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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 83/117

10:00 a.m., August 3, 1983

W. B. Dale, Acting Chairman

Executive Directors	Alternate Executive Directors
	L. K. Doe, Temporary
	G. Ercel, Temporary
	P. D. Péroz, Temporary
	J. Delgadillo, Temporary
R. D. Erb	
	M. B. Chatah, Temporary
	H. Kobayashi, Temporary
	I. R. Panday, Temporary
R. K. Joyce	
	H. A. Arias, Temporary
	G. Grosche
	C. P. Caranicas
R. N. Malhotra	
	J. E. Suraisry
	T. de Vries
A. R. G. Prowse	
G. Salehkhou	O. Kabbaj
	E. I. M. Mtei
	M. Toro, Temporary
	I. Fridriksson, Temporary
N. Wicks	
	Wang E.

J. W. Lang, Jr., Acting Secretary
S. J. Fennell, Assistant

Also Present

His Excellency Erik K. Otoo, Ambassador for Ghana. African Department: P. A. Acquah, D. T. S. Ballali, E. L. Bornemann, R. O. Carstens, A. B. Diao, R. A. Franks, J. W. Kratz, R. P. Kronenberg, S. N'guiamba, I. C. Tandeciarz. Exchange and Trade Relations Department: D. K. Palmer, Associate Director; K. M. Huh, S. Kanesa-Thasan. Legal Department: P. L. Francotte, W. E. Holder. Research Department: W. C. Hood, Economic Counsellor and Director; K.-Y. Chu, E. C. Meldau-Womack, B. E. Rourke, A. Salehizadeh. Advisors to Executive Directors: S. R. Abiad, A. A. Agah, J. R. N. Almeida, P. Kohnert, Y. Okubo. Assistants to Executive Directors: H. Alaoui-Abdallaoui, R. Bernardo, M. Camara, T. A. Connors, M. Eran, G. Gomel, M. Hull, V. K. S. Nair, G. W. K. Pickering, J. Schuijer, Shao Z., N. Toe, J. C. Williams, A. Yasseri.

1. GHANA - 1983 ARTICLE IV CONSULTATION; REQUEST FOR STAND-BY ARRANGEMENT; AND USE OF FUND RESOURCES - COMPENSATORY FINANCING FACILITY

The Executive Directors considered the staff report for the 1983 Article IV consultation with Ghana and a request for a stand-by arrangement in an amount of SDR 238.5 million (EBS/83/140, 7/7/83; and Cor. 1, 7/28/83), together with a request for a purchase equivalent to SDR 120.5 million under the compensatory financing facility (EBS/83/146, 7/12/83; and Sup. 1, 8/1/83). They also had before them a report on recent economic developments in Ghana (SM/83/161, 7/25/83).

The Acting Chairman welcomed the Ambassador for Ghana, His Excellency Erik Otoo.

The staff representative from the African Department stated that there were some errors in Table 2 of EBS/83/140, and also some inconsistencies between that table and the basic data table appearing in the paper on recent economic developments. The staff would issue a corrected version of those tables after the Executive Board Meeting, but if there were any particular questions he would be glad to point out the errors.

Mr. Salehkhou made the following statement:

Throughout most of the 1970s, non-oil developing countries suffered severe economic setbacks, largely as a result of a number of adverse exogenous developments, including most particularly a sharp deterioration in their terms of trade. These difficulties were compounded in Ghana by the continued postponement of a decisive adjustment action to reverse the trend of economic deterioration and pave the way for a resumption of growth. Ghana's economic situation was particularly characterized by large domestic and external imbalances, including substantial price distortions and an increasingly inadequate exchange system that developed into serious disincentive for both domestic production and exports and resulted in smuggling and parallel market transactions. There was also a sharp deterioration in the Government's financial position as the inadequate exchange rate and the parallel market deeply eroded the budget tax base. Furthermore, the Government's recourse to bank credit to compensate for shrinking revenues accelerated the expansion of monetary growth, developing substantial upward pressures on inflation rates, while a critical shortage of foreign exchange forced a considerable curtailment of imports, leading to the emergence of large bottlenecks.

More recently, Ghana's economic and financial difficulties were complicated further by two major adverse exogenous factors, including severe drought and bush fires that inflicted substantial damage to output and infrastructure. There was also the arrival in early 1983 from Nigeria of one million returnees, who are estimated to have augmented Ghana's population by 10 percent and have put severe pressure on already precarious food supplies.

A few figures clearly illustrate the deep deterioration of Ghana's economy throughout the 1970s and in the early 1980s. Real output was about 17 percent (30 percent on a per capita basis) less in 1982 than in 1976. Cocoa purchases by the Cocoa Marketing Board (CMB), which until 1980 provided two thirds of export receipts, declined by 35.8 percent between 1975 and 1981, while the production of gold fell by about 46 percent between 1975 and 1982. Official price indices rose on average by 82 percent a year in 1977-81, despite a heavy subsidization of petroleum prices through the overvalued exchange rate. Finally, despite the shrinking size of the Government in relation to GDP, credit and monetary expansion accelerated to 29 percent in 1980, and to 58 percent in 1981. In the circumstances, the new Ghanaian Government, established by the Provisional National Defense Council upon assuming power on December 31, 1981, recognized the seriousness of Ghana's financial and economic difficulties, and acted swiftly to arrest the declining trend of the economy and to undertake an objective and comprehensive assessment of the situation, which, the authorities felt, was necessary before the implementation of their far-reaching adjustment and reform program.

Thus, while the newly established National Economic Review Committee was assessing the Ghanaian economic situation and developing a short-term and medium-term program, the authorities adopted simultaneously a number of radical corrective measures aimed at reducing liquidity in the system, improving the Government's financial position, and attacking smuggling and corruption. The measures implemented in 1983 were largely of an emergency nature and are being rationalized in the context of the more comprehensive program developed by the National Economic Review Committee to be supported by a one-year stand-by arrangement with the Fund.

Ghana's new program constitutes a definite shift in the country's economic policies toward a broader use of market-oriented economic instruments, particularly through the restoration of price incentives in all the important producing sectors and through a major reform of the exchange system. The program also aims at improving the financial position of the public sector so as to reduce the pressure on monetary expansion and ease the inflation rate. On the other hand, the program strives toward promoting a better supply situation by rebuilding economic infrastructure and liberalizing imports. The main elements of the program were implemented in April 1983, prior to the concluding discussions with the Fund for the requested stand-by arrangement.

The implementation of a major reform of the exchange system and the authorities' commitment with regard to the flexible management of exchange rate policy, are undoubtedly the cornerstone and most important elements of the adjustment program. Given the social and political implications of exchange rate adjustment in Ghana, the new exchange policy, introducing actual depreciations of the currency of up to 990 percent, is indicative of the authorities' serious attitude toward adjustment. While the new exchange rate system may seem complex with its various bonuses and surcharges and implicit rates, it is important to note that exchange rate policy has traditionally been a sensitive issue in Ghana and that some time is needed for the general public to understand and accept the large changes introduced. Furthermore, the authorities clearly view the reform introduced last April as a first step, and have expressed their firm intention to announce the present implicit rates as the new official exchange rates before October 1983, thus eliminating the bonus/surcharge system, and unify during the program period the exchange rate at a realistic level, with the aim of maintaining Ghana's international competitive position. It is also important to note that the way the new system is operated ensures that the Bank of Ghana does not incur, over time, losses in its exchange transactions.

