FOR AGENDA

SM/83/205

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October 13, 1983

To: Members of the Executive Board

From: The Secretary

Subject: Guyana - Staff Report for the 1983 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1983 Article IV consultation with Guyana, which will be brought to the agenda for discussion on a date to be announced.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. J. E. Gonzalez, ext. 73371.

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INTERNATIONAL MONETARY FUND

GUYANA

Staff Report for the 1983 Article IV Consultation

Prepared by Western Hemisphere Department

(In consultation with the Exchange and Trade Relations, Legal, and Treasurer's Departments)

Approved by E. Wiesner and W.A. Beveridge

October 12, 1983

I. Introduction

The 1983 Article IV consultation discussions 1/ with Guyana were conducted in Georgetown during the period July 27-August 12, 1983. Representatives of Guyana in the consultation discussions included the Minister of Finance, the Chairman and other senior officials of the State Planning Secretariat; the Governor and other senior officials of the Bank of Guyana; and senior officials of the Ministries of Agriculture, Energy and Mines, and Manufacturing and Industrial Development. The mission had discussions with the chairmen and senior officials of the Guyana State Corporation (GUYSTAC), the Guyana Sugar Corporation (GUYSUCO), the Guyana Rice Board, the Guyana Mining Enterprise (GUYMINE), the National Energy Commission and the Guyana Electricity Corporation. The mission also had contacts with representatives of Guyana's private manufacturing sector and banking community and with representatives of the Trade Unions Congress (TUC). The staff mission consisted of Julio E. Gonzalez (Head), Frits van Beek, Susana Sosa, Roberto Ramaciotti (all WHD), Girma Begashaw (ETR), Anne K. McGuirk (RES), and Dorothy Quelch (Secretary-WHD).2/

The previous consultation discussions with Guyana were held July-August 1982. The relevant documents, SM/82/201 and SM/82/202, were considered by the Executive Board on November 5, 1982 (EBM/82/142).

As of September 21, 1983, Guyana had overdue payments to the Fund amounting to SDR 8 million (see Appendix I for details).

1/ Guyana accepted the obligations of Article VIII, Sections 2, 3, and 4 of the Articles of Agreement on December 27, 1966.

2/ Mr. J. Sackey, from the IBRD, participated in all of the meetings.

II. Background to the Discussions

Guyana's economy prospered in 1974-76 under the influence of buoyant world market conditions for sugar and bauxite. In 1977 the economy suffered a setback as both sugar production fell and sugar prices declined abruptly. By the end of that year, Guyana's international reserves had been depleted and external payments arrears on current account transactions were accumulating rapidly. In early 1978 the authorities embarked on an adjustment program with the Fund that was supported by a one-year program in the upper credit tranches. The successful implementation of the program resulted in a shift of public sector savings from a negative 3 percent of GDP in 1977 to a positive 4 1/2 percent in 1978. At the same time there was a drastic reduction in the current account deficit of the balance of payments, from 23 percent of GDP in 1977 to 6 percent in 1978. However, output continued to fall as a result of unstable labor relations and poor weather conditions.

The one-year stand-by program was followed in mid-1979 by a three-year program supported with an extended arrangement. Instead of improving as planned, however, Guyana's economic situation deteriorated during 1979. Real GDP declined by 1 1/4 percent because of a fall in agricultural production and a sharp reduction of output in the bauxite industry arising from breakdowns of equipment and a five-week work stoppage. These production setbacks and a further deterioration in the terms of trade contributed to a widening of the current account deficit of the balance of payments to the equivalent of 16 percent of GDP. The oil import bill which had risen from the equivalent of less than 5 percent of GDP before 1973 to about 11 1/2 percent in 1974 reached 18 1/2 percent in 1979.

Economic conditions remained depressed in 1980. Sugar and bauxite production were hampered mainly because of the effects of an ongoing dispute over wages. The production problems led to a major decline in export earnings and forced a cutback in imports. The extended arrangement was canceled in mid-1980 and replaced in July 1980 by a new three-year extended arrangement for SDR 100 million, which was increased in the second year of the program to SDR 150 million, the equivalent of 400 percent of Guyana's quota. This arrangement aimed at increasing the rate of economic growth, which had declined for the third consecutive year to a level 10 percent below that of 1976, and strengthening the public finances and the balance of payments. The program was supported by an IBRD Structural Adjustment Loan of US$14 million and IDA credit of US$8.0 million. The Bank group financing of the program involved the provision of foreign exchange to meet critically needed imports for export-oriented industrial and agricultural operations in both the public and private sectors. In the case of the manufacturing sector, the Bank group assistance was channelled through a revolving Export Development Fund (EDF) for US$8 million. The role of the EDF was to provide foreign exchange to finance intermediate goods imports in order to facilitate the expansion of manufactured exports.

Performance under both programs was disappointing and drawing rights under the Fund program were interrupted shortly after the beginning of the second program year. Guyana's poor economic performance can be traced to the failure to obtain satisfactory output levels in the three main producing sectors and to lax demand policies. The output of bauxite in 1981 was just about three fourths the level of 1977; rice production suffered a similar decline over a five-year period and sugar production stagnated. The factors behind these production declines related to lack of price incentives to producers, marketing and management problems, an acute shortage of skilled manpower, frequent plant breakdowns that reflected in part insufficient foreign exchange for the purchase of spare parts, and, in the case of rice and sugar production, adverse weather conditions in some years.

As a result, the macroeconomic performance of the first two years of the EFF program fell short of the targets set. Real GDP, which was projected to increase at an average annual rate of 6 percent during 1981-82, declined by more than 5 percent, while gross national income declined by about 7 1/2 percent per annum. At the same time, the share of consumption in GDP rose to 87 percent during 1981-82, compared to projected shares of 81-82 percent. Gross domestic savings declined sharply and averaged less than 7 percent of GDP during this period, i.e., more than one third below the projected level in the EFF and SAL programs of 14-18 percent of GDP. The disappointing savings performance resulted from a sharp deterioration in public sector finances. Central government operations deviated from program targets mainly because of higher expenditure for wages and defense. The poor production and export performance also had an adverse effect on the revenue of the Central Government and the earnings of public sector corporations, and consequently the overall deficit of the public sector in 1981 rose to almost 45 percent of GDP in comparison with the programed 23 percent. The deterioration in the public sector finances resulted in heavy reliance on domestic bank credit.

