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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 83/9

3:00 p.m., January 10, 1983

W. B. Dale, Acting Chairman

Executive Directors	Alternate Executive Directors
	w. B. Tshishimbi
	C. Taylor
	G. Ercel, Temporary
	A. Le Lorier
A. Donoso	M. Teijeiro
	C. Dallara
	M. A. Janjua, Temporary
	Jaafar A.
	T. Yamashita
R. K. Joyce	
	J. R. N. Almeida, Temporary
G. Laske	
G. Lovato	
R. N. Malhotra	
	S. El-Khouri, Temporary
J. J. Polak	T. de Vries
	K. G. Morrell
	O. Kabbaj
	E. I. M. Mtei
	J. L. Feito
	I. Fridriksson, Temporary
Zhang Z.	Wang E.

L. Van Houtven, Secretary
J. A. Kay, Assistant

Also Present

African Department: J. B. Zulu, Director; R. J. Bhatia, Deputy Director; O. B. Makalou, Deputy Director; T. T. Gibson, J. Hicklin, P. D. Mortimer-Lee. Exchange and Trade Relations Department: M. Guitian, S. Kanesa-Thasan, A. Pera. External Relations Department: G. P. Newman, H. P. Puentes. IMF Institute: L. A. Benavides, F. R. Ramirez, Participants. Legal Department: H. Elizalde, S. A. Silard. Research Department: G. I. Brown, N. M. Kaibni, G. Khatchadourian, P. J. Montiel, T. K. Morrison, A. Salehizadeh. Secretary's Department: J. C. Corr. Western Hemisphere Department: S. T. Beza, Deputy Director; J. O. Bonvicini, J. M. F. Braz, P. D. Brenner, M. Caiola, D. S. Hoelscher, J. S. Lizondo, C. L. Ramirez-Rojas, F. Rubli-Kaiser, J. F. van Houten. Advisor to the Managing Director: E. W. Robichek. Advisors to Executive Directors: S. R. Abiad, J. Delgadillo, P. Kohnert, H.-S. Lee, P.-C. Maganga-Moussavou, P. D. Péroz. Assistants to Executive Directors: H. Alaoui-Abdallaoui, H. Arias, T. A. Connors, C. Flamant, G. Gomel, A. Halevi, M. Hull, J. A. K. Munthali, V. K. S. Nair, Y. Okubo, G. W. K. Pickering, C. A. Salinas, D. I. S. Shaw, H. Suzuki, J. C. Williams.

1. BOLIVIA - 1982 ARTICLE IV CONSULTATION; AND PURCHASE TRANSACTION - COMPENSATORY FINANCING FACILITY

The Executive Directors considered the staff report for the 1982 Article IV consultation with Bolivia (SM/82/137, 7/12/82; and Sup. 1, 1/4/83), together with a request by Bolivia for a purchase equivalent to SDR 17.9 million under the compensatory financing facility (EBS/82/233, 12/16/82; and Sup. 1, 1/7/83). They also had before them a report on recent economic developments in Bolivia (SM/82/162, 8/9/82).

The staff representative from the Research Department provided recent information on Bolivia's exports. As the calculations for a drawing under the compensatory financing facility had been based partly on estimated data for 1982, the shortfall year, Bolivia ran the risk of overcompensation. As explained in the footnote on page 4 of EBS/82/233, export earnings for October-December 1982 had been estimated at a monthly rate of SDR 71 million compared with SDR 62.1 million in the first nine months of the shortfall year and SDR 74.5 million in the fourth quarter of 1981. Figures for exports in October 1982, which had just become available, showed that the export value in that month had been no more than SDR 56 million. To reach the level estimated for the quarter October-December 1982, therefore, exports in November and December 1982 would have to amount to the average of SDR 89 million a month, which the staff considered to be unreasonably high. Consequently, the staff expected that when data for the whole shortfall year became available, the shortfall would be larger than the SDR 17.9 million now estimated by the staff.

Mr. Donoso made the following statement:

> I would like to thank the staff for its papers on the Article IV consultation and on the proposed purchase under the compensatory financing facility.
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> As described in the staff's paper, during 1982 Bolivia faced a deep economic crisis characterized by falling production and employment, a high rate of inflation, and severe difficulties in the external sector.
>
> In this situation a new government took office in October 1982. The new civilian authorities applied a series of measures on November 6 aimed at correcting the economic imbalances. The measures included:
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> 1. The abolition of the two-tier exchange rate system in favor of a unified exchange rate of 200 pesos per U.S. dollar. (The previous rates were 44 pesos per U.S. dollar for servicing of the external debt and some essential imports and a floating rate for other transactions).
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> 2. Prices of gasoline, diesel oil, fuel oil, kerosene, and jet fuel oil were increased up to 400 per cent.

3. Electricity costs were increased by an average of 150 per cent, according to a progressive scale.

4. The price of bread was increased 150 per cent, rice 45 per cent, and sugar and milk 40 per cent.

5. Transportation rates were increased as follows: air 65 per cent, railway 130 per cent, waterways 120 per cent, land transportation (interdepartmental) 145-155 per cent, urban (taxis) 150 per cent, and urban (mass transit) between 50 and 80 per cent.

6. Reforms of customs duties and prohibition of nonessential imports were introduced on a temporary basis.

7. The presumed costs of the mining sector were reduced to allow higher effective tax yields. Also, temporary taxes were either introduced or increased on nontraditional export goods, on bank credit, and on net fixed assets of economic units. The penalty rate for tax payments in arrears was increased to no less than the commercial bank lending rate.

8. Limited wage increases were granted to compensate for the price impact of the above measures, particularly for the lower-income groups.