The reform of the exchange rate system is complemented by a comprehensive set of far-reaching measures encompassing external, fiscal, and price and income policies. With regard to price and income policies, the program objectives aim at using producer prices as an important incentive for increasing domestic production, particularly for the main export crop, and, on the other hand, at implementing a large price deregulation and a full pass-through to domestic prices of higher import costs. The latter should result, except for petroleum products, in an elimination of all budgetary subsidies. Concerning petroleum products, the authorities feel that, considering the adverse effects on all sectors of the economy of large price increases, which averaged 104 percent in April 1983, it is desirable to implement the elimination of all subsidies only in a gradual manner, with the understanding that the subsidization would not exceed the maximum amount accounted for in the 1983 budget, and that prices in line with international rates will be in effect during the program period.

Price and income policies under the adjustment program also include major adjustments in prices, rates, and tariffs charged by public sector entities; adjustments which ranged from 100 percent to 300 percent, and that should substantially enhance the said entities' financial position, thus sharply reducing their need for bank financing and budgetary support. In order to attenuate the effects of such measures on the population's standard of living, particularly on the civil service, where real salaries in early 1983 were down to 16 percent of their 1975 level, government employees were granted a 60 percent salary increase, while wages are being raised by 25 percent on average in public sector enterprises and in the private sector. On the other hand, the authorities believe that competitive forces will need time to develop in Ghana, and that the economy is still subject to a number of market imperfections. Therefore, they have issued guidelines with regard to manufacturers' and retailers' profit margins, and have reset prices for a number of basic consumer goods.

With regard to the promotion of domestic production and exports, while the upward adjustment in cocoa producer prices, together with the large depreciation of the exchange rate, should play a major part in such a promotion, a contribution of equal importance is also expected from the authorities' efforts to increase the availability of essential imported inputs and to rehabilitate the productive base. These efforts are supported by Stabex credits and by financial assistance from the Food and Agricultural Organization. Rehabilitation of other productive sectors, including timber and gold production, is also being undertaken in cooperation with international organizations such as the African Development Bank and the World Bank. Considering Ghana's abundant natural and managerial skills, the above mentioned policies should result in substantial output increases and sharply improve the country's export performance in a relatively short period of time.

With regard to fiscal policy, major gains are obviously expected from the exchange rate adjustment, the improvement in economic activity, and the reabsorption of parallel market transactions, which should considerably increase government revenues through the restoration of the budget tax base. It should be recalled that in 1982 the authorities introduced important measures on the expenditure side, including severe curtailment of current and development outlays, the introduction of tight control over spending, and an important review of manpower needs leading to reduced overemployment in the civil service and restricted guidelines for new recruitment. As these measures are strengthened in the 1983 budget and as capital expenditures will be limited to replenishing essential supplies and undertaking repairs, total outlays should represent no real increase in 1983, apart from the 60 percent salary adjustment, and should enable the authorities to achieve a further reduction of the budgetary deficit to 3.5 percent of GDP, which compares with 8 percent and 4.6 percent in 1980 and 1982, respectively.

Improvements in the financial position of the Government and the public sector in general are largely consistent with the authorities' cautious monetary and credit policies which are geared to support economic recovery, to aid projected increase in capacity utilization in the economy and to accommodate the immediate requirements of importers and manufacturers. Considering the uncertainties concerning the initial impact of the measures implemented, ceilings cover only the period through August 31, 1983, and should be set for subsequent quarters during the program reviews provided for in the program. The reviews should also re-examine, with regard to monetary policy, the need to increase interest rates on deposits. In this regard, while recognizing the need to aim for positive real interest rates, the authorities felt that it was inappropriate to increase credit costs immediately after the major reforms introduced, particularly in the exchange system, when a sharp increase in credit needs by manufacturers and importers is expected, and that it will be desirable to review interest rate policy once prices stabilize.

With regard to balance of payments policies, the projected large increase in capital inflows will enable the authorities to substantially raise the level of imports in 1983 to sustain economic recovery and alleviate acute shortages of essential goods. However, exports are not expected to change significantly in 1983 as a result of slow recovery in world prices of Ghana's exports and as the positive effects of the adjustment program on exports are felt beginning next year.

Ghana's need for capital inflows to rehabilitate a long-neglected infrastructure as well as manufacturing and agriculture should accelerate the growth of external debt in the medium term, although the level of outstanding debt is relatively low. The authorities are aware of the risks surrounding such an acceleration and are committed to pursue a policy of prudent external debt management so that the debt service burden remains at a sustainable level. Ceilings on external borrowings under the program are largely in line with such a policy.

With regard to the request under the compensatory financing facility, I believe that the staff paper is comprehensive and clearly builds the case in favor of such a use of Fund resources. Finally, while recommending to the Executive Board the adoption of these proposed decisions, I wish to point out that my Ghanaian authorities, in addition to committing themselves to the successful implementation of the present program, have expressed their willingness to adopt supplementary measures which may become necessary to correct any unforeseen adverse development.

Mr. Grosche remarked that it was regrettable that the Executive Board had not had a chance to express its opinion on the developments in the Ghanaian economy over the previous three years. For two years, Ghana had suffered from a decline in world market prices for its products and from an inconsistent economic policy that had depressed economic activity further. However, in April 1983 the authorities had taken courageous efforts to overcome the unsustainable situation. While taken belatedly, they represented a substantial step toward rehabilitating the economy.

The authorities deserved to be commended, particularly because they had decided to introduce reforms at a time when droughts and the influx of returnees made the economic situation even more critical, Mr. Grosche considered. The restructuring of relative prices in order to increase supplies was particularly welcome and he hoped that the authorities could maintain and broaden the new incentive system over time. Appropriate incentives in the form of higher producer prices and effective exchange rate measures had to be accompanied by a greater inflow of imported goods to make possible a higher level of productivity. Therefore, Ghana would have to run a current account deficit and it would be necessary to draw heavily on foreign savings. Could the staff indicate to what extent an increase in interest rates to a positive level would contribute to domestic resource mobilization in Ghana?

A current account deficit was projected for a number of years until exports increased to a level that would make a higher foreign debt service ratio sustainable, Mr. Grosche remarked. He hoped that the authorities would react flexibly if the underlying assumptions turned out to be less favorable than expected. Table 8 on page 34 of EBS/83/140 assumed that a private capital inflow of $192 million in 1983 would partly cover the projected current account deficit of $525 million. Could the staff indicate what would happen if the inflow of foreign capital was not sufficient in 1983? Given the adjustment program, it did not seem appropriate to reduce the level of imports. What would the Government do to secure external financing?

On exchange rate policy, he welcomed the flexible approach adopted by the authorities and hoped that the multiple rates would be unified at the end of the program period, Mr. Grosche stated. Even if a multiple currency practice might serve its purpose on a temporary basis, administrative problems of such a complex system might eventually develop.