The economic situation reached crisis proportion during 1982. According to preliminary data, real GDP is estimated to have fallen by more than 10 percent (Table 1). The sectors most affected were bauxite mining which declined by over 30 percent, manufacturing (especially food, beverage, and tobacco industries) which declined by some 13 percent, the construction and service sectors which declined by about 10 percent and the sugar industry (a 5 percent decline). The drop in manufacturing and commercial activity was in large measure a consequence of the lack of inputs and finished goods because of foreign exchange shortages.

The current account deficit of the balance of payments remained high, the equivalent of 29 percent in 1982. Exports channeled into the official market declined by 30 percent in U.S. dollar terms in 1982, reflecting, in addition to domestic output problems, depressed foreign demand for bauxite and a decline of about one half in the value of rice

exports due to increased illegal sales and loss of markets. Imports fell by more than one third from the 1981 level, reflecting the lack of foreign exchange and the drying up of credit facilities. The deficit in the service account is estimated to have been about US$95 million, of which US$47 million represented accrued interest payments. Guyana has virtually stopped foreign debt service payments except for those arising from the nationalization of foreign companies, and multilateral loans. The overall balance of payments deficit amounted to almost US$130 million in 1982, of which US$125 million represented an increase in external payments arrears.

Table 1. Guyana: Selected Macroeconomic Indicators

	1979	1980	1981	Prel. 1982	Proj. 1983
(Annual percentage change)					
Real GDP at factor cost	-1.4	1.6	-0.3	-10.4	-8.1
Real GDP per capita	-1.7	1.1	-0.4	-6.8	-6.7
GDP at current market prices	5.2	13.7	5.9	-9.1	-4.6
GDP implicit deflator (at factor cost)	5.3	11.5	1.3	3.4	-4.3
National income at current prices	1.7	13.4	-5.4	-9.6	-18.3
Terms of trade	3.8	-2.2	-16.2	-13.7	...
Urban consumer price index					
End of period	19.4	8.5	29.0	19.3	...
Period average	17.8	14.1	22.2	21.0	...
(As percent of GDP)					
Public sector savings	4.1	3.1	-16.4	-18.9	-33.7
Public sector overall deficit	-16.7	-21.7	-44.5	-46.8	-57.8
Current account of the balance of payments	-16.3	-17.9	-32.9	-29.3	-28.3

Sources: Statisitcal Bureau of Guyana; and Ministry of Finance.

As of December 31, 1982, external payments arrears amounted to US$208 million. Of this total, commercial arrears were US$98 million; arrears on the servicing of the external public debt were US$37 million, and arrears on the Bank of Guyana's short-term debt were US$73 million. More than 80 percent of this last amount corresponded to unsettled obligations under the Caribbean Multilateral Clearing Facility (CMCF),

mostly originating in oil imports from Trinidad and Tobago. At the end of 1982, gross official reserves amounted to about US$10 million, and net international reserves (counting arrears as liabilities) were negative by about US$372 million (Table 2).

Guyana's medium- and long-term public debt has increased rapidly in recent years and at the end of December 1982 the outstanding debt was US$660 million, equivalent to about 137 percent of GDP as compared with US$496 million in 1979, or 95 percent of GDP. In 1982 the ratio of actual debt service payments to exports of goods and services fell to about 18 percent from 29 percent in 1979, as Guyana was unable to service all debts. During 1982 agreement was reached with commercial banks for a deferral of principal payments (US$15 million) and with a number of bilateral creditors for the rescheduling of debts (US$35 million), but the main bilateral creditors have made debt rescheduling conditional upon agreement on a program with the Fund (Table 3).

During 1982 there was an expansion of the unofficial exchange market, and it is estimated that unrecorded exports amounted to about 50 percent of officially recorded exports. The exchange rate in the unofficial market is reported at between G$9 to G$10 per U.S. dollar, compared with the official rate of G$3 per U.S. dollar. Payments in the unofficial exchange market are financed mainly by illegal exports of gold, diamonds, rice and some agricultural and industrial products. The fiscal implications of the existence of this parallel economy are substantial. Revenue shortfalls in 1982 on this account are estimated to have been the equivalent of at least 10 percent of the revenue of the Central Government. In addition, the system of domestic price controls in the face of expansionary domestic policies has generated a parallel market for commodities, where prices are at least double and often three times those in the controlled market. These prices are not taken into account in the calculation of the CPI, which rose by an average of 21 percent in 1982, up from an annual average of 17 percent in the period 1978-81.

The overall deficit of the public sector was reduced in 1982, but in relation to GDP it increased slightly (to almost 47 percent); the cutback fell short of the amount that had been planned by the authorities, as a decline in the current deficit of the Central Government was more than offset by the operating deficits of the public corporations. Because of a sharp reduction in foreign financing, capital expenditure of the public sector was reduced by almost 4 percentage points of GDP. About 90 percent of the public sector deficit was financed with central bank credit.

Net domestic assets of the banking system expanded by about 34 percent during 1982, reflecting for the most part the increase in bank credit to the public sector. Liabilities to the private sector increased by 25 percent, and there was a decline in the net foreign assets of the banking system, as was mentioned above.

Table 2. Guyana: External Payments Arrears

(In millions of U.S. dollars)

	December 31				June 30
	1979	1980	1981	1982	1983
Total arrears	29.4	46.4	82.7	208.3	307.3
Arrears with deposits	26.9	27.5	49.1	97.7 1/	125.6 1/
Merchandise	...	...	34.3	68.1	...
Other current payments	...	...	10.2	25.0	...
Valuation adjustment	--	--	4.6	4.6	4.6
Bank of Guyana arrears	2.5	18.9	23.6	72.9	97.7
Interest on bilateral deposits	2.5	3.4	7.9	12.9	18.8
CARICOM clearing facility	--	15.5	15.7	60.0	78.9
Principal	(--)	(15.5)	(14.8)	(57.1)	(76.6)
Interest	(--)	(--)	(0.9)	(2.9)	(2.3)
Central government debt	--	--	1.0	34.5	61.9
Principal	--	--	0.8	24.0	45.7 2/
Interest	--	--	0.2	10.5	16.2 2/
Public corporations' debt	--	--	9.0	3.2	22.1
Nationalization loans arrears	--	--	9.0 3/	--	--
Other	--	--	--	3.2	22.1 2/

Source: Bank of Guyana.

