adjustment in Planned Economies," DM/82/34, May 1982.

(Zaire), the currency had continued to depreciate in nominal effective terms, but there was some reversal of the initial real depreciation. In the remaining cases the currency had ceased to depreciate in nominal effective terms or had appreciated, and the initial real depreciation had been fully or partly reversed; in the case of Yugoslavia (1980), stability of the nominal effective exchange rate was accompanied by a real appreciation over the predevaluation level. This trend continued during 1982, which generally included a substantial part of the second year following the initial devaluation. In four countries there was a substantial real effective appreciation during 1982, ranging from 7 percent to over 42 percent, while the real effective exchange rate index of Korea was relatively stable. The other countries for which data are available experienced real effective depreciations ranging from 3 percent to 7 percent, but in three of these cases another discrete devaluation had taken place in 1982. The partial reversal of the real depreciation in many cases reflected a rate of domestic price increase in excess of foreign inflation, due to the impact on nontraded goods of the change in prices of tradable and, in some cases, to a continuation of the overexpansionary policy stance that had contributed to the original overvaluation.

In most of the cases involving a step depreciation, there was an increase and liberalization of interest rates, accompanied by commitment to flexibility in interest rate policy. Mauritius raised the interbank rate by 50 percent, and the bank discount rate by 14 percent; Morocco raised interest rates by an average of 20 percent; and Somalia made wide-ranging modifications in the interest rate structure, raising the discount rate by 50 percent, unifying commercial bank lending rates, and raising deposit and lending rates. Uganda and Yugoslavia also raised interest rates during the period covered by the arrangement, and Thailand permitted higher deposit interest rates that had previously applied only to long-term instruments to be paid on deposits of shorter maturities as well.

In five other programs, exchange rate policy was an important component of the policy package, although no step depreciation was explicitly required. 1/ The real effective exchange rate index for the currency of Burma, which has been pegged to the SDR since 1977, depreciated by nearly 5 percent during 1981, but returned to the end-1980 level by the end of 1982. Exchange rate policy in Costa Rica, which had been formulated in the context of an acute foreign exchange crisis, was to involve no intervention by the authorities in the exchange market to counter fundamental changes. This commitment was not fulfilled with the result that the currency, which had depreciated by 74 percent in nominal effective terms during 1981, moved very little in 1982. As a result, the 60 percent real depreciation that accumulated during 1981

1/ However, in some of these cases the arrangement contained a review clause referring directly or indirectly to the appropriateness of the exchange rate.

was more than reversed during 1982. In the case of India, exchange rate adjustments were to be made when appropriate to promote external adjustment. The currency depreciated in real terms by 9 percent during the second half of 1981, and remained around that level through the end of 1982. The parallel market in Jamaica was legalized and the Bank of Jamaica was barred from intervening; the program also called for flexibility in the domestic interest rate structure. In the event, the real exchange rate (calculated as an average of the official and parallel market rates) appreciated by close to 11 percent during 1981-82. Finally, Pakistan delinked its currency from the U.S. dollar in early 1982 and there was a real depreciation of 16 percent during the year, more than reversing a small appreciation during 1981.

Exchange rate policy was not an important component of adjustment programs in the five remaining countries (Ethiopia, Madagascar, Mauritania, Sierra Leone, and Zambia), although there were indications that the exchange rate was not at an appropriate level in several cases. In lieu of exchange rate action exchange rate studies were to be made in some cases (Ethiopia, Madagascar, and Sierra Leone), and commitments were made to correct an accumulated appreciation (Mauritania), to reach agreement on exchange rate policy during future reviews (Madagascar), or to conduct periodic reviews of exchange rate policy (Zambia). In all of these countries the real effective exchange rate index appreciated by varying amounts ranging from 15 percent to over 60 percent during 1981-82. An explicit interest rate action was foreseen in only one case (Madagascar).

Table C1. Exchange Rate Changes in Selected Program Countries 1/

(In percent)

	Impact Change 2/		12-Month change		1981 3/		1982 3/	
	Nominal	Real	Nominal	Real	Nominal	Real	Nominal	Real
Country and date of devaluation								
Korea:								
Jan.-Feb. 1980	-16.2 4/5/	-5.8 4/5/	-29.9 4/	-9.9 4/	1.8	3.9	2.1	1.0
Mauritius:								
Sept. 1981	-17.6	-16.5	-13.3	-12.1	-10.2	-7.9	8.4	6.6
Morocco:								
Sept. 1980	-1.8 4/	-0.9 4/	-12.1 4/	-10.8 4/	-6.9 4/	-5.4 4/		
					-1.5	-2.0	-0.2	-3.9
Solomon Islands:								
Mar. 1981	-5.9	-5.8	-1.9	4.1	-2.9	2.2	-6.9	-3.0
Aug. 1982	-9.3 5/	-8.1 5/						
Somalia:								
July 1981	-39.6	-36.5	-34.5	-29.3	-29.2	-25.1	-20.2	-3.8
July 1982	-28.5	-28.2						
Thailand:								
July 1981	-7.2 6/	-7.3 6/	-1.7	-3.9	-2.5	0.1	10.4	6.9
Uganda:								
May 1981	-89.1	-87.7	-90.2	-84.9	-89.8	-72.8	-7.4	16.7
Yugoslavia:								
June 1980	-24.1 4/	-22.4 4/	-25.9 4/	2.5 4/				
July 1981 7/	-10.7 6/	-7.3 6/	-23.5	-8.9	-18.4	-0.5	-24.2	-6.4
Oct. 1982	-16.6	-15.5						
Zaire:								
June-July 1981	-39.0 5/	-33.9 5/	-35.4	-23.3	-34.5	-15.6	10.0	41.7

Source: Staff estimates.

1/ Monthly average effective exchange rate indices computed for surveillance purposes unless otherwise stated. Negative sign indicates depreciation.

2/ Change during the month of devaluation, unless otherwise indicated.

3/ December-December.

4/ Data from miscellaneous Fund documents (Staff Reports for Article IV consultations, reviews, or requests for use of Fund resources).

5/ Month following the month in which action was taken.

6/ Second month following the month in which action was taken.

7/ Although the depreciation of July 1981 has been presented here, there were also significant depreciations during March, August, November, and December 1981.