He noted from the government budget projections that the tax base had been seriously eroded over time, Mr. Grosche went on. Smuggling and tax evasion had become common features in Ghana. Government revenues were expected to increase by more than 250 percent in 1983 as a result of sizable increases in producer prices and exchange rate adjustments. A marked improvement in the operations of the internal revenue service seemed necessary to bring about such a high increase. More important, the projected level of imports would need to be realized. Would the increase in imports of foreign goods meet the program target? There were uncertainties regarding fiscal projections. Expenditure increases might be unavoidable owing to restructuring of the price system, and it therefore appeared that the established credit ceilings would be overshot. Were there contingency plans for raising taxes if revenue shortfalls emerged?

The staff had clearly described the problems caused by the large influx of returnees, in particular, the additional burden on the food supply, Mr. Grosche noted. In the short run, the reintegration of more than one million people would be a severe hardship for society. However, in the medium and long term, the impact of the returning migrants could be positive as they had experienced another social environment, had developed skills, and might be willing to take risks when establishing a new life in their own country. By being more entrepreneurial than their compatriots, they might be better prepared for modern society and contribute substantially to future growth.

With respect to the request for a drawing under the compensatory financing facility, the export shortfall had been attributable, in part, to misguided policies, Mr. Grosche considered. However, on balance, he was willing to support the request. Finally, the authorities had been cooperating closely with the World Bank; he hoped that active participation by the World Bank could be maintained over the long term and that it would continue to yield favorable results.

Mr. Mtei stated that Ghana provided a classic example of a once well-to-do and potentially prosperous economy that had been brought to the verge of collapse because of the authorities' delay in implementing an effective adjustment program. A number of exogenous factors had contributed to the deterioration in the economy, including the depressed commodity markets for Ghana's exports, the intermittent droughts and bush fires, and the recent influx of people resulting in a population increase of 10 percent in a matter of weeks. Even so, the weak economic position was primarily due to the authorities' delay in pursuing appropriate policies.

Ghana's economy had been under severe strain almost continuously for the past decade, culminating in a decline in real growth of 7 percent in 1982 alone, Mr. Mtei observed. Exports had declined sharply, particularly over the previous four years, as the cedi had remained overvalued and inflation had soared. The terms of trade had worsened as international market prices for the main export commodities dropped. Rising costs of imports and decreased export earnings had caused a reduction in imports of essential inputs for agriculture, industries, and services, resulting in underutilization of Ghana's productive capacity. The erosion of the tax base had widened the fiscal deficit, and had led to excessive domestic credit formation. The appreciation of the cedi had been a disincentive for export production and led to the development of parallel markets in goods and to smuggling, which had severely strained the balance of payments position.

He commended the authorities for the courageous steps taken to implement an adjustment program, Mr. Mtei went on. The program was comprehensive and focused on the exchange rate, the most crucial aspect of the economy. The adjustment measures called for a substantial devaluation of the cedi; a viable balance of payments position should be restored as export proceeds would increase and be paid through official channels. Furthermore, imports should be brought back to a satisfactory level.

On fiscal policy, if public expenditure were contained at reasonable levels, it should be possible to direct the increased revenues to productive sectors in order to rehabilitate the Ghanaian economy, Mr. Mtei remarked. He hoped that the authorities had the resolve to persevere with the adjustment measures until the economy was restored to a stable position. That task would not be easy, and there would be attempts from various sections of the population--in particular, from those who had been benefiting from parallel markets--to divert them from their goal.

He urged the staff to follow closely the implementation of the adjustment program so that, if there were deviations, the causes could be identified early enough for prompt corrective measures to be introduced, Mr. Mtei said. The Ghanaian program should not be allowed to fail; its success would be an example to some of the other economies that were in similar straits because of reluctance to take effective adjustment action.

How had the Government used the ₵ 1.3 billion worth of 50-cedi notes withdrawn from circulation to retire its debts at the Central Bank, Mr. Mtei inquired? Did the public not surrender the 50-cedi notes in exchange for notes of lower denomination? If the public had not received compensation, it seemed likely that poorer rural people would have been hit hardest since they were most likely to keep their savings in large-denomination notes because of the absence of banking facilities in rural areas. Such action must have seriously eroded the rural populations' confidence in financial assets and could drive them into a barter system. The staff had referred to the authorities' efforts to refund the former holders of the 50-cedi notes and, under certain conditions, to issue them with interest-bearing stock as compensation. Action of that sort was only a second-best solution, and the authorities would be well advised to do everything possible to reassure the rural public that they would not take such action in future. On a related point, he hoped that once the economy was on track, the authorities would no longer need to enforce payment by check.

He supported the request for the use of Fund resources under the compensatory financing facility, Mr. Mtei indicated. Ghana had a clear balance of payments need, the overall deficit was considerable enough to deserve Fund assistance, and the test of cooperation had been met. The short-term character of the shortfall was evident, and a substantial recovery was projected for the two postshortfall years.

Mr. Joyce remarked that Ghana's adjustment program was long overdue. It was regrettable that the Executive Board had not had the opportunity to discuss developments in the Ghanaian economy for the previous two years, but he appreciated that there had been political changes in the country and that therefore discussions between the authorities and the Fund might have been difficult. He was glad to see that the staff had proposed that, in addition to the review of the stand-by arrangement an Article IV consultation should be held within the next 12 months.

Ghana's economy had stagnated and, indeed, deteriorated over the previous 15 years, Mr. Joyce observed. That deterioration had been partly attributable to the fall in world prices and weakening markets for many of Ghana's export products, but it had also been attributable to the existence of basic structural imbalances. The effect of the policy shortcomings and of the international developments had been accentuated by the sudden return of one million Ghanaian workers from abroad, droughts that had had a particularly severe impact in food-growing areas, and the smuggling and hoarding that had developed because of the rigid pricing policies. As a result there had been shortages of food; shortages of equipment and spare parts, which in turn had inhibited production--particularly of minerals--and the operation of the transportation network, and hence the movements of products to export; shortages of essential imports, particularly insecticides, with a consequent impact on agricultural production; and, finally, shortages of capital, which had prevented further development of the country's resources, including the bauxite deposits in Ghana's interior that required substantial capital investment in transportation and power generation.

At the same time, there had been a deterioration in the fiscal situation, Mr. Joyce noted. As a consequence of the large fiscal deficits, there had been an overextension of credit, a relative reduction in access to credit by the private sector, and a heightened rate of inflation, which in turn had translated into a worsening balance of payments situation despite the increased control of imports and capital transfers.

Although successive Governments in Ghana had been aware of the problems, it was not until recently that an administration had been prepared to go to the root of the problem and to tackle the basic defects in the system, Mr. Joyce considered. The new Government had taken some time to identify its priorities, to begin taking the necessary measures, and to negotiate the program with the Fund. Nevertheless, those steps had been taken in the previous 18 months. Negotiations with the staff had been lengthy, but the authorities had introduced some measures shortly after coming into office in 1982. In April 1983, they had adopted a comprehensive and courageous program. The authorities recognized, first, that fundamental changes were needed; second, that those changes had to be made urgently; and, third, that continued efforts would be required over a number of years if the economy was to be brought back on track.