1/ Arrears on account of merchandise and other current payments without local currency deposits are estimated at US$30-35 million. This would raise total arrears to US$238.3 million to US$243.3 million at end-1982, and to US$337.3 million to US$342.3 million at end June 1983.

2/ Sum of arrears at end-1982 and arrears on account of debt service payments of medium- and long-term public debt.

3/ Paid for by bauxite shipment to ALCAN during the first quarter of 1982.

Table 3. Guyana: Medium- and Long-Term External Public Debt

(In millions of U.S. dollars; end of period)

	1979	1980	1981	1982
Total external debt	496.3	554.1	647.4	660.9
Bilateral	219.6	231.8	290.8	281.6
Multilateral	70.8	107.3	169.6	201.6
Financial institutions	95.7	107.9	98.6	99.3
Suppliers' credits	25.3	26.3	21.4	18.6
Nationalization loans	71.3	66.3	60.4	54.3
Bonds	13.5	14.5	6.6	5.6
Total debt service paid	91.3	69.5	80.2	48.9
Amortization	66.1	42.8	44.1	24.8
Interest	25.2	26.7	36.1	24.1
Ratios (in percent)				
Total debt/GDP	95.4	93.7	113.9	136.6
Debt service/exports of goods and services	29.0	16.9	21.5	18.5
Interest payments/exports of goods and services	8.0	6.5	9.7	9.1
Memorandum items				
Scheduled debt service payments	91.3	69.5	90.2	76.6
Amortization	(66.1)	(42.8)	(53.9)	(42.2)
Interest	(25.2)	(26.7)	(36.3)	(34.4)
Debt service/exports of goods and services (in percent)	29.0	16.9	24.2	28.9
Interest payments/exports of goods and services (in percent)	8.0	6.5	9.7	13.0

Sources: IBRD, External Debt Report System, and Bank of Guyana.

III. Economic Prospects and Policies

The key questions in the consultation discussions were how Guyana would redress the serious breakdown in the production process and the financial imbalances that are affecting the economy. Thus, the discussions centered on (1) the causes of the deterioration in the productive process in Guyana and especially the problems related to the price structure and marketing of the more important export sectors: rice, sugar, and bauxite; and (2) the means by which domestic expenditure would be brought into line with the country's reduced income with the goal of re-establishing the conditions for the resumption of economic growth.

1. Supply policies

The authorities said that the major problem facing Guyana was that of stimulating domestic production. The solution of this problem was essential to generate the income needed for improving consumption standards and financing the investment required for sustained growth. In their view, overall production has been curtailed primarily by the adverse international market conditions facing bauxite, sugar and rice--the main traditional sources of foreign exchange. They said another important factor has been the lack of foreign exchange which has inhibited the flow of imported inputs and spare parts necessary for the use of existing productive capacity to serve both the domestic and export markets. Also playing a role was the tardy flow of foreign funds contractually committed to agreed projects of the investment program.

However, the authorities noted that measures aiming at the correction of certain structural deficiencies in the main productive sectors had already been put into place, and that further action in this direction was contemplated. Specifically, in May 1982 the Government announced a program aimed at increasing economic efficiency in the public corporations and redefining the role of the public and private sectors in the economy. The main measures taken or to be taken as part of the action program are: (a) contracts with two foreign companies were signed to study the viability of the bauxite industry and provide direct on-site assistance; (b) in the rice sector, the Government put into effect measures to decentralize and reduce the functions of the Guyana Rice Board; (c) in the sugar sector, the Government has been implementing a three-year rationalization program with the objective of increasing yields and reducing the unit cost of production; (d) measures to expand manufacturing, particularly for exports, including the redrafting of the investment code, a task which should be finalized toward October 1983; (e) the limitation of public sector enterprises in manufacturing to present activities; and (f) a strengthening of public sector enterprises management through technology and marketing partnership arrangements, and equity participation by the foreign and domestic private sector in existing public enterprises.

In regard to the bauxite sector, in early 1983, the Government concluded contracts with two U.S. companies to prepare a comprehensive master plan for the industry, to conduct a marketing study, and to provide technical assistance in the bauxite operations. Direct on-site assistance is being provided for one year by four U.S. technicians involved on a full-time basis in the supervision and administration of mining operations. This assistance is likely to increase the industry's chances of benefiting from the expected recovery of international demand. Besides these two studies, the EEC is sponsoring a study on the prospects for Guyanese bauxite products in the European market. The final reports from the two U.S. companies were submitted to the Government at the end of August 1983.

According to the preliminary findings of the foreign consultants, there is considerable scope for reducing cost and increasing productivity. However, the implementation of some of these measures will require the availability of foreign exchange for some urgent imports of equipment and spare parts. At the present level of production, the operating loss of GUYMINE is over G$150 million per annum on sales of G$250 million. However, if US$8 million would become available in 1984 for spare parts and minor capital expenditure, it is estimated that sales over G$300 million could be achieved, reducing the loss to more manageable figures. Guyana has comparative advantages over other world producers of bauxite due to the superior quality of its bauxite and proximity to major markets. However, Guyana has experienced marketing difficulties because, as a result of the nationalization of the industry, it is no longer vertically integrated with the major users of bauxite. In the view of the consultants, Guyana had a chance to recover a substantial share of the bauxite market provided that costs are reduced, efficiency is improved, and marketing efforts are undertaken.

Concerning the rice industry, the authorities stated that many policy changes announced in the Government's Economic Program have been carried out. The functions of the Guyana Rice Board (GRB) regarding the importation and distribution of imports, the provision of credit, the undertaking of extension and research, and the provision of small milling facilities and machinery and equipment have been transferred to commercial importers and distributors, or to other government agencies, national banks or ministries. As a result, the work force of the Rice Board was reduced by 700 persons in 1982.

The mission pointed out that although the function and organization of the GRB had been improved, problems which have a direct bearing on prices and marketing had not been addressed. Thus, Guyana continued to lose a considerable share of its principal export market, CARICOM, where it receives double the world price. In 1982 Guyana exported a little over 34,000 metric tons to CARICOM countries (mainly to Trinidad and Tobago and Barbados) which was only about 45 percent of the 76,000 tons exported to that market in 1980. The reasons behind this loss are an overvalued currency, and, perhaps most important of all, the nonremunerative producer prices paid by the Guyana Rice Board. The Guyana

Rice Board, which handles all legal rice exports, pays to the producers only one half of the export price received from the CARICOM countries. The mission pointed out that this price and marketing arrangement is responsible for the large disappearance of rice from the official market, estimated at more than 40,000 tons of the 179,000 tons of rice produced in 1982. Smuggling of rice out of the country remains, in addition to gold, a major source of black market financing for imports. With this background, the mission found reasonable the advice given by the IBRD and the IDB that the authorities should give the producer access to both domestic and export markets not only to stimulate production but also to minimize illegal exports.