The Treatment of External Debt Rescheduling in the 1981 Arrangements

In recent years, an increasing number of Fund members have found it necessary to request a rescheduling of external commitments at the same time that they requested access to Fund resources. Although it would be preferable to formulate an adjustment program when the outcome of the rescheduling negotiations is known, creditors have normally required Fund members to conclude stand-by arrangements with the Fund before initiating firm discussions on rescheduling. Of the 27 programs under review, 12 explicitly envisaged rescheduling during the program period without stating the precise amounts and terms of debt relief. This section deals with the treatment of rescheduling in these programs, including some presentational aspects. For a more general discussion of the treatment of rescheduling in Fund programs, the reader is referred to "Fund Policies and External Debt Servicing Problems" (SM/83/45).

The presentation of debt rescheduling in staff memoranda accompanying requests for use of Fund resources varied considerably among the 12 programs. In five cases (the Central African Republic, Liberia, Mauritania, Somalia, and Uganda) rescheduling was envisaged, but no explicit assumption was made with regard to the actual amount of debt service payments that would be postponed. In the case of Jamaica, the balance of payments projection took the expected amount of debt rescheduling into account, but did not show it explicitly (it was consolidated with other capital inflows). In the case of Madagascar, the balance of payments showed an ex ante financing gap, which was expected to be closed by rescheduling or other exceptional balance of payments financing. Finally, in only five cases the balance of payments contained an entry which explicitly showed the assumed amount of debt service payments to be postponed; in three cases (Pakistan, Senegal, and Togo), the expected debt rescheduling was shown above the line, and in two cases (Sierra Leone and Zaire), it was shown as a financing item.

With the exception of Jamaica, Liberia, and Mauritania, mid-term reviews were scheduled in all of the programs that envisaged rescheduling, and with the exception of Togo, the review was a performance criterion. There was a clear tendency for programs which envisaged rescheduling to apply the review clause more often than other programs; 8 of 12 programs envisaging rescheduling planned a review as a performance criterion, compared with 2 of 15 programs in which no rescheduling was anticipated.

A phased reduction of external arrears was a performance criterion in 7 of the 12 programs which envisaged rescheduling. It was explicitly specified in three cases that the reduction in arrears had to be through cash payments (the Central African Republic, Madagascar, and Zaire). In the remaining four cases (Liberia, Sierra Leone, Somalia, and Uganda), it was not specified whether the reduction had to be through cash payments or rescheduling. In the cases where such a specification was not made, higher than anticipated rescheduling of arrears would make it possible to satisfy performance criteria under the arrangement with less use of foreign exchange and, consequently, a less stringent policy program.

The way rescheduling was treated in the financial programming exercise varied considerably. In the cases of Jamaica and Senegal, the performance criteria relating to domestic credit by the banking system were adjusted automatically so that the credit ceiling would be increased if the actual amount of debt service payments postponed fell short of expectations, and decreased if the actual amount proved to be larger than expected. In both cases, the credit ceiling was also made dependent on other exceptional balance of payments financing. The automatic adjustment was asymmetrical in that a shortfall in debt rescheduling below a certain limit would not trigger further increases in the credit ceiling, implying that such a shortfall would require the implementation of further policy measures in order to meet the objectives of the program.

In the case of the Central African Republic, the arrangement explicitly required that a further reduction of external arrears through cash payments should be undertaken if external debt service payments were rescheduled. Although an explicit assumption about the amount of postponed debt service payments was not made at the time when the program was designed, it was specified that funds made available through rescheduling of commitments vis-a-vis Paris Club members had to be used mainly for additional cash reductions in arrears. To assure this, it was established as a performance criterion that an agreement on a timetable for a further reduction in arrears had to be reached at the time of the mid-term review. Following the review, it was decided not to require a further reduction in arrears because actual commitments falling due exceeded the amounts provided for when the adjustment program was formulated. The case of Uganda is similar in that no assumptions were made with regard to the amount of debt service payments to be postponed. However, if rescheduling of commitments made additional funds available, the arrangement did not call for additional cash payment of arrears; instead, it was mentioned in the letter of intent that the resources thus made available could be used to ease the constraint on imports.

Components of Changes in the External Current Account Balance

Changes in the ratio of the external current account balance to GNP may be summarized by an arithmetic decomposition into terms that measure developments in price, market share, export market growth, interest payments, and other service account transactions. Such a calculation has been made for the countries under review for the period 1979-1982. 1/ In interpreting the results of the analysis, account should be taken of a number of limitations inherent in the data and methodology. Firstly, the individual terms of the decomposition sometimes represent exogenous developments but in most cases are endogenous and caused by other events; hence they do not necessarily represent causes of changes in the external current account balance, but rather are determined along with the observed movement in the current account. Secondly, the countries under review entered into arrangements with the Fund at various times during 1981 and not all of the economic programs that were approved continued in effect throughout 1982. The information for 1981 and 1982 is therefore best viewed as describing the broad experiences of countries with upper credit tranche arrangements during the period, rather than as capturing the effects of Fund-supported programs. Thirdly, the underlying data were developed in the context of the World Economic Outlook exercise and may not be identical with data included in staff reports describing individual country arrangements.

1/ A similar decomposition was presented in EBS/82/97, Supplement 1, 6/10/82, pp. 20-26, for the 23 countries which had programs during most of calendar year 1980. The decomposition of the average change in the ratio of the current account to GNP, $(CA_1/GNP_1)-(CA_0/GNP_0)$ is defined algebraically as follows: The effect of changing trade prices (row 2 of Tables E1 and E2) is $x_1(p_{x1} - p_{xo}) - m_1(p_{m1}-p_{m0})$. This term is comprised of two components, the impact of movements in the terms of trade on national income, $x_1[(p_{x1} - p_{xo})-(p_{m1} - p_{m0})]$; and the effects of differences between domestic and world inflation, $(x_1 - m_1)(p_{m1} - p_{m0})$. The effect of a changing export market share (row 3) is $p_{x0}\ x_1(a_1 - a_0)/a_1$. The effect of growth in export markets (row 4) is $x_0(g_x - g_y)/(1 + gy)$. The effect of a changing real import propensity (row 5) is $-p_{m0}(m_1 - m_0)$. The effect of changes in the investment income account is $(int_1 - int_0)$. The effect of changes in the rest of the service account (row 7) is $(s_1 - int_1)-(s_0 - int_0)$. The subscripts 1 and 2 refer to the period for which the decomposition applies and the prior year respectively. "CA" stands for the current account balance (positive represents a surplus); "x" for the ratio of real exports to real GNP; "m" for the ratio of real imports to real GNP; "p_x" for the ratio of export prices to the GNP deflator; "p_m" for the ratio of import prices to the GNP deflator; "int" for the ratio of the investment income account to GNP; "s" for the ratio of the net service account to GNP; "a" for the share of a country's exports in its export market (a weighted average of its partner countries' non-oil import bundle); "g_y" for the growth rate of real GNP; and "g_x" for the growth rate of the country's export market.