The authorities had taken a number of key steps, Mr. Joyce observed, to limit restrictions and to restore incentives. First, they had taken action to reform the exchange rate system: more realistic effective rates of exchange for the cedi had been established. He realized that the authorities wished to proceed cautiously and hence had started with essentially transitional arrangements involving multiple rates and a system of bonuses and surcharges. As the authorities intended to establish a unified rate at a realistic level by the end of the stand-by arrangement, their exchange rate action should be acceptable to the Fund.

Second, the authorities had taken measures to establish more realistic producer prices, an essential element if production and exports were to be increased, Mr. Joyce commented. As the authorities themselves had recognized, those measures alone were not enough, and it was essential to increase imports of agricultural inputs--in particular, insecticides--and to begin providing some incentives for production by ensuring that goods would be available in country stores so that farmers could make use of their financial gains.

Cocoa prices had been increased by 67 percent, Mr. Joyce noted. The authorities had also introduced new wage and salary guidelines; minimum wages had been increased substantially, and wages in the Civil Service had been increased by 60 percent. Nonetheless, the authorities had stated their intention to narrow economic differentials and to limit future wage increases to an amount justified by increased productivity. Their pricing and income policies and, in particular, their decision to let higher import costs be reflected in most domestic prices were welcome. Furthermore, the action taken to increase substantially the prices, rates, and tariffs charged by public utilities and public sector corporations, and to remove price controls on domestically produced products, must have been a difficult step. Nevertheless, it was essential if the hoarding and smuggling within the economy was to be eliminated. The authorities' intention to monitor both revenue and expenditure on a monthly basis was commendable. He hoped that they would be able to implement their intentions. Often in a country experiencing economic difficulties, the morale and expertise of the administration deteriorated, and the ability to implement new measures was weakened.

The authorities hoped to narrow the fiscal deficit from 4.6 percent of GDP in 1982 to 2.5 percent in 1984, which depended on whether production and exports, and hence government revenues, would be as buoyant as projected, Mr. Joyce observed. Could the staff provide any last-minute information with respect to that objective?

Cautious monetary and credit policies were to be pursued, Mr. Joyce noted. The credit expansion permitted under the terms of the stand-by arrangement would, to a large extent, be used to accommodate the needs of the private sector and the commercial enterprises in the public sector.

He was impressed by the actions taken by the authorities and could therefore support both requests, Mr. Joyce said. The stand-by arrangement provided adequate evidence that the test of cooperation with the Fund had been met. He did, however, have some concerns. First, the balance of payments outlook was uncertain. Total exports were not expected to recover in 1983, and a large increase in imports--of over 80 percent--had been projected for that year. Such a high level of imports was necessary, but the current account deficit would increase to 10 percent of GDP and, even with a substantial increase in capital inflows, the overall balance of payments was expected to record a deficit of $141 million.

Second, the fiscal outlook was uncertain, Mr. Joyce went on. One major weakness was that revenues were dependent on import duties; if there were delays on imports entering the country, actual revenues might fall short of target, and there was the risk that monetary targets would be overshot. Could the staff outline the Ghanaian authorities' contingency plan? He supposed that additional revenue measures could be introduced, as no action had been taken in April 1983.

Third, on a more fundamental point, he was concerned that the program might not be realistic in the short term or medium term, Mr. Joyce continued. In the short term, there would be a period of large increases in prices because of the effect of the new exchange rates, the elimination of consumer subsidies--with the exception of petroleum--and the lower increases in wages and salaries. All those measures were necessary and advisable, but were difficult for any government or any population to live with. The authorities were clearly aware of those dangers. Indeed, they had initially had some trouble selling the adjustment program to the public, but in recent months had had more success in that regard.

Fourth, the rate of inflation was projected to decline from 50 percent in 1983 to 25 percent in 1984, Mr. Joyce observed. However, it was likely that the rate of inflation would increase in the short term, resulting in greater hardship for the people. The medium-term prospects for inflation depended on world market develpments, and he could only hope that they would improve.

Fifth, the restoration of the production base depended on the authorities' determination to stick with the policies that they had outlined, their willingness to make more credit available to the private sector, and their ability to restore the confidence of investors, Mr. Joyce noted. In that connection, he welcomed the World Bank's decision to hold a Donors' Conference later in 1983; his Canadian authorities hoped that they would be able to take a supportive position at that time with respect to the authorities' intentions.

Finally, he was concerned about the debt service ratio, Mr. Joyce remarked. In the past Ghana's debt service ratio had been low because the authorities had been unable to borrow. However, the debt service ratio was expected to increase sharply, reaching 43 percent in 1986. It was evident that Ghana would not be able to overcome its problems for a long time, so that the association between Ghana and the Fund was likely to be close in the coming years. The authorities would face difficulties in trying to improve the economic situation, but he was impressed by their determination to introduce measures necessary for a recovery.

Mr. Doe said that he generally endorsed the staff evaluation of the Ghanaian economy. The structural imbalances that characterized the economy during most of the 1970s appeared to have continued through the early 1980s in the form of large fiscal deficits, rapid growth in the money supply, high rates of inflation, an overvalued currency, and a weak external position. Attempts to correct the deteriorating situation in

1978/79 had been unsuccessful. Ghana's economic situation had deteriorated further as the world recession deepened, adversely affecting its terms of trade. Except for a short-lived marginal improvement in 1980, real GDP had fallen during the previous four years, particularly in 1982, when economic activity had declined by an estimated 7 percent.

The authorities, recognizing the need for adjustment, had taken decisive measures to reverse the economic decline and to establish a sound base for sustained growth, Mr. Doe observed. He commended them for their courage in tackling those difficult problems. If the authorities continued to pursue appropriate policies, rapid recovery was possible, largely because of Ghana's favorable resource base, its supply of skilled manpower, and its relatively extensive infrastructure.

The far-reaching measures introduced by the authorities--especially those in the key area of exchange rate policy--deserved the full support of the international community, particularly the Fund, the World Bank, and concessionary lenders, Mr. Doe considered. He hoped that the authorities would initiate as early as possible a medium-term plan for the Donors' Conference to be organized by the World Bank in late 1983.

On the general focus of the economic program for 1983/84, the restructuring of relative prices in favor of the productive and export sectors could provide the necessary incentive for realizing a real GDP growth of 4 percent in 1984, Mr. Doe stated. The 67 percent increase in the producer price of cocoa was appropriate, and the authorities should be encouraged to maintain a flexible pricing policy in the cocoa sector.

As to fiscal policy, the exchange rate action should assist in widening the tax base, Mr. Doe continued. The tariffs on imports had been simplified and reduced. Other revenue-raising measures, such as the increase in government fees and charges, and the restructuring of the export duty on gold exports, should also improve the revenue position. The expenditure control system already in place would help to ease the growth of spending and would contribute to the expected reduction in the budget deficit to about 3 percent of GDP in 1983 and 1984.

On the external side, he supported the authorities' intention to be flexible in exchange rate management and to work toward achieving a unified rate of exchange, Mr. Doe indicated. He also welcomed their commitment to a phased reduction of the external payments arrears by about $100 million during the program period.

He supported the authorities' request for a drawing under the compensatory financing facility, Mr. Doe remarked. The shortfall was largely attributable to low prices for exports and was therefore beyond the control of the authorities. Finally, Ghana had cooperated with the Fund in an attempt to resolve its economic and financial difficulties.