With respect to the sugar industry, which is at present the largest net earner of foreign exchange, the Guyanese representatives ascribed its lack of profitability--operating deficits were about G$80 million in 1981 and 1982 and the deficit is estimated at G$140 million in 1983--to the low international sugar prices, even though only a small portion of sugar exports is sold at the world market price. A strong effort had been made to reduce costs, in particular through the reduction of the nonseasonal labor force, which was now down to 28,000 (from 31,300 in 1981) and was expected to be cut by a further 1,500-2,000 workers in 1983; at the same time, equipment at Guysuco's estates had been upgraded. However, there had been no new investment in the mills for at least ten years, and the scarcity of foreign exchange had also made it difficult to achieve adequate replanting for lack of fertilizer. The authorities estimate that to restore efficiency to the industry, GUYSUCO needs a capital injection of US$25 million for 1983, US$20 million for 1984, and US$22 million in 1985. Another major problem facing GUYSUCO was the difficulty in retaining managerial and technical staff because of low salaries.

Representatives of GUYSUCO stated that, because of the high fixed cost at the present production level, the total cost per pound was about 22 U.S. cents. Still, even at the target output level of 350,000 metric tons (compared with a capacity of 450,000 tons per annum) the unit cost of 17.5 U.S. cents a pound would exceed the average selling price. Barring substantial capital expenditures in the second half of 1983, production in 1984 was unlikely to exceed 270,000 tons and unit cost would rise to 25 U.S. cents a pound.

The mission pointed out that, despite the efforts made to increase production and reduce costs, sugar production had failed to reach the levels achieved in 1976 and 1978, even though Guyana has been exporting more than 90 percent of its production to the European Economic Community, the United States and East European countries at prices well above world market prices. At the same time GUYSUCO's operating deficit had been escalating, and no effort had been made to reduce the subsidy to the domestic consumption of sugar which costs the industry close to G$40 million a year. Further, as advised by the IBRD, the mission said that the Government should consolidate the limited capital equipment of GUYSUCO by closing down or leasing if possible the smaller sugar estates to the private sector. Although all these measures would have the

effect of reducing somewhat the operating deficit of GUYSUCO, they were considered insufficient to eliminate it. The mission pointed out that the only alternative to a drastic reduction in employment was a more realistic exchange rate which, together with the measures mentioned above, could improve the financial position of GUYSUCO.

Another major obstacle to the rehabilitation of the major export industries and the economy in general was the insufficient level of private foreign investment. The Guyana representatives stated that the major deterrants to the promotion of private investment had been the absence of confidence resulting from the rapid nationalization of industries in the early 1970s and the absence of a well defined private investment code. To this end, the Government has engaged a foreign consultant to draft a revised investment code. The authorities hoped that in time the new investment code would help remove the doubts regarding the Government's determination to give assurances to private investors, both nationals and foreigners, concerning the security of their investment.

2. Balance of payments prospects and policies

The authorities said that the acute balance of payment difficulties the country has been facing stemmed mainly from external developments. These included the declines in the prices of sugar, rice, and bauxite, a lagging world economy, which had precipitated an increase in protectionist policies in developed countries with respect to such commodities as sugar, as well as delays in the flow of foreign funds from international institutions.

In the discussion of the outlook for Guyana's balance of payments in 1983, the authorities indicated that they expected official export earnings to decline for the fourth consecutive year to US$221 million, down US$126 million from the 1981 level and US$21 from the very depressed level of 1982.

Imports were projected to decline by about 6 percent in 1983, following a reduction of almost 36 percent in 1982. The projected reduction in imports reflects the serious foreign exchange shortage, which has forced the authorities to restrict imports to the barest minima for consumption in order to keep essential services going and to provide some inputs critical for productive activities. The authorities remarked that as foreign exchange becomes more scarce, barter agreements will become more important with countries also facing exchange problems.

Net payments for services have increased considerably in the last two years, mostly on account of net accrued interest payments abroad. Accrued interest payments which were around US$25 million in 1979 increased to an average of US$50 million a year in 1981 and 1982. For 1983, net interest payments are projected to be US$51 million. As Guyana has been unable to meet its debt service obligations since 1981, a large amount of arrears on these obligations had been accumulated by the end of June 1983. The accumulation of arrears on interest payments is expected to continue during 1983.

The authorities expected the current account of the balance of payments to show a deficit of US$131 million in 1983, compared with US$142 million in 1982 and $187 million in 1981. This apparent improvement is attributable mainly to a reduction in imports because of the shortages of foreign exchange and because foreign financing is no longer available (Table 4).

In regard to the capital account, the authorities were estimating a net outflow of US$6 million. This figure takes into account what had already happened in the first half of 1983, and the net amortization payments on existing foreign loans during the second half of the year.

On the basis of the above estimates for the current and capital accounts, the overall deficit in 1983 is projected to be US$137 million. This deficit will be financed almost entirely by a further accumulation of payments arrears. The accumulation of arrears during the first half of 1983 had already been close to US$100 million, and by June 1983 the foreign exchange holdings of the Bank of Guyana were nil.

Against this background, the mission inquired about measures the authorities would be adopting to deal with the country's balance of payments problems. The mission pointed out that the Government's efforts in the recent past to adapt its policies and programs to changes in the international environment had proven inadequate. The poor management of the key sectors of the economy continued to be reflected in sharp declines in export volumes. Although some progress had been made in correcting certain weaknesses of the export sectors, progress has been very slow and inefficient operations continued to be a major constraint inhibiting the economy's performance.

The mission drew attention to data which indicate a significant real appreciation of the Guyana dollar since the last devaluation in 1981 (Chart 1). This appreciation resulted from the widening inflation differential between Guyana and its main trading partners, and from the appreciation of the U.S. dollar against other major currencies. The mission also noted the existence of repressed domestic inflation which suggests that the inflation differential might well be much higher than that obtained from the official price index. Under these circumstances, foreign exchange commands a substantial premium above the official rate. This has furthered the growth of the illegal market, where the exchange rate is quoted at three times the official rate. The mission questioned the adequacy of the prevailing official exchange rate to deal with the country's balance of payments problems in the light of the increasing role of the parallel market, and the increasing use of external payments arrears as a way of financing the large balance of payments deficit.