Finally, the terms of the decomposition are presented as averages across subsamples of countries which have common characteristics, but there was a wide diversity of experience; despite differences in averages from one subgroup to another, there is often much overlapping among the subsamples.

The external current account balance of the countries under review worsened on average by a cumulative 2.5 percentage points of GNP during 1979-80 and by a further 0.4 percentage points during 1981-82 (Table E1). The deterioration reflected mainly adverse developments in the prices of imports and exports (line 2), which comprise two components: (i) the impact of movements in the terms of trade on national wealth (i.e., the change in the amount of imports that can be purchased with export proceeds), and (ii) the effect of differences between domestic and world inflation on the ratio of the current account deficit to GNP. 1/ The impact of other mostly exogenous factors was less adverse over the period. There was a modest positive stimulus equivalent to 1.6 percent of GNP from export market growth (line 4) during 1979-80. 2/ As the recession deepened in 1981, this source of improvement fell to 0.3 percent of GNP and in 1982 export markets contracted slightly. Growing net interest payments (line 6) on all debt, public and private, affected the current account ratio adversely by an average of 0.4 percentage points of GNP in each of the four years. The lack of movement of this term when interest rates rose substantially in 1980 and 1981 reflects the predominance in the sample of low-income countries, for which most debt is concessional or on fixed terms. The impact of all mostly exogenous factors (the sum of lines 2, 4, and 6) was positive in 1979, but thereafter there was an adverse effect averaging 2 percentage points of GNP per year. 3/

The deterioration in the mostly exogenous elements of the external current account ratio was counterbalanced to some extent by developments in other components, which measure factors that are largely endogenous. The export market share rose marginally in 1979 and fell slightly in

1/ When a country with a current account deficit experiences more rapid domestic inflation than the increase in import and export prices (assuming real output and trade are unchanged), nominal GNP grows more rapidly than nominal imports and there is a decline in the ratio of the current deficit to GNP.

2/ The export market is defined as a weighted average of industrial country export destinations, with weights proportional to importance among destinations. Growth is measured by the increase in volume of total non-oil imports in these markets relative to the growth of GNP of the exporting countries.

3/ Although these terms may be considered as mostly exogenous, they contain elements which are clearly endogenous such as the domestic price component in the trade price term and the fact that interest payments depend on the quantity of debt as well as movements in the interest rate.

each of the three following years. 1/ The impact of the real import propensity (line 5), which is positive when import volume expands more slowly than real GNP, added about 0.9 percent on average to the current account deficit in 1979, but contributed to a cumulative improvement equivalent to 4.9 percent of GNP in the external current account ratio during 1980-82. This term is sometimes an indication of adjustment of import demand levels, but may also reflect the existence of exchange and trade controls when availability of foreign finance is constrained.

There were distinctive differences in the external current account experience of countries pursuing different types of adjustment strategies, both in terms of the external environment and in the accommodation of exogenous circumstances. There was an average cumulative improvement equivalent to 1.9 percent of GNP during 1981-82 for countries with programs aimed mainly at demand restraint, while countries following a structurally oriented or mixed adjustment strategy experienced an average cumulative worsening of 2.5 percent and 1.0 percent of GNP, respectively (Table E2). Although countries with programs based on demand restraint and mixed objectives faced more severe exogenous shocks, lower real import propensities in these countries contributed a cumulative 7.3 percent and 4.1 percent of GNP, respectively, toward current account improvement. By contrast, lower real import propensities contributed to an improvement of only 0.2 percent of GNP for countries with structurally oriented programs. Lower current account deficits and the containment of import demand were generally important objectives of the adjustment strategies aiming mainly at demand restraint, while structurally oriented programs often included a widening of current account deficits in the initial stages of the adjustment process. Another difference among the groups is the better average export performance of countries with structurally oriented programs; export market shares (line 3) accounted on average for a cumulative improvement of 1.0 percent of GNP for these cases, while market shares contracted over the period for the other countries, worsening the deficit by an average cumulative 2.4 percent for the demand restraint group and 1.3 percent for those with mixed objectives. Considerable emphasis was generally given to export promotion in the countries with structurally oriented adjustment programs.

1/ This term is calculated as the difference between the growth rate in the volume of exports and that of the country's export markets. It reflects many influences including the responsiveness of exporters to changes in export market growth, domestic profitability of exports, external competitiveness, and domestic demand for exportables.

Table E1. Changes in the External Current Account Balance of Program Countries, 1979-82 1/

(In percentage points of GNP)

	1979	1980	1981	1982	1979-1982
1. Average change in ratio of current account balance to GNP	-1.7	-0.8	-0.3	-0.1	-2.9
2. Effect of changing trade prices	0.3	-1.7	-2.4	-1.5	-5.3
3. Effect of changing export market share	0.3	-0.2	-0.7	-0.3	-0.9
4. Effect of growth in export markets	0.7	0.7	0.3	-0.1	1.6
5. Effect of changing real import propensity	-0.9	0.7	2.2	1.9	3.9
6. Effect of changing interest payments on external public debt	-0.3	-0.6	-0.3	-0.5	-1.7
7. Effect of changes in rest of service account	-1.8	0.3	0.6	0.4	-0.5
Memorandum item:					
8. Sum of lines 2, 4, and 6	0.7	-1.6	-2.4	-2.1	-5.4

Source: Staff estimates.

1/ Unweighted averages for the countries under review, excluding Dominica, for which movements in the current account ratio have been extremely large. A positive entry represents a factor that raises the current account surplus or reduces the deficit.