Mr. Erb commented that Ghana provided an interesting case and also an important adjustment program for the Fund. When the Fund had been criticized in the United States, Ghana had often been cited as a country that had faced internal problems and political instability because it had adopted a Fund-supported adjustment program. However, looking at Ghana's record over the previous few years, he found it was evident that failure on the part of the authorities to make the necessary changes could lead to an even greater deterioration in the economic and political situation that would occur under a Fund program.

He was in broad agreement with the staff appraisal regarding the Article IV consultation and the request for a stand-by arrangement, Mr. Erb indicated. The adjustment program adopted by the authorities was a belated but significant first step toward addressing the severe imbalances in the economy. Maximum annual access to Fund resources seemed justified, given the serious maladjustment in the payments position and the significant policy adjustments being implemented. Nevertheless, it was doubtful whether a sustainable balance of payments position would be achieved within a period of time that was consistent with the temporary character of Fund resources. Like other Directors, he was concerned about the magnitude and the length of adjustment that were required. It was therefore essential for the authorities to pursue a sustained and rigorous adjustment effort so that Ghana did not find itself with continued unsustainable financing needs in the future.

He shared the staff view that given the magnitude of the adjustment measures being implemented and recognizing the possibility of slippages, it would be difficult to set performance criteria far in advance, Mr. Erb stated. It was therefore wise to hold two comprehensive reviews, at which time policies could be reassessed in light of the circumstances and performance criteria could be set for the next period of the stand-by arrangement. Those reviews would be extremely important, and the authorities should not treat them as a pro forma exercise but as an opportunity to make necessary policy adjustments.

The authorities should be commended for their major reform of the exchange rate system, which was clearly the centerpiece of the current program, Mr. Erb went on. He was concerned that the revised system might remain unnecessarily complicated and might still leave the cedi substantially overvalued. It was therefore important that the new exchange rate system--which would be established before the next review--would include a mechanism for further adjustment of the exchange rate. The key to success in that area would be, at a minimum, strict adherence to the established schedule of depreciating the cedi and, perhaps, an acceleration in the rate of depreciation. The authorities should be flexible in managing their exchange rate in the future. The increase in producer prices for cocoa in conjunction with the exchange rate action should aid in reversing the continuous decline in Ghana's export base. The Cocoa Marketing Board (CMB) seemed to receive a disproportionate share of cocoa revenues, which would, if accrued to farmers, provide further incentives for production. Streamlining of CMB operations, perhaps in cooperation with the World Bank, should be given high priority since it could eliminate some of the inefficiencies associated with current procedures.

The decline in the fiscal deficit as a percentage of GDP between 1981 and 1983 was related primarily to the tripling of revenues in 1983, Mr. Erb noted. The restoration of the tax base through increased economic activity was appropriate, but greater attention should be paid to identifying areas where the Government could adjust expenditures in the event that revenues were not as high as expected. Expenditures were expected to increase by 50 percent in real terms in 1983; presumably, that figure was calculated after the impact of the devaluation of 35 percent. Greater attention should be given to reducing real increases in spending and not just to controlling expenditures within planned levels. Future fiscal action seemed to focus primarily on establishing new taxes, and, therefore, the Government had to be careful not to create disincentives to production through a tax system that negated the impact of price incentives.

It was difficult to understand why price controls were being phased out rather than eliminated, because by eliminating them the administrative cost would be reduced, thereby aiding in fiscal adjustment, Mr. Erb said. Prompt elimination of the subsidy on petroleum would also be appropriate.

Fiscal policy, which had determined the rate of monetary growth in Ghana in the past, would continue to be important in the future, Mr. Erb remarked. He was concerned that fiscal deficits could be much higher than expected, which would have detrimental implications on the monetary side. The authorities should give more attention to traditional monetary rules rather than relying on extraordinary measures such as the stabilization operations that had been used in the past. On a related point, the negative domestic savings rate that had emerged in 1983 was discouraging, and an increase in interest rates--which had been halved in 1982--should not be delayed. In the short run a realistic structure of interest rates could halt the apparent capital flight, which was reflected in a consistently large errors and omissions item in the balance of payments.

On the external side, prospects for financing the balance of payments in 1983 were not good, Mr. Erb observed. A 600 percent increase in private capital inflows to a level of $192 million was projected--an amount equal to more than one third of the current account deficit. In view of the government control of the import program and the expected lags in payments, reductions in import levels could be expected should financing not materialize in the short run, thus increasing the possibility of an unfinanced balance of payments gap that could approach $150 million in 1983. The import program needed to be closely monitored.

The medium-term outlook for the balance of payments was also a source of major concern, Mr. Erb commented. The current account deficit--projected to be 10 percent of GDP in 1983 and 1984, declining to only 8 percent of GDP in 1987--was not likely to be sustainable, particularly as more than two thirds of the financing was based on projected government borrowing, which included possible Fund support. The staff had referred to the authorities' objectives of pursuing a prudent external debt management policy and of improving their debt monitoring arrangements so as to contain the future debt burden. At the first interim review, the financing requirements of the Ghanaian adjustment effort should be thoroughly examined. He was particularly concerned about the projected deterioration in the debt service ratio from less than 11 percent in 1982 to almost 50 percent in 1987. Fund charges and repurchases alone would account for one fifth of the projected 1987 debt service. In the circumstances, continued medium-term borrowing on nonconcessional terms--including the $400 million that would be allowed in 1983--would not be prudent; therefore, further adjustments in the current account might be necessary.

With respect to the request for a drawing under the compensatory financing facility, he had problems with the magnitude of the Fund support because part of the shortfall was attributable to factors within the control of the authorities, Mr. Erb stated. Most of the shortfall could be accounted for by changes in unit value rather than volume and could therefore be regarded as largely beyond the control of the authorities. Nevertheless, there were also volume shortfalls--in particular, of gold and wood--that seemed to be largely the result of the pursuit of inappropriate policies. He, therefore, did not support full compensation of the shortfall. If part of that shortfall had been due to the accumulation of stocks--which was within the authorities' control--the staff would have reduced the amount to be compensated. While he realized that it was technically easier to calculate the proportion of the shortfall due to stockpiling than to calculate the proportion due to the pursuit of ill advised policies, it was important for the staff to make such a calculation so that compensation did not take place in cases where government policies had exacerbated the shortfall. However, he could support the proposed decision with respect to the compensatory financing facility.

Mr. de Vries said that it was regrettable that more than three years had elapsed since the previous Article IV consultation with Ghana. It was true that the situation had been difficult during the interim period, but that should have been a reason to hold a consultation. Major distortions had developed in the economy during the previous three years. As a result, total production had declined sharply, and even smuggling had been unable to maintain the level of production. Metal production--even of gold, with its high increase in price and its easy marketability--had also declined steadily. Furthermore, the food supply had diminished and the problem had been worsened with the repatriation of many Ghanaians.

The Government had tried to combat high inflation by introducing price controls; hence, prices had become stable, but production and trade had shifted to the black market and was no longer taxed, Mr. de Vries commented. As a result of the reduction in tax revenues and the short supply of foreign exchange, imports of necessary raw materials and spare parts had had to be reduced. As Mr. Erb had said, it was clear that lack of adjustment could lead to great hardships and political instability.