As pointed out by the staff, these measures will produce a substantial reduction in the public sector deficit for 1983.

The Bolivian authorities have indicated that these measures were of an emergency nature, defined to face most immediate problems and that they would be complemented with others in the context of a more comprehensive plan within 100 days.

The authorities have already expressed their willingness to closely cooperate with the Fund in finding solutions to the present economic and financial difficulties of the country, probably with an extended arrangement early this year.

Present exchange restrictions ought to be regarded as temporary and arising from the deep and rapid deterioration of the external sector. Large international reserve losses and failure to receive timely proceeds from some exports produced a dramatic scarcity of foreign exchange needed to pay for imports of basic consumption goods. Despite the willingness and the efforts made to comply with normal servicing of the external debt, arrears could not be avoided. At the end of September this year, negative net reserves of the Central Bank reached $365 million. Thus, the introduction of restrictions must be considered as emergency measures.

> A new round of negotiations with commercial banks and other creditors is in progress or has been agreed upon, the intention being the prompt elimination of arrears and the finding of appropriate arrangements for the servicing of the external debt.

Mr. Almeida stated that he strongly supported the request by the Bolivian authorities for a drawing under the compensatory financing facility. The staff had been rather cautious in its estimates. The excess of export earnings for natural gas might be exaggerated because no growth in volume had been projected for the next two years, even though the average compound growth rate for the past three years had been 28 per cent a year. However, he understood that large natural gas discoveries had recently been made in Argentina, Bolivia's most important export market. He could agree with most of the staff analysis regarding the country's economic situation, which was rather unusual for a less developed country, in that there had been a consistent improvement in the terms of trade during the past year. The deterioration in the balance of payments had been due to a fall in export volume, and to erratic capital movements.

As usual, Mr. Almeida went on, he had been impressed by the high caliber of Bolivia's financial statistics. Few countries were able to produce a table showing flow of funds as accurately as Bolivia. He had four questions to put to the staff. First, on page 15 of SM/82/137, Supplement 1, it was said that according to official estimates real GDP had declined by 8 per cent in 1982, but that the drop might have been even more pronounced. Perhaps the staff could say something about the deficiencies in the official estimates. Second, he had been surprised by the affirmation on page 14 of SM/82/137 that a fixed exchange rate was the most appropriate regime for Bolivia in a long-run context, given the country's attitude toward inflation. Attitudes were important, but facts of life were still more so, and Bolivia had endured inflation of 25 per cent in both 1980 and 1981, while at present the figure was over 200 per cent. He did not consider those numbers compatible with a fixed exchange rate, and he would be grateful if the staff would elaborate.

Third, Mr. Almeida remarked, he was confused by the comments on wage policy in SM/82/137 and SM/82/162. In SM/82/137 the staff had said that wage policy was one of the weakest links in Bolivia's economic policies. In SM/82/162 the staff had said that wage data were scanty and did not permit a definite conclusion on the evolution of labor income. Some clarification would be appreciated. Fourth, he found no information in SM/82/137, Supplement 1 regarding a forthcoming report on the volume of natural gas reserves, which had been expected in the second half of 1982. He wondered whether there was any further information on the gas question.

He had been greatly encouraged by the recent measures taken by the Bolivian authorities, Mr. Almeida stated. The depreciation of the peso and other steps showed how strongly the authorities felt the need to put their house in order. The staff seemed to be divided on those measures.

In EBS/82/233 the staff had said that the measures formed a firm basis for a future adjustment program under an extended arrangement; but in SM/82/137, Supplement 1 the staff had said that the new measures were only a *significant first step*. The Fund should proceed with an extended arrangement as rapidly as possible, in order to enhance and support the good intentions of the authorities.

Mr. Feito noted that the requested purchase would bring Bolivia's outstanding purchases under the compensatory financing facility to 32.1 per cent of quota, so that it was still under 50 per cent. He strongly supported the request, which clearly met all the criteria. He was in broad agreement with the staff assessment of the Bolivian economy. The country was facing a serious economic and financial situation, and it was evident that the authorities were trying to tackle the situation. The overall balance of payments had been in deficit for the past five years, although there had recently been some improvement with the deficit falling from SDR 400 million in 1981 to less than SDR 300 million in 1982. Unfortunately the changes were due largely to a fall in imports as a consequence of the serious shortage of foreign exchange. The data for 1982 showed that the deficit would still be very large, and that the country's balance of payments needs were therefore great.

The Bolivian authorities, Mr. Feito continued, had made several attempts to redress the country's economic disequilibrium. All their efforts had been insufficient and in most cases extemporaneous. Even though close contact had been made with the Fund, political developments had largely frustrated the adjustment efforts. The present Government had set as one of its key objectives the implementation of an emergency economic recovery program. The authorities had adopted a series of major measures, including the reunification of exchange markets, moderation in wage increases, and several other steps intended to reduce the fiscal deficit. Nevertheless, the situation was so serious it would take several years before Bolivia's balance of payments would become sustainable. Meanwhile, the efforts by the present Government represented important steps in the right direction that deserved the Fund's support. In addition, they represented closer cooperation with the Fund, especially in view of the authorities' intention to request an extended arrangement. He would be interested to know the status of that request.

As to cooperation with the Fund in general terms, Mr. Feito commented that the request for the compensatory purchase was under 50 per cent of quota and that, nevertheless, the staff had commented on Bolivia's exchange restrictions and multiple currency practices. The staff seemed to be implying that the elimination of such restrictions could be considered a necessary demonstration of the authorities' cooperation, and that the extent of cooperation was only acceptable because the matter would be dealt with in the near future in connection with discussions for the use of some of the Fund's other resources. It would not be appropriate for the Fund to give the impression that it was establishing additional conditionality for drawings in the first 50 per cent of quota under the compensatory financing facility. He would be interested to hear the staff's comments on the point. In particular, it would be important to know whether a member could be compelled to eliminate certain restrictions in order to obtain approval of a purchase in the first 50 per cent of quota under the compensatory financing decision.