The authorities agreed with the mission upon the need for adjusting the exchange rate. However, they were very concerned about the disruptive effects of a major devaluation on real wages, and on the financial position of public enterprises, especially those that are not net foreign exchange earners. They also were concerned about capital losses that

Table 4. Guyana: Balance of Payments

	1981	1982	Proj. 1983 1/
(In millions of U.S. dollars)			
Current account (including transfers)	-187.0	-141.6	-130.6
Merchandise	-93.1	-38.3	-41.2
Exports, f.o.b.	(346.9)	(242.1)	(221.2)
Imports, c.i.f.	(-440.0)	(-280.4)	(-262.4)
Services and transfers	-93.9	-103.3	-89.4
Capital account (net)	106.2	29.2	-6.5 2/
Public sector	111.3	30.5	-6.5
Private sector	-5.1	-1.3	--
Errors and ommissions	43.1	-18.3	--
Special transactions 3/	4.2	--	--
Overall balance	-33.5	-130.7	-137.1
Change in net international reserves (increase -) 4/	-2.8	5.1	...
Change in arrears (increase +)	36.3	125.6	...
(In percent of GDP)			
Current account deficit	-32.9	-29.3	-28.3
Overall balance	-5.9	-27.0	-29.7

Sources: Statistical Bureau of Guyana; Bank of Guyana; and Fund staff estimates.

1/ Based on the estimates for the first half of 1983.
2/ Includes scheduled disbursements, scheduled amortization, and debt refinancing and deferment.
3/ Includes exchange profits and losses from exchange rate variations and proceeds from SDR allocations.
4/ Does not include external payments arrears.

certain corporations, which had accumulated arrears on their foreign obligations, might experience in the wake of a major devaluation of the Guyana currency. They noted that the economy was already operating near the floor of imported inputs required for production activities and that provision of adequate foreign exchange resources up front would be required to preserve and reinforce the productive capacity of both the public and private sectors. The mission observed that such a strategy would require a large resource transfer from the rest of the world to finance the gap that exists at present between supply and demand. In the present international financial setting this is most unlikely, especially in view of the existence of large foreign payments arrears.

During 1981 and 1982 there was an intensification of restrictive practices in Guyana's exchange and trade system. The list of commodities for which import licenses are guaranteed was reduced significantly and now includes mainly selected capital goods, spare parts, raw materials, and drugs. Currently, applications for import licenses are generally not approved for consumer goods nor for commodities for which substitutes exist locally. Guyana's exchange system involves the following restrictions on payments and transfers for current international transactions subject to the Fund's approval under Article VIII, Sections 2(a) and 3: (i) continuing accumulation of external payments arrears; (ii) a multiple currency practice arrising from the introduction of an unofficial exchange rate to official purchases of gold from individual producers; (iii) an annual limit of G$200 per person on exchange allocation for tourist travel; and (iv) a prohibition, since January 28, 1982, on cash gift allowances abroad.

3. Domestic financial policies

In spite of the serious economic imbalances afflicting the Guyanese economy, the authorities had strong misgivings about an adjustment policy that curbed domestic expenditure, fearing that it would increase the underutilization of productive capacity.

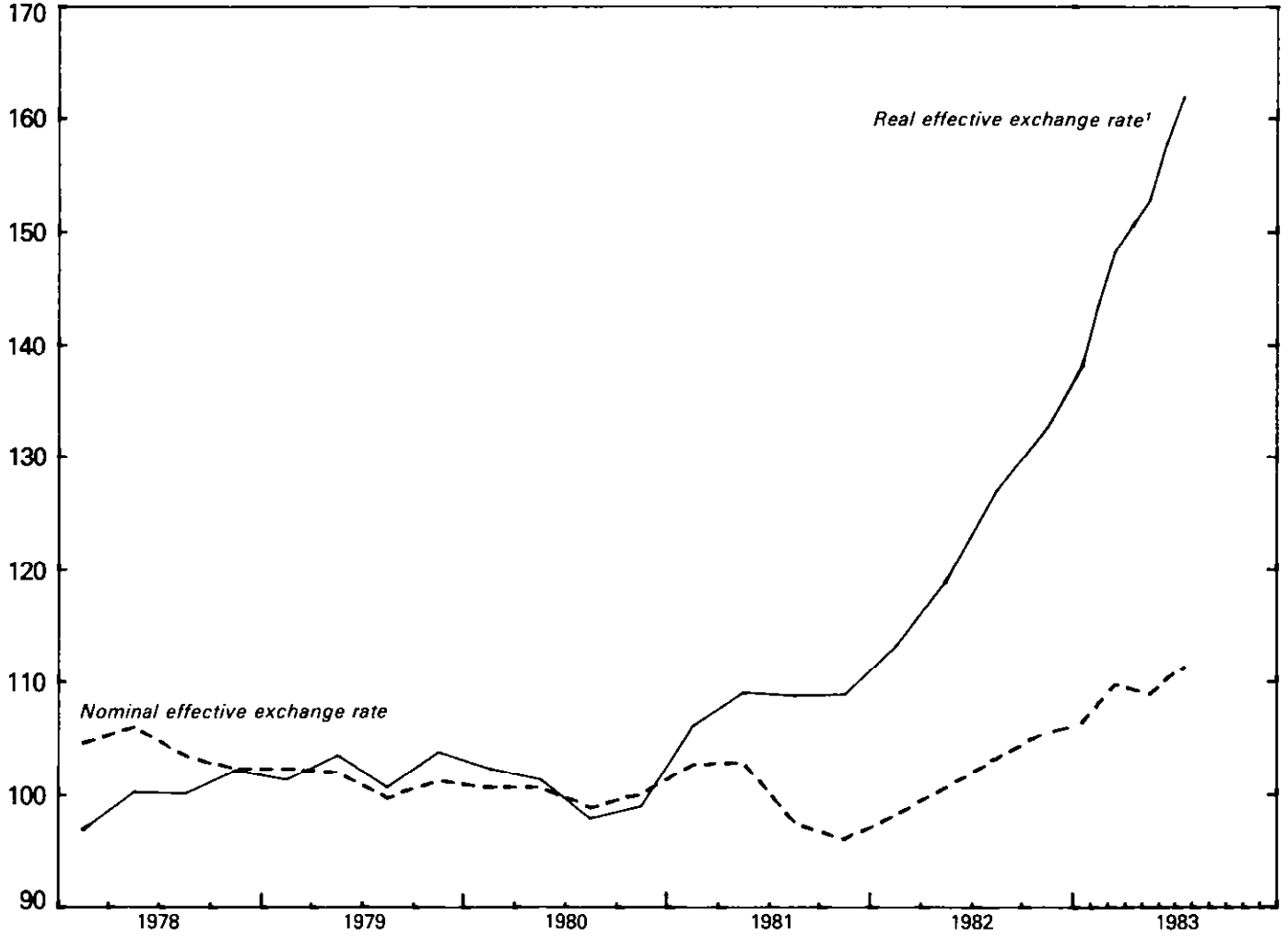
Nonetheless, the authorities noted, adverse exogenous developments had prompted the adoption of important domestic adjustment measures in 1982. Expenditures had been restricted by a 17 percent reduction in the number of Civil Service employees, the freezing of nominal wages and stricter expenditure controls for government services. As a result, central government wage outlays declined by 6 percent, expenditures on government services and other noninterest current payments contracted by 27 percent, and total central government outlays were held virtually to the 1981 level.1/ At the same time, however, central government revenue declined by 2 percent (because of the decline in economic activity and unfavorable external developments) and offset the expenditure cuts. For the public sector as a whole the deficit in 1982 reached about 47 percent of GDP, as the public corporations registered for the second consecutive year levels of dissaving equivalent to almost 5 percent of GDP (Table 5).