Fortunately, the authorities had begun to take major adjustment action, Mr. de Vries remarked. The adjustment efforts were centered around the exchange rate. Exchange rate policy in Ghana had a strange history. In 1972, the authorities had devalued the cedi to about one third of its previous value, but it had been appreciated again after the President had been imprisoned. Between 1972 and 1978, a flexible exchange rate had been adopted; as a result, the currency had depreciated to 42 percent of its previous value and had remained at about that level until recently. It was vitally important that the new adjustment effort should be effective, and he agreed with Mr. Erb that some mechanism--perhaps incorporated into one of the early reviews--should be introduced to ensure continued flexibility in exchange rate management.

The authorities had made courageous efforts to introduce an adjustment program, Mr. de Vries agreed. Apparently, the present program was not fully supported by the population in general, and there was still a great deal of opposition from certain groups that would no longer be able to gain from the economic distortions.

Previous speakers had drawn attention to some of the major areas where adjustment was needed, Mr. de Vries noted. Given the drastic action that was necessary, it would be difficult to predict the outcome, and he agreed with the staff that it was beneficial to have two major reviews during the period of the stand-by arrangement. Those reviews would have to deal with four major areas. First, budgetary policy and the effect of decisions taken by the Cocoa Board would need to be considered. He hoped that more concrete projections concerning the budget position would be possible in the future. Second, the authorities' monetary policy would need to be monitored. Interest rates had moved in the wrong direction, so that they continued to be negative in real terms. Third, the balance of payments projections and financing requirements would need to be reviewed. Finally, the staff should ensure that the authorities were managing the exchange rate flexibly.

The balance of payments projections indicated that the deficit would remain more or less constant, reflecting the hope that the new program would make available additional funds for development, Mr. de Vries remarked. The financing projections were rather vague at present, but as the situation became clearer perhaps they could be based on firm statistics. He hoped that the outcome of the Donors' Conference, to be held later in 1983, would be positive. Were there any plans for combining the program review with the Donors' Conference?

He could approve the request for a drawing under the compensatory financing facility, Mr. de Vries said, although he did have some doubts. First, the price of cocoa had been falling, but the staff had projected that it would rise slightly in the future. The cocoa buffer stock--of which the Fund had not approved--had influenced price developments, and prices had apparently stabilized at too high a level; the authorities were therefore partly responsible for the export shortfall.

Second, the method used by the staff to project gold prices was different and more favorable to Ghana than the methods that had been used in the case of the major gold producer, South Africa, Mr. de Vries observed. Could the staff comment on that situation? In conclusion, in difficult circumstances the authorities had undertaken important adjustment action. He hoped that they would succeed in introducing their measures, which would clearly benefit the country as a whole.

Mr. Chatah stated that over the previous decade Ghana had experienced a high rate of inflation, large external imbalances, and sluggish and often negative economic growth. The general deterioration had been due, at least in part, to the large fiscal deficits, the rapid expansion in liquidity, and the unrealistic exchange rate. Price controls, which had been intended to slow down inflation, had been largely unsuccessful, had created distortions, and had further impaired the export sector. The difficult situation had been made much worse by droughts, worldwide recession, and a sudden reflux of Ghanaians from abroad in the early part of 1983. In spite of that rather bleak picture, there were reasons to believe that a fairly rapid turnaround in the economy could still be achieved.

The country was favorably endowed with natural resources, and it had a relatively developed infrastructure and skilled manpower, Mr. Chatah noted. The authorities intended to implement a strong and comprehensive adjustment program. They would have to lay the basis for sustained growth, particularly in the export sectors, while at the same time reducing liquidity expansion in order to ease the underlying inflationary pressures. In view of the comprehensive nature of the adjustment efforts and the staff's projections that the economy would recover, he supported Ghana's request for a stand-by arrangement. It was also clear from the staff analysis that the request for a purchase under the compensatory financing facility met all of the requirements, and he supported the proposed decision.

Mr. Wicks stated that he could generally endorse the staff appraisal and supported the proposed decision. Ghana's severe need for adjustment justified the maximum use of Fund resources allowable under present policies. The success of the adjustment program could have implications for other countries in Africa, and the Executive Board's discussion was therefore particularly important.

Despite Ghana's distressing economic decline in recent years, it was a fortunate country compared with many because of its rich mineral endowments, its long-established agricultural sector, and its relatively advanced infrastructure, Mr. Wicks considered. Part of the recent decline had undoubtedly been due to the external environment, the sustained decline in world prices for Ghana's exports, and the return of one million compatriots. However, inadequate economic policies had been partly responsible for the decline. The courageous measures recently introduced by the Government were commendable, particularly with respect to the exchange rate and pricing policies, and the authorities' commitment to maintaining adjustment measures into the medium term was welcome.

to a Fund-supported program. Since that time, the fundamental imbalances had grown larger, economic activity had diminished further, and the foundations of the economy had weakened, primarily as a result of inappropriate domestic policies.

The adjustment process would undoubtedly be an arduous one, but the key to reviving economic activity clearly rested with the exchange rate and pricing policies, which would, among other things, bring about the restoration of incentives, Mr. Fridriksson considered. The exchange rate policy adopted by the authorities involved radical changes, and it would be interesting to follow developments over the period of the arrangement and beyond to see how strongly and quickly production and exports responded to the increased incentives. If the adjustment policy were pursued as intended and the projected recovery materialized, he would agree with Mr. Mtei and Mr. Wicks that Ghana might provide an example from which others could benefit. Ghana's rich resource endowment should allow for a rapid recovery of domestic production and exports, but the durability of the recovery would be determined by the perseverance of the authorities.

The size of the adjustment program was fully justified by the severity of the situation, as well as by the potential for a quick recovery, Mr. Fridriksson said. He shared the staff view with respect to a purchase under the compensatory financing facility. Ghana's export sector was beset with problems of unusual magnitude, but the request met all the requirements set forth in the Articles of Agreement and in the compensatory financing facility decision.

Mr. Suraisry remarked that Ghana's economy had suffered in recent years owing to external developments and continued postponement of decisive adjustment action. In April 1983, the authorities had adopted a courageous and comprehensive adjustment program, and he supported their request for a stand-by arrangement. The substantial restructuring of relative prices in favor of the productive sector was a key element and was long overdue. The increase in the level of imports, which would be made possible by Fund support, was also necessary to increase the pace of economic activity.

As to fiscal policy, the authorities were to be commended for their efforts to strengthen the revenue base, which had been seriously eroded in recent years, Mr. Suraisry considered. The substantial improvement in budget revenues in 1983 was expected to come mainly from a sharp increase in import duties resulting from much larger imports. Considering the temporary nature of such an increase, it might be necessary to consider a more fundamental reform of the tax system in the future. The 1983 budget allowed for a lower overall budget deficit than in 1982. With respect to domestic financing of the budget, he was not clear what the item "other" referred to in Table 3, page 11 of EBS/83/140. If that item referred to an accumulation of domestic arrears, the reduction of those arrears might present budget problems in later years, which could complicate the implementation of the program. Could the staff comment on that matter?