Table E2. Changes in the External Current Account Balance of Program Countries Classified by Adjustment Strategy, 1981-82

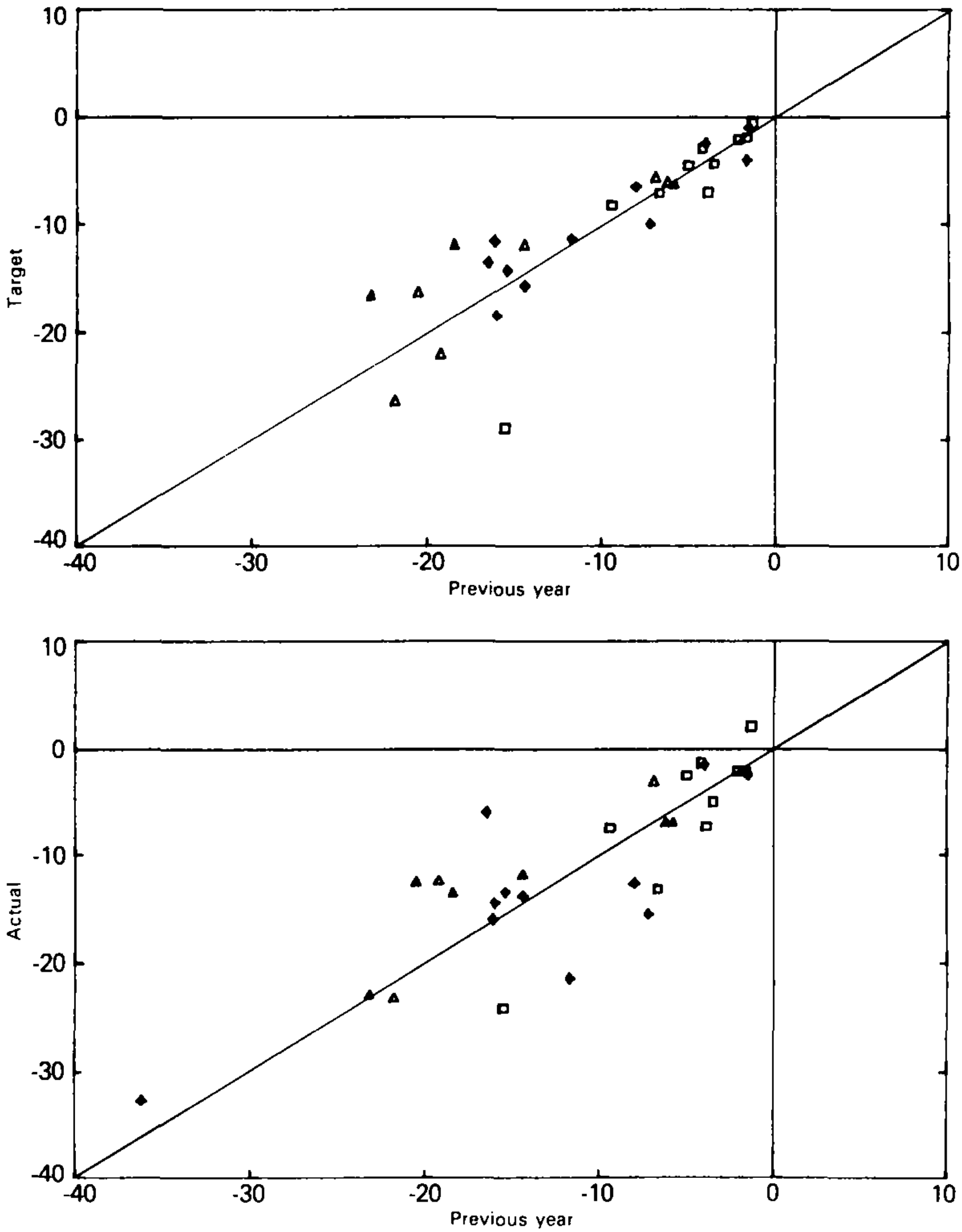
(In percentage points of GNP)

	All Countries		Adjustment Strategy: Demand Restraint		Adjustment Strategy: Structurally Oriented		Adjustment Strategy: Mixed Objectives	
	1981	1982	1981	1982	1981	1982	1981	1982
1. Average change in ratio of current account balance to GNP	-0.3	-0.1	1.0	0.9	-2.3	-0.2	--	-1.0
2. Effect of changing trade prices	-2.4	-1.5	-4.0	-0.9	-1.0	-0.3	-2.0	-2.9
3. Effect of changing export market share	-0.7	-0.3	-1.2	-1.2	0.8	0.2	-1.4	0.1
4. Effect of growth in export markets	0.3	-0.1	1.0	0.3	-0.1	-0.6	0.2	-0.2
5. Effect of changing real import propensity	2.2	1.9	4.5	2.8	0.4	-0.2	1.4	2.7
6. Effect of changing interest payments on external public debt	-0.3	-0.5	-0.1	-0.7	-0.7	0.1	-0.2	-0.8
7. Effect of changes in rest of service account	0.6	0.4	0.8	0.6	-1.7	0.6	2.0	--
Memorandum item:								
8. Sum of lines 2, 4, and 6	-2.4	-2.1	-3.1	-1.3	-1.8	-0.8	-2.0	-4.2

Source: Staff estimates.