1/ Not taking into account the refunding operation for the rest of the public sector.

GUYANA

INFORMATION NOTICE SYSTEM INDEX OF REAL EFFECTIVE EXCHANGE RATE

(1980 = 100)



[1]Trade weighted index of nominal exchange rates deflated by seasonally adjusted consumer prices; increases mean appreciation.

Table 5. Guyana: Consolidated Public Sector Operations

	1979	1980	1981	Prel. 1982	Proj. 1983
	(In millions of Guyana dollars)				
Revenues	412.2	455.1	578.9	550.6	568.8
Central government current	394.9	451.3	558.2	547.3	558.5
Central government capital	17.3	3.8	20.7	3.3	10.3
Expenditures	-791.4	-975.6	-1,243.0	-1,163.4	-1,201.0
Central government expenditures	-677.4	-852.1	-1,125.8	-1,075.8	-1,115.6
Current	(-497.3)	(-597.6)	(-774.3)	(-754.5)	(-857.6)
Capital (net of transfers)	(-180.0)	(-254.5)	(-351.5)	(-321.3)	(-258.0)
Public corporations' capital expenditures	-114.0	-123.5	-117.2	-87.6	-85.4
Public corporations' current balance	156.7	192.7	-46.2	-66.9	-168.3
Overall public sector deficit	-222.5	-327.8	-710.3	-679.7	-800.5
Financing					
Net external financing	80.6	130.0	340.2	143.9	
Domestic banking system	197.0	346.0	271.8	609.5	
Other	-55.1	-148.2	-98.3	-73.7	
Memorandum item					
Central Government current balance	-102.4	-146.3	-216.1	-207.2	-299.1
	(In per cent of GDP)				
Central government revenues	31.1	30.2	36.2	37.9	41.1
Central government expenditures	59.7	64.7	77.8	80.1	80.5
Overall public sector deficit	-16.7	-21.7	-44.5	-46.8	-57.8

Sources: Ministry of Finance, and Bank of Guyana

In 1983, the situation has become critical, the authorities said, because of the effects that the acute shortage of foreign exchange was having on the resources accruing to the public sector, as the transfer of activities to the illegal markets increases. It was estimated that the Central Government alone was likely to have a current account deficit of G$300 million, equivalent to almost 22 percent of GDP. Current expenditure is expected to increase by 13 percent, mainly on account of a larger increase in interest payments, and the increase in current revenue is expected to be only of the order of 2 percent, as certain excise and consumption taxes were increased. Outlays for capital formation are expected to decline sharply as a result of the unavailability of foreign financing, and will be limited to those projects already under execution and for which foreign financing had actually been committed. Total central government outlays are projected to increase by less than 4 percent, but the overall deficit of the Central Government would still reach almost G$600 million, equivalent to 43 percent of GDP.

Concerning the operations of the public corporations, the authorities said that their overall performance is expected to deteriorate considerably in 1983, with many of them approaching the point of total paralysis because of the lack of raw materials and spare parts. Production and export earnings of GUYMINE (bauxite) and GUYSUCO (sugar) would decline sharply, with their combined operating losses expected to reach G$300 million or 75 percent higher than in 1982. For the public corporations as a whole, a record high current account deficit equivalent to 12 percent of GDP is projected. Investment expenditure would be held to a minimum.

The latest projection indicated that the consolidated public sector deficit will show negative savings equivalent to almost 33 percent of GDP in 1983, 14 percentage points higher than in 1982. Even with reduced capital outlays, the overall deficit is projected to reach almost 58 percent of GDP. The bulk of this deficit will be financed by credit from the banking system, and thus the net domestic assets of the banking system are projected to show another large increase in 1983, which would be well in excess of the growth in liabilities to the private sector. Although interest rates were raised substantially in recent years (most recently in June 1982), they are far below the domestic inflation rate. The authorities have been reluctant to raise interest rates further, but in May 1983 a tax-free savings scheme was introduced in an effort to promote personal savings.

The mission pointed out that the fiscal problem will become even worse if the authorities fail to take stronger measures to bring the operations of the public sector under control. In its view, the fiscal imbalance had become so large that, even under the most favorable assumptions (elimination of subsidies, successful implementation of supply-side measures, and an upturn in world economic activity), a massive reduction in the level of public expenditure would be needed to bring the deficit down to manageable proportions.

The mission noted that a devaluation of the currency, in combination with fiscal and wage restraint, would lessen the required domestic expenditure cut. Because the major public sector enterprises produced mainly for the export market, a devaluation would improve the fiscal outcome, assuming that its effects would be passed on to consumers and would not be offset by wage increases. The effect of a devaluation would be to substitute foreign demand for the required reduction in domestic absorption. This would reduce the cost of adjustment in terms of unemployment, compared with reliance solely on contractionary demand management policies.