Although noting the Donors' Conference sponsored by the World Bank, he hoped that the Ghanaian authorities were considering encouraging direct investment in Ghana, Mr. Wicks said. Ghana was fortunate in having rich natural resources, and he wondered whether there might be more scope for investment in that area.

With respect to the exchange system, given the authorities' concern over the political implications of an outright devaluation, he accepted as an interim measure the introduction of policies that constituted a multiple exchange practice, Mr. Wicks commented. The introduction of such an exchange system amounted to an effective and major devaluation, but the challenge of administering such a system was quite daunting; he therefore welcomed the authorities' intention to depreciate the two exchange rates quarterly in order to maintain competitiveness.

On the external side, Mr. Wicks stated, a prerequisite for economic recovery would be an increase of imported inputs for the import-competing and export sectors. The adjustment obviously relied on substantial capital flows, but the staff paper had not provided enough detail about the precise sources of such inflows. He wondered about the difference between debt and nondebt-creating flows. Had the staff had any indication of the commercial banks' attitudes toward lending to Ghana? How sure was the staff that the private medium-term capital--estimated at $192 million--would be forthcoming? The staff seemed to imply that the volume of imports would be cut if capital inflows failed to materialize as envisaged. Could the staff comment on what effect a cut in imports would have on the program? The authorities' intention to reduce the payments arrears by $100 million during the life of the program was welcome. The debt service ratio was comparatively low at present but was expected to rise in 1984 and to stay above 30 percent for the rest of the decade. Clearly, cautious debt management policies were essential.

With respect to the request for a purchase under the compensatory financing facility, Ghana met the test of cooperation and had a balance of payments need, Mr. Wicks said. The shortfall in 1982 had been largely attributable to the fall in world prices of cocoa. However, inappropriate economic policies--in particular, the overvaluation of the exchange rate--had contributed to the decline in export prices. He shared the staff view that the shortfall would be temporary, given the expected recovery in world prices, but the sharp increase in cocoa prices forecast for 1984 was was optimistic. In conclusion, although the Ghanaian economy was faced with great problems, the Government had shown its intention to deal with them with courage. Important decisions had already been taken by the authorities, but a great deal of determination would be needed to maintain their policies over several years.

Mr. Fridriksson welcomed the long-overdue consultation with Ghana, as well as the courageous measures that the authorities had taken to reverse the tragic developments in the economy during recent years. Discussions had taken place between the Fund staff and the authorities in 1980 and 1981, but it was regrettable that those discussions had not led to a Fund-supported program. Since that time, the fundamental imbalances had grown larger, economic activity had diminished further, and the foundations of the economy had weakened, primarily as a result of inappropriate domestic policies.

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The authorities had taken a major step toward substantially devaluing the exchange rate, Mr. Suraisry observed. He could understand their reasons for introducing a multiple exchange rate system based on bonuses and surcharges; however, that system was complex and inefficient, and he welcomed their commitment to simplify it starting on October 1, 1983. Their intention to implement a flexible exchange rate policy and to unify the exchange system by the end of the program period was also welcome. The staff paper mentioned that the Bank of Ghana would monitor the exchange rate system closely so that it should not incur losses from exchange transactions. The short-term implications of the system for the profits and losses of the Bank of Ghana were unclear. Could the staff explain why the budget did not appear to be directly affected by the exchange rate system?

The adjustment program included two reviews, but no performance criteria had been established beyond August 1983, which was inevitable given the uncertain results of the various adjustment measures, Mr. Suraisry noted. In view of the size of the imbalances in the economy, there was clearly no room for slippages, and, if unforeseen adverse developments occurred, the authorities should be prepared to take necessary adjustment action. In conclusion, he supported the proposed decisions and welcomed the authorities' intention to seek further Fund support in the medium term; however, successful implementation of the current program was of paramount importance.

Mr. Prowse stated that Ghana provided a most interesting case for the Fund. While it was helpful to stress the potentially rich resources of the country, the important objective was to activate and utilize those resources. Like others, he regretted that the Fund program with Ghana was so long overdue. The extent and rigor of the adjustment program would not have been so great had Ghana approached the Fund earlier.

He realized that there was some uncertainties with respect to many aspects of the program, Mr. Prowse remarked. He was particularly impressed by the courage of the authorities in implementing major adjustment measures prior to completion of negotiations with the Fund on the stand-by arrangement. The request for maximum access was therefore justified.

He had a number of points to make or questions to raise on domestic policy, Mr. Prowse indicated. First, the importance of reducing the subsidy on petroleum--which still represented about 50 percent of the world market price--during the course of the program should be emphasized to the authorities. Second, how did the financial measures taken in early 1982--including the requirement that all payments of ₵ 1,000 and above be made by check and the freezing and vetting of all deposit accounts exceeding ₵ 50,000--affect the long-term development of the financial system? Third, could the staff explain how the reduction in the salary differentials was to be achieved?

On the external side, the exchange rate adjustment and its future management was a key part of the program, as it would have an important effect on domestic production and export income, and on the use made of the country's substantial natural resources, Mr. Prowse said. Could the projected inflow of capital be achieved? He noted that a great deal of the balance of payments financing relied on public sector borrowing. Should there not be more conscious efforts to attract private equity investment, perhaps in the natural resources area? The volume of borrowing was extremely large relative to exports, and the debt service ratio would rise significantly in the future. Although the projected increase in the debt service ratio was perhaps excessive, he did not want to recommend that the authorities should rely less on external borrowing, because, without those inflows, prospects for economic growth were slim.

Savings were essential to the restoration of the productive sector, and yet domestic savings in aggregate were projected to be negative, Mr. Prowse noted. Could the staff indicate what prospects there were for increased private savings? Did the financial structure encourage savings, or was further adjustment of interest rates necessary? The costs of borrowing would accumulate, and it was therefore essential that any capital inflows, which were not free of cost, should be applied productively. Otherwise, the problems existing at the end of the decade might be even more severe than the present ones.

He was concerned about the capacity of the Government to deal with the administration of the complex exchange and price arrangements, Mr. Prowse concluded. It was in view of those uncertainties that he welcomed the proposed reviews under the program, and he also noted Mr. Salehkhou's reassurance that the authorities were willing to take supplementary measures should the need arise. What sort of measures did the staff or Mr. Salehkhou envisage if the external projections were not achieved; for example, if access to external borrowing were lower than expected or exports did not increase as projected? Finally, he supported the staff decision with respect to the request for a drawing under the compensatory financing facility.

Mr. Malhotra indicated his support for the proposed decisions. The authorities, confronted with a serious economic situation, had decided to implement a strong adjustment program. They had already taken drastic measures with regard to the exchange rate and were intending to maintain a flexible exchange rate over the coming months, with the aim of simplification and eventual unification of the exchange system by the end of the program period. The authorities had demonstrated great courage in implementing those measures, given the political situation.