Mr. Dallara stated that his authorities were in broad agreement with the staff appraisal, and that he supported the request for a drawing under the compensatory financing facility. It was clear that the economic position in Bolivia had become serious by early 1982. He agreed with the staff that the emergency economic measures announced by the Government in November 1982 could be regarded as a significant first step toward the revitalization of the Bolivian economy. It was essential that the authorities should vigorously pursue their policies in the coming months if they were to have any chance of success.

Past experience with a number of attempts to stabilize the Bolivian economy had been less than encouraging; what was needed was a persistent and comprehensive adjustment effort, Mr. Dallara commented. The budget deficit had reached alarming proportions during the first nine months of 1982, and it was imperative that expenditures on wages and salaries should be brought under control without delay. In those circumstances, the projected wage increases of up to 30 per cent, embodied in the emergency program, seemed to be rather high. On the revenue side, greater efforts would have to be made to improve both the structure and the operation of the tax system, and the problem of tax evasion would have to be dealt with. The use of extrabudgetary funds was also disturbing.

He had noted with dismay the extremely rapid increase in labor costs in the parastatal industries, in particular the petroleum corporation, during the first nine months of 1982, Mr. Dallara remarked. He would be interested to know why the increases in labor in the parastatals were greater than those in the other major sectors for which data were provided. The authorities were clearly willing to tackle the budget problem, as could be seen from the steps described both by the staff and by Mr. Donoso. The emergency program contained actions that would substantially reduce the public sector deficit in 1983, and he would be interested to have more details regarding the degree of improvement that might be envisaged during the year. It was particularly interesting to recall that the staff had said in July 1982 that the Central Bank could finance a deficit of no more than 2.5-3 per cent of GDP, given the financial resources at the disposal of the country.

Monetary policy had clearly been too accommodating in 1982, Mr. Dallara considered. Distortions in the pricing mechanism had had an adverse effect on the economy; they seemed to have been a major factor in the country's fiscal and balance of payments problems. He therefore welcomed both the authorities' earlier acknowledgments that the previous price controls and subsidies had in fact led to a misallocation of resources and created disincentives, and the steps that had been taken or were planned to reduce the level of subsidies; he encouraged the authorities to continue taking strong action in that field.

In the external sector, the recent reunification of exchange markets was a helpful step, Mr. Dallara observed. He would, however, welcome comments on the reasons for having chosen a rate of $b 200 = US$1. He wondered whether, even though the parallel market had been officially abolished, it did not still exist, and if so, at what rate?

All the criteria for a drawing under the compensatory financing facility had been met, Mr. Dallara noted; he could therefore support the proposed drawing. In reaching that conclusion, he placed special emphasis on the recent measures taken by the authorities, as evidence of their determination to cooperate with the Fund in an effort to deal with the country's balance of payments problems. The authorities had indicated their desire to pursue, with the Fund, the possibility of undertaking an extended arrangement, which would support an even broader adjustment effort. He agreed that a broader adjustment effort was required but, in view of the past experience of relations between Bolivia and the Fund, he was not entirely certain that an extended arrangement would be the most appropriate form of support for the authorities' present effort.

Mr. Taylor remarked that it was a pity that the Executive Board had had to wait so long since the previous Article IV consultation with Bolivia in 1979. The difficulties facing many Latin American economies at present made it important for the Fund to maintain regular Article IV consultations with its members in that area. It was particularly important that the Executive Board should be involved, through an Article IV consultation, if negotiations with a country regarding a Fund program should be frustrated or if a member was contemplating enlarged or extended access to Fund resources. He noted that the possibility of an extended arrangement had been mentioned by the staff in all three of its papers, and also by Mr. Donoso. Like Mr. Dallara, he doubted rather strongly whether the nature of the problems facing Bolivia made an extended arrangement the best approach. The policies hitherto adopted or planned were clearly not in themselves a sufficient basis for an extended arrangement with the Fund.

Bolivia's foremost need was for a period of stabilization involving strong corrective measures, Mr. Taylor observed. Many Executive Directors would surely have serious doubts about initiating a medium-term program with a country where inflation had risen from an annual rate of about 25 per cent in 1980-81 to over 200 per cent in October 1982. Even if the baskets used for price indices were out of date, as maintained by the staff, there might have been an enormous surge of inflation during the year. Moreover, the weakness of the statistical base made it doubtful whether there was sufficient economic information on which to establish the policies needed for an extended arrangement. The decision establishing extended arrangements called for the adoption of structural adjustment measures as part of a concerted medium-term approach, implying a high level of commitment and administrative expertise on the part of the authorities. He was not implying that an extended arrangement could not be considered at some stage; however, there were major uncertainties at present that would best be addressed through the medium of an initial one-year stand-by arrangement, which could accommodate any structural adjustment that might prove necessary during the period. When the regional situation became calmer, he might look toward a longer program with more equanimity.

Bolivia's difficulties seemed in some respects to have been caused to some extent by developments in some neighboring countries, Mr. Taylor observed. Bolivia was, for instance, self-sufficient in oil, and the terms of trade had improved significantly since the mid-1970s. The openness of the economy had meant that devaluation could rapidly lead to wage pressures and that excess domestic demand pressures had usually had a substantial effect on the balance of payments. There had thus been large recourse to foreign borrowing, including reliance on short-term loans, and the capital account had been further substantially weakened by the flight of capital associated with political instability.