IV. Staff Appraisal

Over the past several years, aggregate demand has exceeded output by margins that have been shown to be unsustainable. In 1982 the overall deficit of the public sector reached 46 percent of GDP and for 1983 the deficit is expected to be 57 percent of GDP. Monetary policy has been oriented to accommodate the financing of the public sector deficit which, in turn, has resulted in a total exhaustion of the Central Bank's gross international reserves and a large accumulation of foreign payments arrears. At the same time, declines in output have been registered in all sectors of the economy, but particularly in the main export sectors--rice, sugar, and bauxite. In 1982 the output of rice and sugar was below the levels achieved in 1977-78 and the output of bauxite was about 60 percent of its 1978 level. Real GDP contracted by 9 percent in the period 1978-81, declined by more than 10 percent in 1982 and is expected to decline by a further 8 percent in 1983. Although export earnings from the major sectors have been hard hit by the world recession, the main factor behind the disarray of the economy has been the cumulative effects of government policies that have brought about distortions in the price and productive structures of the economy, damaged production and investment incentives, and precipitated the flight of financial and human capital. The result has been a major balance of payments crisis with widespread shortages of industrial inputs, consumer goods, and essential foodstuffs.

Based on developments in the first half of 1983, it is expected that for 1983 as a whole Guyana will incur an external current account deficit of some 28 percent of GDP, despite a reduction in imports. As Guyana has been unable to borrow abroad, the overall balance of payments deficit is projected to be the equivalent of 30 percent of GDP, financed for the most part through a further increase in arrears. The accumulation of external payments arrears reached US$307 million at the end of June 1983, equivalent to about 66 percent of projected 1983 GDP.

It is the view of the staff that the measures taken by the authorities in 1982 and in the first half of 1983 fall far short of what is needed to deal with the country's economic difficulties. As regards the supply side, the reorganizational measures recently implemented in the public corporations and the structural changes now being proposed

do not go far enough. They need to be reinforced by the rationalization of the price system and the elimination of subsidies to the consumer, which would reduce scarcities and contribute to strengthening the financial position of the public sector corporations. To minimize the inflation and unemployment effects of the required corrective measures, it is necessary to restrain wage increases. The decline in the country's foreign earnings that has taken place since 1979 represents a reduction in real income that will have to be borne. Strict implementation of a restrained incomes policy, complemented by improvement on the supply side of the economic process and by supporting fiscal and credit policies, would reduce sharply the diversion of activities to the black market and would improve the chances that the adjustment effort will be successful.

Concerning the domestic financial policies that are being pursued by the authorities, the reliance on deficit financing of the public sector is too great, the cuts in spending are too limited, and the revenue measures are unduly modest. Moreover, the currency is substantially overvalued and is a major cause of the disequilibrium in the public sector. A devaluation would improve the fiscal outcome, assuming that its price effects will be passed on to consumers and that wage increases will be limited. Also, an adjustment of the exchange rate would facilitate relative price changes conducive to the restoration of a sustainable balance of payments position, lessening the reliance on direct import controls, and thus contributing to the recovery of economic activity.

Implementation of a restrained fiscal policy would help the Bank of Guyana to achieve adequate control over domestic credit. From the present starting point, the Bank of Guyana does not have any room to absorb losses in international reserves. To assist in the efficient management of credit policy and to discourage capital outflows, a flexible approach to interest rates should be employed, within the framework of a prudent credit policy of the Central Bank.

Guyana's very difficult external debt problems will be resolved only through the adoption of a general stabilization program. What is needed is to reverse the trend of public finances and at the same time to assure that the conditions for the resumption of economic growth are created. Within the framework of better domestic policies, Guyana could be in a better position to negotiate the refinancing of its external debt.

In sum, the authorities are faced with the painful alternatives of whether to let the economy continue to follow the present path with the consequent deepening of the existing crisis, or to adjust in a way that bears the promise of breaking out of the present distressing situation.

Guyana maintains restrictions on payments and transfers for current international transactions, arising from restrictions on the provision of foreign exchange for tourist travel and cash transfer abroad,

from the existence of external payments arrears; and from the introduction of a multiple currency practice. Furthermore, Guyana's external payments arrears have increased since the last Article IV consultation. The staff encourages the authorities to adopt policies that would facilitate the elimination of these restrictions as soon as possible. In the meantime, the staff does not recommend that the Executive Board approve the restrictions.

Fund Relations with Guyana

Status:	Article VIII.			
Quota:	SDR 37.5 million. Guyana has not yet consented to the increase in its proposed maximum quota to SDR 49.2 million under the Eighth General Review.			
Fund holdings of Guyana dollars:	As of August 31, 1983		Millions of SDRs	Percent of Quota
	Total		112.34	299.57
	Of which:	EFF	(29.28)	(78.08)
		CFF	(15.77)	(42.06)
		SFF	(29.78)	(79.42)
Overdue payments to the Fund (as of September 21, 1983)	Total		8.02	21.39
	Of which:	CFF repurchases	(4.66)	(12.43)
		EFF repurchases	(1.08)	(2.88)
		Semiannual charges	(1.52)	(4.05)
		Quarterly charges	(0.76)	(2.03)
SDR Department:	Cumulative allocation		14.53	...
	Holdings		--	--
Exchange rate:	Pegged to the U.S. dollar since 6/2/81 at G$3.00 per U.S. dollar.			
Gold distribution:	Gold acquired: 17,117 fine ounces.			
Distribution of profits on gold sales:	US$3.2 million.			
Last Article IV consultation	Discussions were held during July 20-August 19, 1982; consultation completed by the Board on November 5, 1982 (EBM/82/142).			