Chart 1

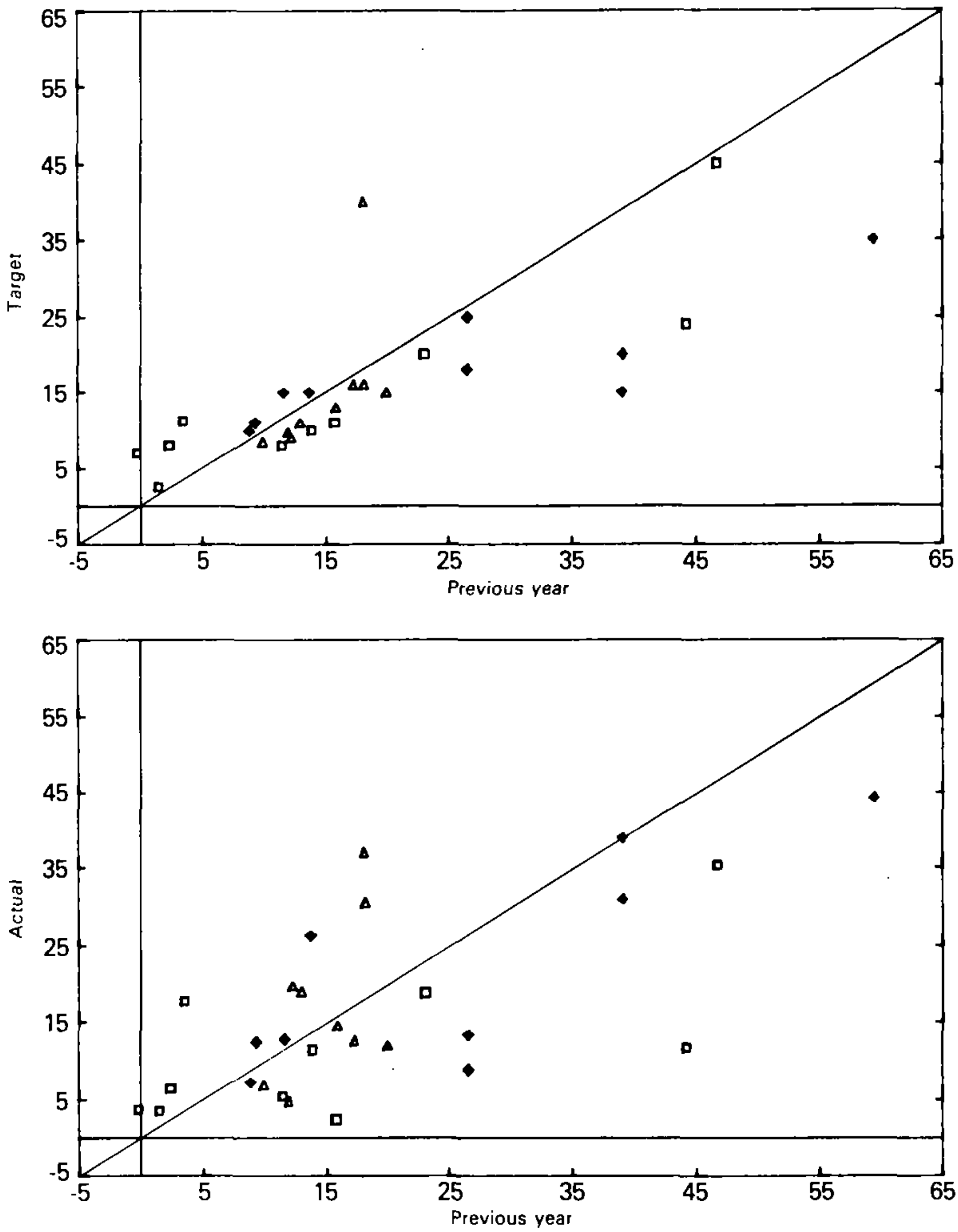
TARGETED AND ACTUAL EXTERNAL CURRENT ACCOUNT DEFICIT



Note: The above charts show the ratio of the current account to GDP for the year prior to each annual program on the horizontal axis. The corresponding targeted and actual current account ratios for the subsequent annual program are shown on the vertical axis above and below respectively. Countries with structurally-oriented programs are depicted by squares, countries with demand-restraint programs are depicted by triangles, and countries with mixed objective programs are depicted by crossed diamonds. Points above the 45 degree line in each chart represent targeted and actual improvements in the current account ratio, compared to those in the previous year. The difference in the vertical position between the two charts, for any particular observation, depicts the difference between the targeted and actual outcome.

Chart 2

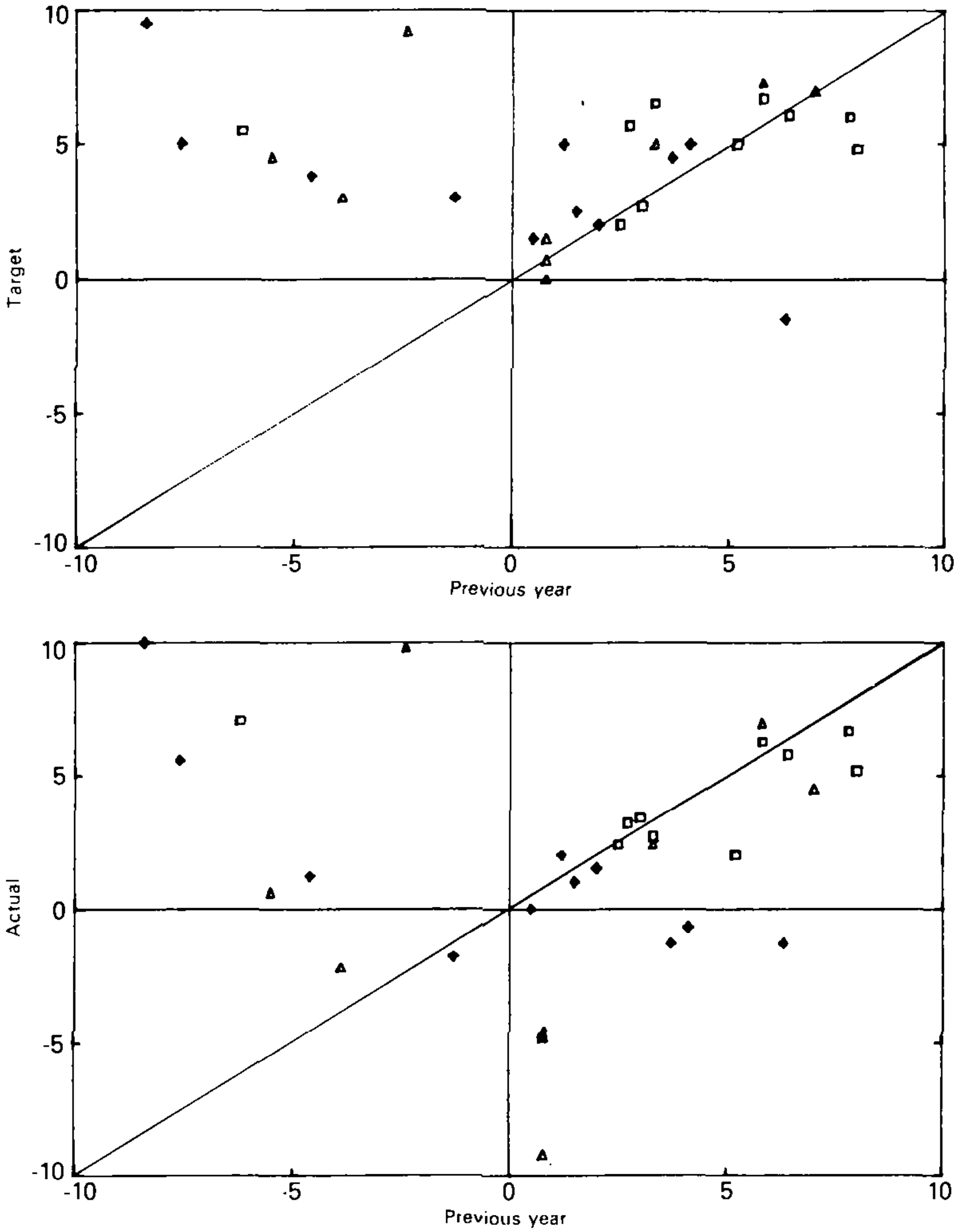
TARGETED AND ACTUAL INFLATION RATE



Note: The above charts show the rate of increase of the consumer price index or when applicable, the wholesale price index for the year prior to each annual program on the horizontal axes. The corresponding targeted and actual rates of inflation for the subsequent annual program are shown on the vertical axis above and below respectively. Countries with structurally-oriented programs are depicted by squares, countries with demand restraint programs are depicted by triangles, and countries with mixed objective programs are depicted by crossed diamonds. Points above the 45 degree line in each chart represent targeted and actual increases in the rate of inflation larger than those in the previous year. The difference in the vertical position between the two charts, for any particular observation, depicts the difference between the targeted and actual outcome.