The Government that had taken office in October 1982 had acted quickly to produce the important package of measures described by Mr. Donoso, Mr. Taylor remarked. The measures represented a substantial further attempt to grapple with the fiscal situation, and the unification of the exchange rate at a much lower level than the previous official one was a bold step that would presumably need to be supported at least for a while by adjusting import controls and exchange restrictions. He would welcome any comments on the adequacy and direction of those measures. In passing, he noted that in SM/82/137 the staff had referred to the scanty data available on the financial operations of much of the parastatal sector, and he hoped that the authorities would take steps to improve their fiscal control in that important sector.

On the external front, Mr. Taylor went on, he had noted that there was a trade surplus in the first nine months of 1982, and that the overall deficit in the balance of payments had declined. However, the apparent improvement reflected a shortage of reserves and a withdrawal of external credits. He had been alarmed to see that the arrears in the official foreign exchange market had risen to US$120 million by September 1982, and he would be interested in an estimate of the level of external payments arrears following the reunification of the exchange rate.

As to the request for a drawing under the compensatory financing facility, Mr. Taylor felt that there would be little disagreement that Bolivia's exports had been badly affected by the world recession. In particular, the international prices for tin and silver had been very depressed. The resulting effect on the balance of payments justified the proposed request, and all relevant criteria were met. However, it would have been difficult for his authorities to accept the existence of unapproved exchange restrictions as evidence that the test of cooperation had been fulfilled, without the actions to unify the exchange rate. That step in itself did, however, show that the test of cooperation in an important field had been fulfilled. He had noted the staff observations to the effect that actual exports in the shortfall year were likely to be smaller than indicated by figures based on partly estimated data. He had been encouraged by indications that the new Government was determined to tackle the serious economic problems in the economy, and he welcomed the start that had been made. He would encourage the authorities to consider an early arrangement with the Fund, but he felt that it should be a stand-by arrangement rather than the extended arrangement that the authorities appeared to be contemplating.

Miss Le Lorier stated that she shared the views expressed in EBS/82/233, and that she supported the proposed decision. The language of the staff appraisal had given her the feeling--as it had to Mr. Feito--that the test of cooperation had been applied perhaps more harshly than usual for a drawing in the first 50 per cent of quota under the compensatory financing facility.

The rather long interval since the previous Article IV consultation was perhaps not a matter for great concern in view of the many staff missions to Bolivia that had been undertaken since 1979, Miss Le Lorier remarked. It was, however, regrettable that the authorities and the Fund had not been able to come to an agreement for the use of Fund resources, especially as the deterioration in the economic situation had been largely attributable to policy decisions rather than to exogenous factors. She had been pleased to learn that the Bolivian authorities were considering initiating discussions for an extended arrangement soon. It was evident that a much longer period than one year would be needed for completing the adjustment process, which would have to involve a substantial structural component. On the other hand, there seemed to be no escape during the coming year from continuing with the policy reforms introduced in November 1982.

In present circumstances it might be difficult to look far ahead, Miss Le Lorier commented. Nevertheless, she hoped that the economic development plan, now under preparation, would be completed in the not too distant future. She regretted that there were so few indications of the possible medium-term prospects in the staff paper, although she understood that it might be difficult to give final figures while negotiations were under way. If the preparation of a long-term plan was likely to take several months, it might be appropriate to give some thought to a one-year arrangement as a second-best means of supporting the efforts already under way.

She had no difficulty with the analysis by the staff of the causes underlying recent developments, Miss Le Lorier stated. She would rather discuss the immediate prospects. She had had some difficulty in assessing the impact of the emergency measures adopted in November 1982 and described in the staff papers, and she would welcome further information. For instance, what would be their effect on the public sector deficit on a full-year basis, and to what extent would they fall short of the staff's recommendations? The increases in prices of food and petroleum products, as well as the rise in public tariffs, were impressive when taken at face value; on the other hand, apart from the increases in the prices of petroleum products, they were still considerably below the current rate of inflation. It would have been helpful to have some assessment of the projected subsidies for 1983 on the basis of the new prices. The establishment of a minimum wage might be interpreted in opposite ways: it might allow a sharp reduction in subsidies, or it might stiffen the present rigidities and produce the kind of vicious circle mentioned by the staff.

Regarding the prospects for 1983, Miss Le Lorier inquired first to what extent the public sector might be reduced. The gap between the proportion of GDP actually taken up by the public sector in 1982--somewhere in the neighborhood of 20 per cent--and what the staff viewed as reasonable financing by the Central Bank--2.5-3 per cent of GDP--was very large. It seemed unlikely that the gap could be closed by the end of 1983 and, like Mr. Dallara, she would like to know what advance was likely to be made in the coming year. Second, it would be interesting to know what level of imports would be needed to allow for a small recovery, or at least the stabilization of economic activity. Imports had been cut to 60 per cent of their 1981 level, and she wondered whether a maintenance of the present level was consonant with the continued functioning of the economy without impairing export capacity to any significant extent.

Clearly, the next question would unavoidably be how much external financing the authorities could secure in 1983, Miss Le Lorier went on. She would appreciate further information on the lines of credit that the Central Bank was hoping to negotiate with the World Bank and the Inter-American Development Bank, as described on page 12 of SM/82/137. One major difficulty was obviously the recent buildup in external payments arrears. She strongly urged the Bolivian authorities to undertake a new rescheduling arrangement with the banking system as soon as possible, since the present arrangements did not cover amortization payments falling due after March 1983. Then there was the problem of bilateral loans. If Bolivia found that it was not in a position fully to service that part of its debt during 1983, a multilateral approach should be considered without undue delay. Some comment on the point would be welcome. Finally, the external debt situation was one more reason for Bolivia to enter into a new arrangement with the Fund as soon as possible. By providing financial assistance and facilitating the adoption of an underlying adjustment program, such an arrangement could significantly contribute to easing the critical situation facing the country.