Guyana-Basic Data

Area and population	
Area	83,000 sq. miles (215,000 sq. kilometers)
Population (end-1982)	765,000
Annual rate of population increase (1977-82)	-0.5 percent
GNP (1982)	SDR 391 million
	US$432 million
	G$1,296 million
GNP per capita (1982)	SDR 511

Origin of GDP	1980	1981	Prel. 1982	Proj. 1983
		(percent)		
Agriculture	21.6	22.1	24.4	25.9
Mining	14.1	12.5	9.6	6.3
Manufacturing	13.3	14.1	13.8	13.3
Construction	7.1	7.2	7.2	7.5
Government	20.7	20.9	21.6	23.0
Other services	23.2	23.2	23.4	24.0
Ratios to GDP				
Exports of goods and nonfactor services	69.7	65.5	54.8	54.4
Imports of goods and nonfactor services	-86.6	-98.5	-82.3	-70.5
Current account of the balance of payments	-17.9	-32.9	-29.3	-28.3
Central government revenues	30.2	36.2	37.9	41.1
Central government expenditures	60.9	73.2	107.0 1/	84.4
Public sector savings	3.1	-16.4	-18.9	-33.7
Public sector overall surplus or deficit (-)	-21.7	-44.5	-46.8	-57.8
External public debt (end of year)	93.7	121.6	136.5	141.7
Gross national savings	13.5	1.9	-0.8	-2.5
Gross domestic investment	31.5	34.8	28.4	25.1
Money and quasi-money (end of year) 2/	50.0	55.6	76.0	104.7
Annual changes in selected economic indicators				
Real GDP per capita (at factor cost)	1.1	-0.4	-6.8	-6.7
Real GDP at factor cost	1.6	-0.3	-10.4	-8.4
GDP at current prices (market prices)	13.7	5.9	-9.1	-4.6
Domestic expenditure (at current prices)	14.9	14.3	-11.7	0.5
Investment	(12.3)	(16.8)	(-25.6)	(-15.7)
Consumption	(16.0)	(13.3)	(-6.1)	(5.7)
GDP deflator	11.5	1.3	3.4	-4.3
Consumer prices (annual averages) 3/	14.1	22.2	21.0	...
Central government current revenues	14.3	23.7	-2.0	2.1
Central government current expenditures	20.2	29.6	-2.6	13.7
Money and quasi-money 2/	15.6	17.8	24.3	27.7
Money	(12.9)	(11.1)	(20.3)	(21.0)
Quasi-money	(17.2)	(21.8)	(26.4)	(31.3)
Net domestic bank assets 4/	23.2	6.3	13.6	2.0
Credit to public sector (net)	(27.2)	(5.9)	(19.2)	(4.2)
Credit to private sector	(15.8)	(7.8)	(-35.1)	(-30.6)
Merchandise exports (f.o.b., in U.S. dollars)	33.7	-10.9	-30.2	-8.6
Merchandise imports (c.i.f., in U.S. dollars)	24.7	11.1	-36.3	-6.4

	1980	1981	Prel. 1982	Proj. 1983
Central government finances	(millions of Guyana dollars)			
Revenues	451.3	558.2	547.3	558.5
Expenditures	597.6	774.3	1754.5	857.6
Current account surplus or deficit (-)	-146.3	-216.1	-207.2	-299.1
Overall surplus or deficit (-)	-458.0	-590.3	-1,002.7	1/-600.4
External financing (net)	93.4	388.7	127.9	...
Internal financing (net)	364.6	201.6	874.8	...
Balance of payments	(millions of U.S. dollars)			
Merchandise exports, f.o.b.	389.2	346.9	242.1	221.2
Merchandise imports, c.i.f.	-396.1	-440.0	-280.4	-262.4
Investment income (net)	-35.8	-53.6	-47.5	-45.0
Other services and transfers (net)	-63.4	-40.3	-55.8	-44.4
Balance on current and transfer accounts	-106.1	-187.0	-141.6	-130.6
Public sector capital (net)	51.0	111.3	30.5	-6.5
Private capital and errors and omissions 5/ (net)	-42.9	42.2	-19.6	--
Arrears	17.0	36.3	125.6	137.1
Change in net reserves of banking system and public sector (increase -)	81.0	-2.8	5.1	--

International reserve position 6/ (end of year)	Dec. 31 1981	June 30 1982	Dec. 31 1982	June 30 1983
		(millions of SDRs)		
Central bank (net)	198.2	283.5	-322.8	-437.5
Central bank (gross)	5.9	3.3	9.6	1.4
Rest of banking system (net)	-8.9	-20.9	-13.8	-13.6

1/ Reflects a G$460 million equity contribution from the Central Government to some corporations to repay their bank overdrafts.

2/ Monetary system.

3/ Official CPI.

4/ In relation to the stock of money and quasi-money at the beginning of the period. Excludes contra-entry of SDR allocations.

5/ Includes exchange profits and losses and profits from sale of gold by IMF.

6/ At exchange rates prevailing at the end of the period. Includes liabilities on account of external arrears.

Financial Relations of the World Bank Group with Guyana

IBRD/IDA lending operations as of June 30, 1983:	Disbursed		Undisbursed	
	IBRD	IDA	IBRD	IDA
	(In millions of U.S. dollars)			
Education	6.35	7.03	3.55	--
Agriculture and forestry	20.57	2.53	2.33	9.66
Transportation	--	4.40	--	--
Program and structural adjustment loans	19.35	5.00	0.57	--
Sea defense	10.09	--	--	--
Energy	9.48	--	4.52	--
Other	0.52	--	0.98	--
Total	66.36	18.96	11.95	9.66

Principal repayments:	US$6.18 million.
Debt outstanding, including undisbursed:	US$96.80 million.
Commitments, July 1982-June 1983:	Nil.
Disbursements, July 1982-June 1983:	US$14.2 million.
IFC investments:	US$2.0 million.
Structural adjustment loan:	A structural adjustment loan of approximately US$22 million was approved by the Bank's Board in February 1981. The second and final tranche of the loan was released, following some delay, in July 1982.
Technical assistance:	The IBRD has provided technical assistance to Guyana through its project lending operations. In addition, a US$8 million loan for technical assistance in the power sector and a second technical assistance loan for US$1.5 million, approved in conjunction with the structural adjustment loan, are under execution.

Recent economic and sector missions:	Structural adjustment loan and investment review supervision missions (July and November 1982) and economic missions in February and July-August 1982. (Report--"Guyana: Recent Developments and Short-Term Prospects" green cover draft.) These missions were conducted parallel to IMF missions and a number of joint meetings were held with the authorities. A special consultation mission in August 1982. A number of missions in connection with the supervision of ongoing lending operations have taken place during the past year.
Aid Consultative Group:	The fifth meeting of the Caribbean Group for Cooperation in Economic Development was held under the chairmanship of the IBRD in June 1982 in Washington, D.C. The sixth meeting will take place in December 1983.