Chart 3

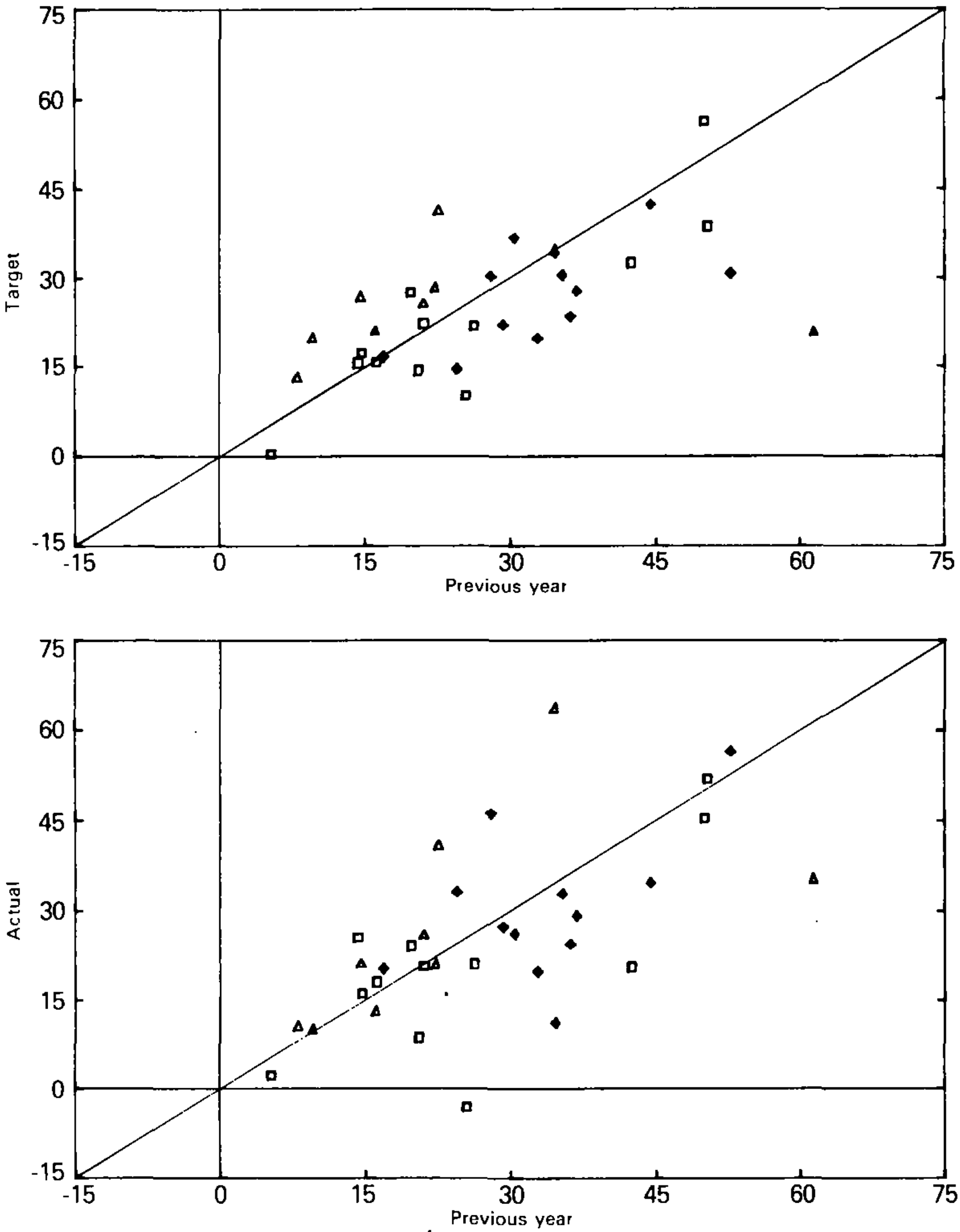
TARGETED AND ACTUAL REAL ECONOMIC GROWTH



Note: The above charts show the real growth rate for the year prior to each annual program on the horizontal axes. The corresponding targeted and actual real growth rates for the subsequent annual program, are shown on the vertical axis above and below respectively. Countries with structurally-oriented programs are depicted by squares, countries with demand-restraint programs are depicted by triangles and countries with mixed objective programs are depicted by crossed diamonds. Points above the 45 degree line in each chart represent targeted and actual improvements in the rate of real growth compared to the previous year. The difference in the vertical position between the two charts, for any particular observation, depicts the difference between the targeted and actual outcome.

Chart 4

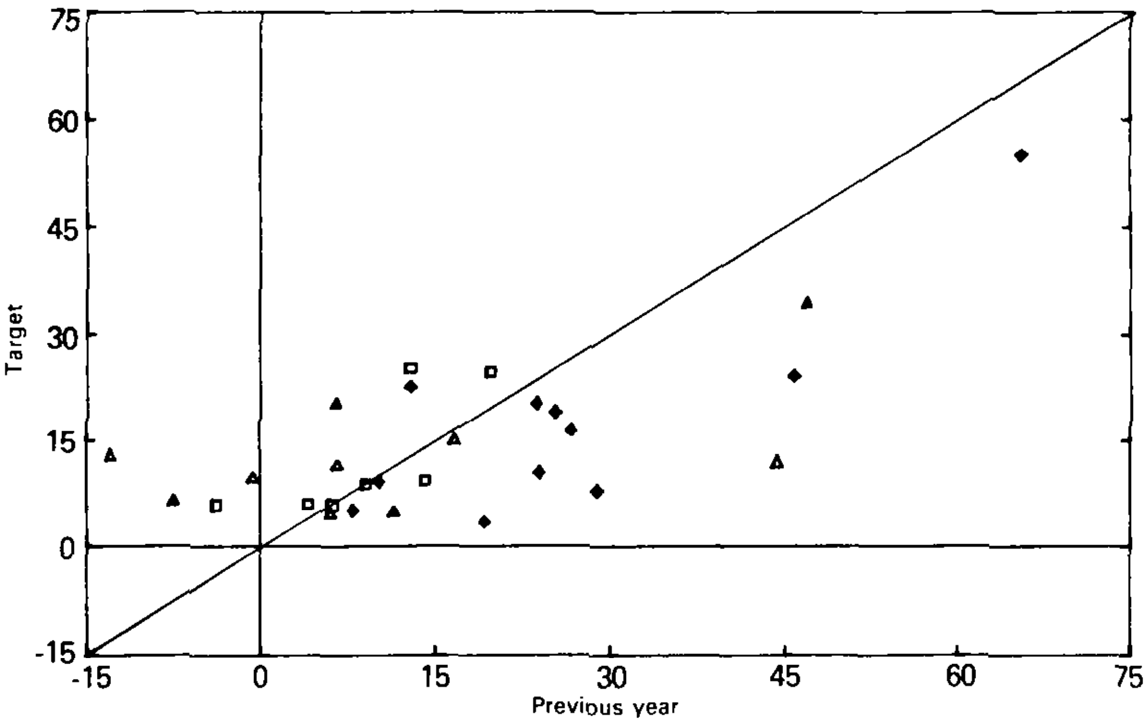
TARGETED AND ACTUAL DEVELOPMENTS IN TOTAL CREDIT