The staff representative from the Western Hemisphere Department, replying to questions, observed that, since the staff report had been issued, 2 new governments had taken office in Bolivia for a total of 11 governments between 1978 and 1982. The constant changes of government disrupted the administrative machinery in Bolivia; each change of government meant that experts left the public sector and in some cases the country itself. In the circumstances, it was difficult to obtain high-quality statistics. Indeed, many of the statistical statements in the report were partly subjective. Whole areas of statistics were in fact lacking.

A number of Executive Directors had inquired whether the staff considered that Bolivia should enter into an extended arrangement or a stand-by arrangement with the Fund, the staff representative noted. The measures taken in November 1982 were the first for many years to show consistency between one field of endeavor and another. Nevertheless, they probably still fell short of what was needed to close the fiscal gap. The authorities had indicated that they would prepare a comprehensive plan within 100 days, which would expire at the end of February 1983. At that time they intended to submit a budget, a monetary program, and an exchange rate strategy. But delays in the timetable could take place. Thus, the previous day, some members of the Government had resigned. Some time could be required for a new economic team to take hold and develop the budget. Nor had any monetary program yet been prepared. It was therefore rather premature to try to answer questions as to what would happen in 1983. All that could be said was that a great deal still had to be done.

For instance, the staff representative explained, although petroleum product prices had risen by 400 per cent for jet fuel and 200 per cent for gasoline, according to the World Bank the opportunity cost for a barrel of oil was some $37.30, and after the recent increases, the retail price in Bolivia was still only $16.26. The same situation applied to electricity rates. Tax evasion had also been widespread. Finally, there was the question of the wage strategy, a point mentioned by several Executive Directors. There were no reliable wage indices in Bolivia. The staff's information had had to be derived from other sorts of data. At the beginning of 1982, the Government had issued strict instructions that no wage adjustments of more than 30 per cent should be permitted in the public sector. Nevertheless, some enterprises had allowed adjustments of 100 per cent. It remained to be seen whether the guidelines issued by the Government for the preparation of the 1983 budget would be adhered to.

Whether the Bolivian authorities would request an extended arrangement or stand-by arrangement would depend on how much structural adjustment they thought that they could undertake, the staff representative explained. It would be well to await the arrival of the actual request.

Responding to a comment by Mr. Taylor regarding the interval between consultations, the staff representative recalled that although the previous consultation with Bolivia had been held in 1979, in 1980 the Executive Board had discussed a stand-by arrangement for the country. To fit the travel schedule, consultation missions usually went to Bolivia in midyear. A mission for the 1980 Article IV consultation had visited Bolivia in July 1980, but the consultation could not be completed because a military takeover had occurred while the mission was in La Paz. Another mission went to Bolivia in February 1981; it had not only conducted an Article IV consultation, but had also begun negotiations for a stand-by arrangement. There had been some deviation from the agreed-upon program, and the authorities had asked the mission to return to Bolivia. It did so in July 1981, and its work was again interrupted by a change of government. The next

Government lasted only two months, so that no consultation was held with it. During 1982, Article IV consultations had been held in May, but since then there had been two changes of government.

Commenting on questions raised by Mr. Almeida, the staff representative said, first, that the staff had felt that the drop in GDP in 1982 could be more than 8 per cent, largely because the 8 per cent figure had been based on estimates prepared before the recent change of government. The feeling that the drop would be more than 8 per cent was partly subjective. Regarding the volume of natural gas available in Bolivia, the World Bank had prepared a report, the draft of which had been finalized toward the end of December 1982. According to that document, the proven and probable natural gas resources of Bolivia were 7.1 trillion cubic feet. Of that amount, 4.7 trillion cubic feet were proven reserves, and the remainder probable reserves. On the basis of estimated consumption and possible exports to Argentina, which had already been negotiated, Bolivia would probably have sufficient gas to export to Brazil as well. However, the authorities wished to have still further information on the probable reserves and had asked for further technical assistance from the World Bank. After further exploratory missions, the report was to be finalized during the second quarter of 1983.

Regarding the exchange rate, the staff representative went on, in Bolivia there was a disposition to favor a fixed exchange rate, but the staff believed that it was necessary to be pragmatic. It was for that reason that the staff had suggested that in present circumstances a flexible exchange rate policy was probably the most suitable. It was important to be cautious in interpreting changes in price figures in Bolivia, especially during 1982, which had been an abnormal year. Many prices had increased on speculative grounds; they would not necessarily do so again in the future. It had been asked why the state oil company had granted larger adjustments than some other state enterprises. The simple fact was that the oil company had decided to do so, despite the government injunction. Wage adjustments had been higher still in some other state enterprises. It was for that reason that the staff had placed such great insistence on controlling wages in the public sector.

Concerning the exchange rate, Mr. Dallara had inquired how the rate of $b 200 = US$1 had been decided on, and whether there was still a black market rate, the staff representative recalled. In adopting the $b 200 = US$1 rate, the authorities had indicated that the regulations governing the exchange rate were to be reviewed as part of the 1983 program. There was still a parallel market rate in Bolivia and the proceeds of some exports were not surrendered at the official rate; the present rate in the parallel market was $b 320 = US$1.

The latest information regarding arrears was that at the end of 1982 arrears were $205 million, of which $110 million were capital and $95 million due to interest, the staff representative continued. That did not mean that the balance of payments figures shown in EBS/82/233 needed to be changed; the arrears had been higher than projected but the loss of reserves lower. As to the lines of credit granted to Bolivia, the Inter-American Development Bank had granted $110 million for building a gas pipeline to the high plateau, and a loan of $35 million to be disbursed through the banking system for industrial and commercial purposes. Some of the imports of wheat into Bolivia had been paid for by the United States under Public Law 480.

The United Nations had held a meeting in New York with all the UN agencies to see whether it would be possible to raise financial assistance to Bolivia, the staff representative from the Western Hemisphere Department recalled, but the prospects had been rather dim because none of the agencies had any spare money. Meanwhile, the Central Bank's short-term liabilities with the Central Bank of Brazil, plus capitalized interest, had been renegotiated on a seven-year maturity with a two-year grace period at 2 1/8 per cent over LIBOR. A commercial bank loan to the Bolivian Central Bank, which had been for one year, had been renegotiated on a three-year basis. The Bolivian authorities had been in contact with the private commercial banks on the question of default, but no formal negotiations had taken place. The earlier agreement with the commercial banks had implied that Bolivia would enter into a stand-by arrangement with the Fund, but the commercial banks seemed to have waived that particular request. It would be very important to discover how much the commercial banks were willing to lend in fresh money to Bolivia, as the outcome might determine the type of program that the Bolivian authorities could adopt.

The staff representative from the Exchange and Trade Relations Department commented that there had been no change in the Fund's policy regarding the test of cooperation. Bolivia's willingness to cooperate had been well established. While it might at times be doubted whether the country had the capacity to cooperate, because there were many changes in government, its willingness had been demonstrated by the many requests made for staff missions and by the decisions made recently to undertake needed measures. While the staff had not recommended Executive Board approval of Bolivia's restrictions, in EBS/82/233 it had been decided to provide a description of the restrictive system, in line with Executive Board requests for such descriptions in papers containing requests for drawings under the compensatory financing facility. The staff had not been applying a stricter test of cooperation in the present case; the ample description of the restrictive system was only meant to supply adequate information.

Regarding the issue of the choice between an extended arrangement and a stand-by arrangement, the staff representative from the Exchange and Trade Relations Department remarked that, from an abstract standpoint, it could be argued plausibly that Bolivia's economy would benefit from a medium-term structural adjustment program. Such a program could certainly be devised, and it would suit the provisions of the decision on the extended Fund facility. As a matter of strategy, however, and in view of the immense uncertainties surrounding Bolivia, it might be better at the present moment for Bolivia to consider a one-year stand-by arrangement.

Miss Le Lorier explained that she had no objection to Bolivia undertaking an extended arrangement with the Fund. Her point had been that negotiations between Bolivia and the Fund had already been quite lengthy, and that it would clearly take several months more for Bolivia to prepare a multiyear adjustment program in line with the requirements of an extended arrangement. In view of the importance of providing assistance rapidly, she had thought that it might be better to offer a one-year stand-by arrangement than to seek longer-term perfection.

The staff representative from the Western Hemisphere Department recalled that when the stand-by arrangement with Bolivia had been negotiated in 1980, the stategy proposed by the staff had been exactly that described by Miss Le Lorier. The letter of intent relating to that arrangement had stated that Bolivia was entering into a one-year stand-by arrangement with the Fund and that if that arrangement were successful, it would negotiate an extended arrangement.

The Acting Chairman remarked that, as the staff representative from the Western Hemisphere Department had explained, the Fund had made many efforts to remain in contact with the Bolivian authorities, and that at no time had the authorities rejected those efforts. Nevertheless, in the circumstances it had not been possible to complete Article IV consultations in a manner that would have satisfied the Executive Board. Management and staff had in many countries made renewed attempts to complete consultations even in cases where there were obvious difficulties. Nevertheless, he would take note of the observations by Mr. Taylor and other Directors regarding the matter of Article IV consultations with members, particularly those that might be candidates for the use of the Fund's resources either under the compensatory financing facility or in the upper credit tranches.

Mr. Taylor commented that he hoped that when the staff visited countries either to discuss Article IV consultations or to negotiate an arrangement, it would make it clear that it was important for the country to provide sufficient information to enable the Executive Board to make a judgment and to be kept in the picture. It seemed to him that on some occasions a staff mission visiting a country for an Article IV consultation sometimes entered into discussions for a possible arrangement. It should be made clear to the authorities that the Article IV consultation had priority.

Regarding the test of cooperation in connection with drawings under the compensatory financing facility, Mr. Taylor recalled that in the past some members of the Executive Board had asked for an explicit reference to the existence of unapproved exchange restrictions. For his part, he felt that it was essential that there should be that sort of reference in papers connected with drawings under the compensatory financing facility. The existence of unapproved exchange restrictions was relevant to any assessment of what a country meant when it said that it would cooperate with the Fund. As he understood it, the existence of unapproved exchange restrictions meant that the staff believed that in the foreseeable future those restrictions were not likely to be lifted, and that was a judgment regarding the intentions of the authorities. He had also been asking the staff to provide an assessment of how important the maintenance of those unapproved restrictions was in relation to the balance of payments situation. He was glad to see that the staff was beginning to make such appraisals.

Mr. Donoso stated that he would convey to his authorities in La Paz the interesting remarks made by Executive Directors. He was especially grateful for the recognition by Executive Directors of the importance of the measures taken by the Bolivian authorities since November 1982, and of the fact that those measures reflected a serious commitment to address the main problems of the Bolivian economy. The Government had given itself a fixed period in which to establish a more comprehensive program. For the time being, the authorities were not making a decision between a stand-by arrangement and an extended arrangement. They would take that step when they had had time to formulate their program.