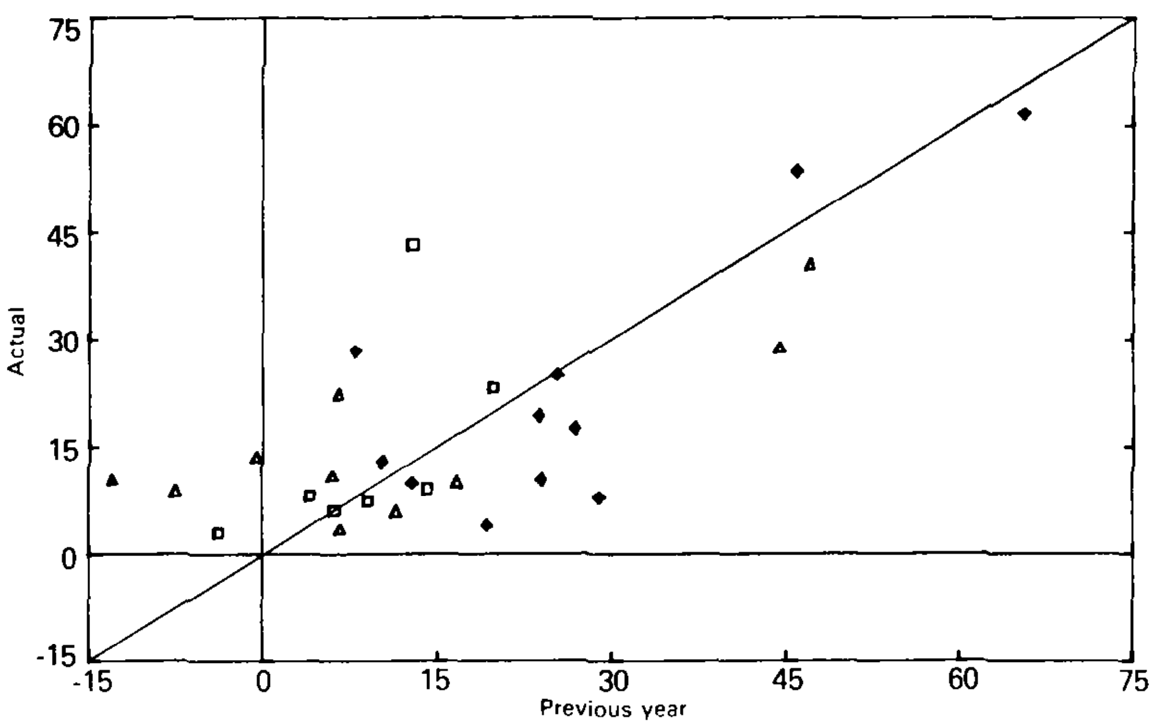


Note: The above charts show the rate of growth of overall credit or when applicable, net domestic assets of the central bank (measured as a percentage of broad money) for the year prior to each annual program, on the horizontal axes. The corresponding targeted and actual rates of growth for the subsequent annual program are shown on the vertical axis above and below respectively. Countries with structurally-oriented programs are depicted by squares, countries with demand-restraint programs are depicted by triangles, and countries with mixed objective programs are depicted by crossed diamonds. Points above the 45 degree line in each chart represent targeted and actual increases in credit expansion larger than those in the previous year. The difference in the vertical position between the two charts, for any particular observation, depicts the difference between the targeted and actual outcome.