The Acting Chairman made the following summing up:

Executive Directors generally agreed with the thrust of the staff appraisal on Bolivia's economic position and prospects contained in the report for the 1982 Article IV consultation. While noting that Bolivia continues to confront very severe problems, Directors were encouraged that the elected Government that had assumed office in October 1982 had moved boldly to adopt adjustment measures that were long overdue, and that a comprehensive program of economic adjustment and reactivation was now being developed. Directors commented favorably on the emergency measures and in particular they noted the magnitude of the exchange rate correction and of the adjustments made in controlled prices, especially for fuels. They also commended the new authorities for the prudence they had displayed in wage policy, which they stressed would be central to the success of the adjustment effort.

Given the size of the imbalances that had to be corrected, much still remained to be done, perhaps including, it was suggested, a debt restructuring, before the country would be in a position to resume the normal service of its external obligations and to phase out other exchange restrictions. A major and sustained effort to reduce the very large disequilibrium in the public finances is badly needed to create the conditions for a revival of economic activity. Monetary policy will have to be consistent with the other aspects of the economic adjustment program.

Directors noted the authorities' expressed intention to enter soon into discussions with the Fund with a view to establishing a stand-by or extended arrangement. Directors welcomed the intention of the authorities to implement a stabilization program that would justify substantial Fund support with conditional resources. They stressed the need for Bolivia to proceed with fundamentally important structural measures, which would require great determination, as well as time, for taking hold. Several Directors observed that, notwithstanding their full acceptance that Bolivia's problems are importantly structural and medium term in character, a number of considerations pointed toward a one-year stand-by arrangement as perhaps the most practical approach in the first instance. However, it was agreed that the issue will have to be considered on its own merits when it arrives.

Finally, the importance of regular Article IV consultations with Bolivia was noted.

The Executive Board then took the following decision:

Purchase Transaction - Compensatory Financing Facility

1. The Fund has received a request by the Government of Bolivia for a purchase of SDR 17.9 million under the Decision on Compensatory Financing of Export Fluctuations (Executive Board Decision No. 6224-(79/135), adopted August 2, 1979).

2. The Fund notes the representation of Bolivia and approves the purchase in accordance with the request.

3. The Fund waives the limitation in Article V, Section 3(b)(iii).

Decision No. 7300-(83/9), adopted
January 10, 1983

2. MAURITIUS - PURCHASE TRANSACTION - BUFFER STOCK FINANCING FACILITY - INTERNATIONAL SUGAR AGREEMENT

The Executive Directors considered a request by Mauritius for a purchase equivalent to SDR 3.605 million, equivalent to 8.9 per cent of quota under the buffer stock financing facility (EBS/82/231, 12/13/82; and Sup. 1, 1/7/83).

Mr. Tshishimbi stated that his Mauritian authorities were grateful to the Executive Board and to management for the constant attention that they had devoted to the resolution of the financial difficulties that had beset Mauritius for the past several years. In return, Mauritius had demonstrated a remarkable sense of cooperation in its use of Fund resources. The Executive Board had recently discussed the staff report for the mid-term review of the financing program for fiscal year 1981/82 supported by a stand-by arrangement. In concluding that review, the Executive Board had noted that the 1981/82 program had been successfully carried out. Apart from the government sector, where there had been some slippages, the major targets had either been exactly attained or even exceeded. For instance, real GDP had reached the targeted growth rate of 5 per cent a year. Inflation had been reduced from 27 per cent a year in 1980/81 to 13 per cent in 1981/82, although the target had been 25 per cent. The external current account deficit had been reduced from about 15 per cent of GDP in 1980/81 to 5 per cent of GDP in 1981/82, although the target had been 12 per cent. Finally, the overall balance of payments deficit had been reduced from 10 per cent of GDP in 1980/81 to 3 per cent in 1981/82, compared with some 6 per cent in the program.

The staff had indicated in EBS/82/231 that the balance of payments was likely to remain weak for most of the year ahead, Mr. Tshishimbi went on. The current account deficit was expected to increase to 6 per cent of GDP, while the overall balance of payments deficit could exceed 4 per cent of GDP. At the same time, the authorities envisaged a further drawdown of the country's already meager foreign reserves. In the circumstances, the request presented by Mauritius was fully justified and he recommended its approval by the Executive Board.

Mr. Malhotra remarked that the request for a drawing equivalent to SDR 3.605 million related to special buffer stocks created and held by Mauritius under the stocking obligation of the International Sugar Agreement. Mauritius was very dependent on exports of sugar, which accounted for over half its total exports. The fluctuations in sugar production in recent years, due either to crop disease or to severe cyclones, had had adverse effects on the economy. It was thus unfortunate that when sugar production was expected to recover in 1982, the country would find itself facing very depressed world prices. He was glad to note from EBS/82/231 that the International Sugar Council was proposing to hold a negotiating conference in Geneva in May 1983 to secure the cooperation of the European Community in finding a long-term solution to the world sugar crisis. The staff had shown conclusively that Mauritius had a balance of payments need and that, despite recent improvements, it would face an overall balance of payments deficit in the neighborhood of SDR 60 million for fiscal year 1982/83, while gross reserves would decline to the equivalent of three weeks' imports. It was noteworthy that in recent years Mauritius had been making significant adjustments, both internal and external, by implementing Fund-supported programs. Cooperation with the Fund had proved beneficial to the country, and the authorities' assurance regarding continued cooperation was welcome. He wholeheartedly supported Mauritius' request.