Chart 5

TARGETED AND ACTUAL DEVELOPMENTS IN CREDIT TO THE PUBLIC SECTOR

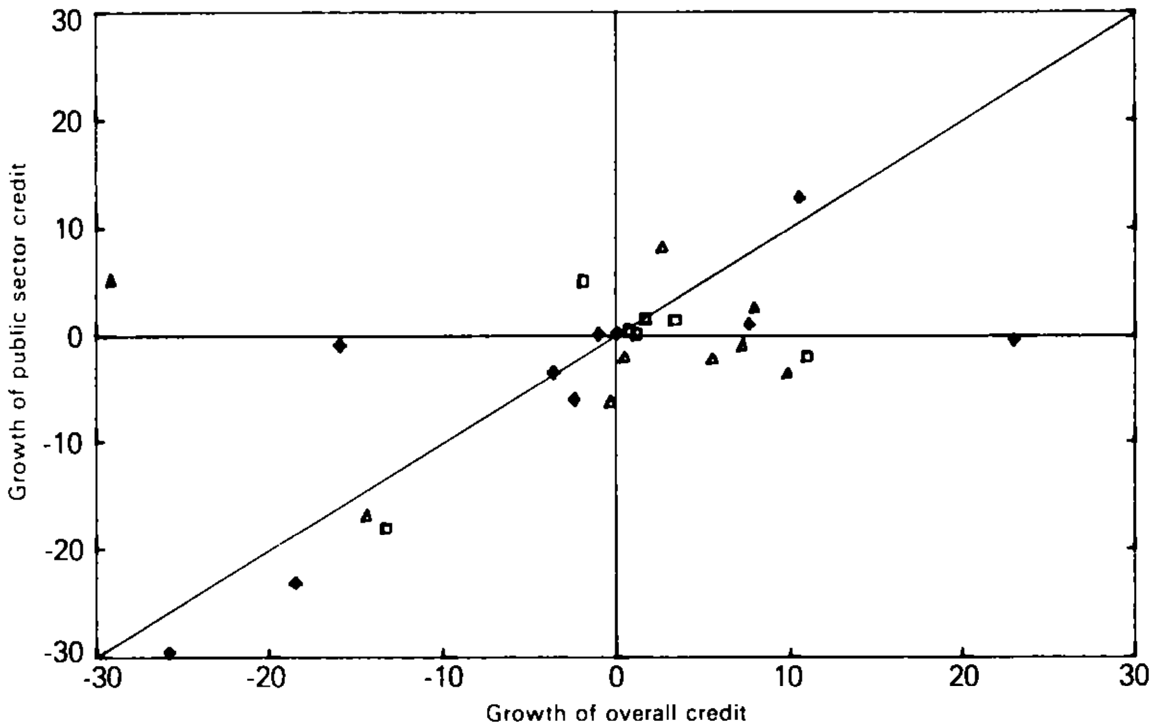




Note The above charts show the rate of growth of credit to the public sector or when applicable, credit to the government (measured as a percentage of broad money) for the year prior to each annual program, on the horizontal axes The corresponding targeted and actual rates of growth for the subsequent annual program are shown on the vertical axis above and below respectively. Countries with structurally oriented programs are depicted by squares, countries with demand-restraint programs are depicted by triangles, and countries with mixed objective programs are depicted by crossed diamonds Points above the 45 degree line in each chart represent targeted and actual increases in credit expansion larger than those in the previous year The difference in the vertical position between the two charts, for any particular observation depicts the difference between the targeted and actual outcome

Chart 6

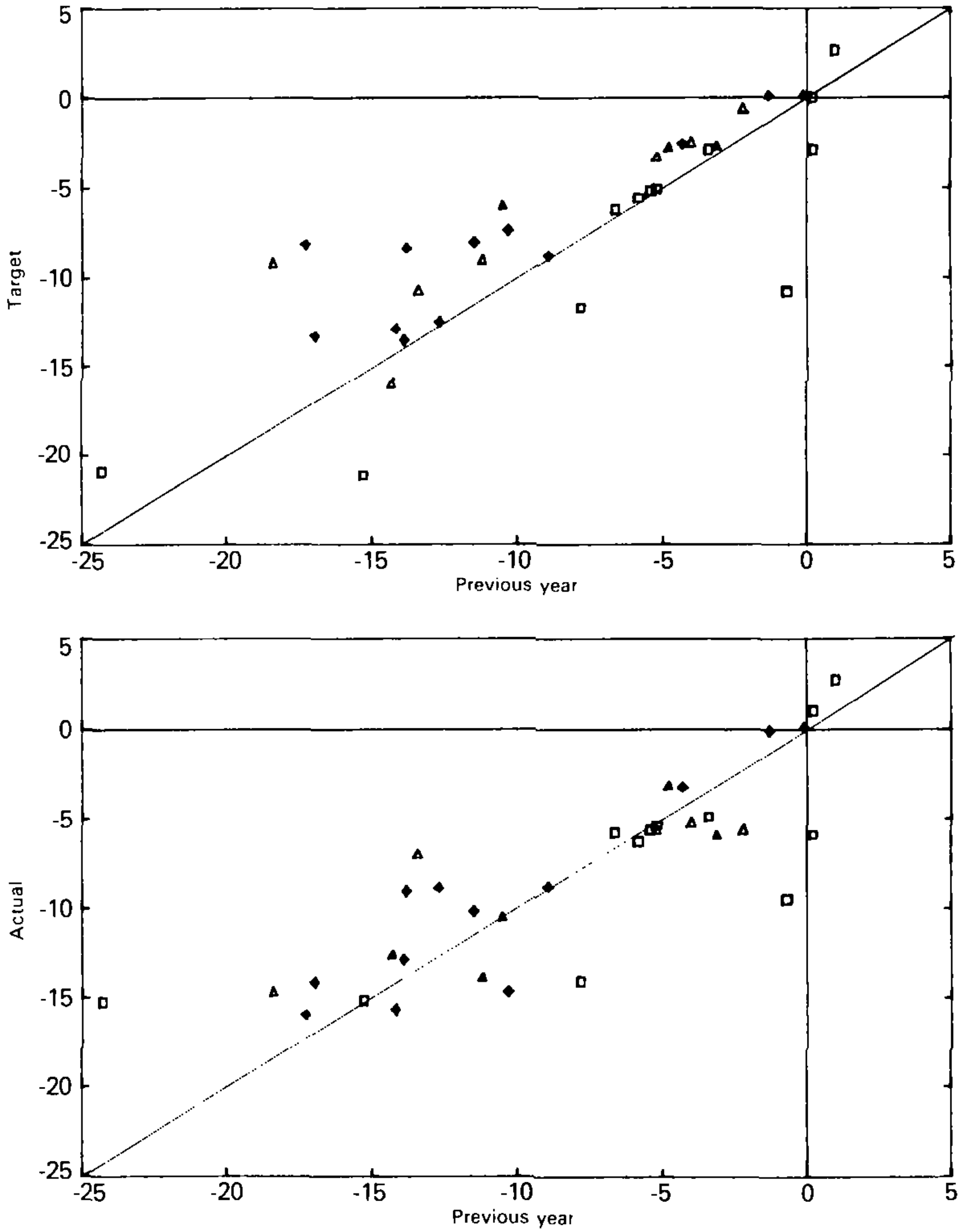
DEVIATIONS FROM TARGETED GROWTH OF TOTAL CREDIT AND CREDIT TO THE PUBLIC SECTOR



Note: The above charts show the deviation of actual from targeted performance of overall credit growth (or where applicable net domestic assets of the central bank) on the horizontal axis, and the deviation of actual from targeted performance of credit growth to the public sector on the vertical axis. Both variables are measured as the deviation in percentage points of the initial base of broad money, so that negative entries represent excess growth over targets. Countries with structurally-oriented programs are depicted by squares, countries with demand-restraint programs are depicted by triangles, and countries with mixed structural and demand programs are depicted by crossed diamonds. The 45 degree line shows the relation between deviations from targets of public sector credit and deviations from target of overall credit.

Chart 7

TARGET AND ACTUAL PUBLIC SECTOR FISCAL DEFICIT



Note The above charts show the ratio of the overall deficit of the government to GDP for the year prior to each annual program, on the horizontal axes. The corresponding targeted and actual ratios of the deficit to GDP for the subsequent annual program are shown on the vertical axis above and below respectively. Negative entries represent deficits. Countries with structurally-oriented programs are depicted by squares, countries with demand-restraint programs are depicted by triangles, and countries with mixed objective programs are depicted by crossed diamonds. Points above the 45 degree line in each chart represent targeted and actual improvements in the deficit-GDP ratio compared to those in the previous year. The difference in the vertical position between the two charts, for any particular observation, depicts the difference between the targeted and actual outcome.