Miss Le Lorier stated that she could warmly support a request from Mauritius for a purchase under the buffer stock financing facility. In the present situation of the sugar market, there was little doubt of the need for constituting the stocks required under the International Sugar Agreement, and Mauritius had complied with its obligations by constituting stocks in July and September 1982. Mauritius had been actively cooperating with the Fund, and its performance under a recent program had been quite satisfactory. The proposed purchase, however small it might seem, would represent a useful contribution to the country, allowing it to draw down its gross reserves somewhat less than it would otherwise have had to do.

Mr. Mtei supported the proposed decision. Table 1 on page 3 of EBS/82/231 indicated that the balance of payments outturn for Mauritius would deteriorate somewhat in 1982/83. The overall deficit as a percentage of GDP would increase from 3.2 per cent in 1981/82 to 4.4 per cent in 1982/83, reflecting, in part, a shortfall in export earnings from sugar as a result of depressed prices on the world market. Despite an increase in the output of sugar from 524,000 tons in 1981/82 to about 700,000 tons in 1982/83, it was expected that the export value would remain unchanged. In the meantime, reserves were expected to fall to about three weeks' imports. Mauritius' balance of payments need was therefore clearly established.

As to the test of cooperation, Mr. Mtei noted that the most recent program for Mauritius had been approved by the Executive Board on December 21, 1981 and supported by a one-year stand-by arrangement. The authorities had made considerable progress with their adjustment efforts, as they had managed to reduce the overall deficit in the balance of payments from 9.7 per cent of GDP in 1980/81 to 3.2 per cent in 1981/82.

Mr. Jaafar stated that he could support the request by Mauritius for a purchase equivalent to SDR 3.605 million under the buffer stock financing facility; he also supported the proposed waiver of the limitation in Article V, Section 3(b)(iii). Like Mr. Tshishimbi, he had noted that during the past year or so the performance of the Mauritian economy had been better than had been expected under the stand-by arrangement. The current account deficit for fiscal year 1981/82 had been SDR 56 million, less than half the expected deficit of SDR 123 million. Similarly, the overall balance of payments deficit had been SDR 33 million instead of the expected SDR 65 million. The main reasons for the improvement in the performance were a reduction in project-related imports, the favorable impact of the depreciation of the rupee in September 1981, and prudent management policies. In fiscal year 1982/83, however, the balance of payments situation was expected to deteriorate, primarily because of the depressed markets for Mauritius' exports. His chair appreciated the considerable difficulties faced by countries relying heavily on exports of sugar. An effort had been made by a group of sugar producers and consumers to stabilize the sugar market within the International Sugar Agreement. Unfortunately, the European Community was not a member. He hoped that the conference to be held in Geneva in May 1983 would make progress toward greater cooperation between the European Community and the International Sugar Organization. If greater stability could be achieved in the price of sugar, it would greatly help to stabilize the export earnings of countries such as Mauritius, which relied heavily on the sugar trade.

Mauritius had already met its obligations under the International Sugar Agreement by fully constituting obligatory stocks of 26,966 tons of sugar, Mr. Jaafar observed. He was satisfied with the evaluation used for the purpose of the buffer stock facility, and he had noted that the sugar stocks were free of collateral. He also noted with satisfaction the undertaking of the authorities to cooperate with the Fund in finding appropriate solutions to their balance of payments difficulties. The request met all the requirements of the buffer stock financing facility, and he therefore had no hesitation in supporting it.

Mr. Dallara commented that the buffer stock and balance of payments aspects of the request were straightforward. As far as the test of cooperation with the Fund was concerned, the ongoing adjustment effort that the Board had reviewed in November 1982, was clear evidence of the willingness of the Mauritian authorities to cooperate with the Fund. He willingly supported the request and encouraged the authorities to move ahead with their commendable adjustment effort.

Mr. Morrell stated that the request was a very straightforward one that clearly met all the criteria under the buffer stock financing facility. He would therefore warmly support it.

The Acting Chairman noted that nearly all speakers had referred to the test of cooperation in connection with a drawing under the buffer stock financing facility. However, in EBS/82/231 the staff had made no mention of cooperation per se. The staff had written the paper as it had because neither the decision on the buffer stock financing facility nor that on the International Sugar Agreement made reference to the requirement of cooperation with the Fund that was so integral a part of the decision on compensatory financing.

The staff representative from the Research Department agreed that the buffer stock financing facility decision did not include any reference to cooperation. However, in their 1969 report, "The Problem of Stabilization of Prices of Primary Products," on which the buffer stock decision was based, Executive Directors had indicated in item (3) of Section 2 that the Fund would want to apply the requirement that members should cooperate with it in efforts to find a solution for their balance of payments problems, in providing any buffer stock assistance. It had therefore been the practice to include that sentence in the staff appraisal for any request.

The Executive Board took the following decision:

1. The Fund has received a request by the Government of Mauritius for a purchase of SDR 3.605 million under the decision on Buffer Stock Financing Facility: The Problem of Stabilization of Prices of Primary Products, Executive Board Decision No. 2772-(69/47), adopted June 25, 1969, as amended by Decision No. 4913-(75/207), adopted December 24, 1975, and the decision on Buffer Stock Financing Facility: 1977 International Sugar Agreement, Executive Board Decision No. 5597-(77/171), adopted December 16, 1977.

2. The Fund determines that this purchase would be in conformity with the decisions referred to in (1) above, notes the representations of Mauritius, and approves the purchase in accordance with the request.

3. The Fund waives the limitation in Article V, Section 3(b)(iii).

Decision No. 7301-(83/9), adopted
January 10, 1983

APPROVED: June 20, 1983

LEO VAN HOUTVEN
Secretary