As to fiscal policy, important measures had already been introduced, and the fiscal deficit would be reduced from about 4.6 percent of GDP to 3.5 percent of GDP during 1983, Mr. Malhotra observed. The authorities hoped to restore the revenue base, which had been greatly eroded in the past. They anticipated a large increase in tax revenues, but since that increase was based on import taxes there could be some difficulties in realizing the targets. Decisive action had been taken on the pricing front, especially with respect to prices of public sector enterprises and utilities. Price adjustments of between 100 percent and 300 percent had resulted in the elimination of budget deficits, except with respect to petroleum products. Incentives aimed at increasing production and exports had been provided through higher producer prices and the devaluation of the exchange rate.

On the monetary side, a cautious but flexible approach was necessary, since the impact of the exchange rate action and the pricing policies could not be fully anticipated at present, Mr. Malhotra considered. The staff had demonstrated flexibility in planning to establish performance criteria at the time of reviews of the adjustment program.

More generally, it was clear that implementing such drastic measures over a short period would create tensions and difficulties for the authorities, Mr. Malhotra said. It was the role of the Fund to encourage the authorities to persevere and also to provide them with the resources necessary to rectify the large imbalances that had materialized. The staff had noted that the current account deficit would be large for some time, in part because it was necessary to strengthen the supply side of the economy through increased imports. He was concerned that the debt service ratio was expected to quadruple. Could the staff indicate how the borrowed capital would be invested? Would that capital be directed toward the export sector, so that the debt servicing capacity of Ghana could be improved? He hoped that the Donors' Conference organized by the World Bank would be successful and that concessional flows to Ghana could be improved, thereby reducing the need for high-cost borrowing.

The authorities were right in adopting a cautious interest rate policy, Mr. Malhotra remarked. While positive interest rates would encourage domestic savings, it was evident that, at least in the short term, the potential for a substantial increase in financial savings was limited. Furthermore, the authorities hoped to reduce inflation from 50 percent to 25 percent. In Ghana's case, the interest rates should not follow current rates of inflation but should be geared to the planned rates of price increase.

With respect to the request for a drawing under the compensatory financing facility, the export shortfall was largely beyond the control of the authorities, Mr. Malhotra said. The entire shortfall should therefore be compensable.

Mr. Caranicas remarked that Ghana provided a classic example of a non-oil developing country that had needed financial assistance but had approached the Fund only after a long delay. A number of speakers had expressed doubts about the implementation of the adjustment program, allegedly because of the lack of political consensus in the country. It was difficult in a country such as Ghana to determine the extent of popular support. The authorities had already introduced a number of harsh measures, which seemed to have been accepted by the population at large.

The exchange rate had been overvalued for many years and had been the principle obstacle to economic growth in the past, Mr. Caranicas considered. From a political viewpoint, it had been extremely difficult for the authorities to reform the exchange system; such action represented a heroic effort by the Government, and he had no doubt about the administrative capacity to implement the adjustment measures.

The authorities deserved the full support of the Fund because they had demonstrated their commitment to implement the extensive adjustment program, Mr. Caranicas commented. He therefore supported the request for drawings under the stand-by arrangement and the compensatory financing facility. Could the staff explain why it considered the export shortfall to be largely beyond the control of the authorities? What was the status of the International Cocoa Agreement, and what was its effect on the export shortfall of cocoa?

Mr. Delgadillo indicated his agreement with the staff appraisal and his support for the proposed decisions. After many years of economic decline in Ghana, the authorities had introduced adjustment measures to cope with the situation. The objectives of the program, if accomplished within the estimated adjustment period, would provide the base for sustained recovery in the future. The courageous measures already implemented, particularly with respect to the exchange rate policy, needed to be closely monitored. Furthermore, a flexible approach with respect to the interest rate and pricing policies was necessary.

Mr. Panday stated that he agreed with the thrust of the staff appraisal. The Ghanaian economy had suffered from various imbalances as a result of inappropriate policies followed by the authorities in the past. Courageous measures had been introduced to correct the economic imbalances, and he therefore supported the proposed decisions.

The staff representative from the African Department noted that Ghana would be discussed again by the Executive Board before the end of October 1983. With respect to the exchange rate policy, it was true that the new system appeared complex since the bonuses and surcharges were being applied through the banks. There was a firm timetable for simplifying the system and, eventually, unifying the exchange rate. In their letter of intent, the authorities had committed themselves to transforming the bonuses and surcharges into straightforward dual rates by October 1, 1983. Furthermore, they intended to unify the exchange rate by the end of the period of the stand-by arrangement. They had also committed themselves to adjusting the exchange rates for inflation differentials between Ghana and a group of countries on a quarterly basis. The staff attached considerable importance to the timetable outlined by the authorities.

Both the domestic price and the exchange rate policies would be managed flexibly, the staff representative considered. It was understandable that in current circumstances, particularly with respect to the tremendous food shortages, the authorities had wished to maintain certain safeguards and had not yet formally abolished the system of price controls.

The interest rate policy was an important issue, the staff representative stated, and should be seen as part of an overall flexible pricing policy. It would have been difficult for the authorities to maintain a positive interest rate over the previous three years, but it was an important issue for the future and would be dealt with in the scheduled program reviews. The link between capital outflows and the interest rate was not direct, as some Directors had implied; there were many factors that had led to capital flight in the past.

The authorities had clearly indicated in their letter of intent that they would eventually eliminate the petroleum subsidy, the staff representative remarked. The price of petroleum would be raised in October 1983 and again in January 1984, thereby eliminating the subsidy under the budget. However, until the exchange rates were unified, there would be a need for further price adjustment once the subsidy had been eliminated from the budget because petroleum was coming in at the less depreciated exchange rate. By the end of the period of the stand-by arrangement, domestic petroleum prices should reflect the world market price, and any changes thereafter would reflect changes in Ghana's unified exchange rate.

The staff was also concerned about the forecast of fiscal performance, as it was directly linked with the capital inflows, the staff representative explained. Estimates regarding public capital inflows were probably fairly realistic; a number of capital inflows had already been approved, and others were in the pipeline. The forecast of private capital inflows was based on discussions that the authorities had had with various sources regarding credit totaling about $340 million, of which $200 million was expected to be used in 1983. That financing was made up largely of supplier credits to the mining sector, timber sector, and agricultural sector. Given the profitability of gold and timber exports after the exchange rate action, both figures were at least plausible. Nevertheless, there was a degree of uncertainty concerning the timing of private capital inflows; if they were not forthcoming in 1983, some of the imports included in the staff projections would not take place. Consequently, there could be an impact on the balance of payments. However, he was more concerned about the fairly immediate impact of a reduction of imports on revenues and receipts. If that situation were to arise, action would be necessary on three fronts.

First, the level of expenditure would need to be adjusted, although the room for adjustment was not large, the staff representative went on. Second, on the revenue side there were certain measures--particularly with respect to sales and excise taxes--that could be introduced if necessary. Furthermore, there was some flexibility in the tax revenue forecast; for instance, tariff receipts from imports covered by special licenses had not been included. In addition, the revenue forecast had not included any resources accruing in connection with the World Bank reconstruction import credit. Third, there was also the possibility that the authorities could increase borrowing from the banking system. The adjustment program was extremely tight, particularly with regard to bank financing for the second half of 1983, and, in view of those uncertainties, that the staff had formulated the performance criteria on credit only for August 1983. The ceilings for October and December 1983 would be set during the first review mission.

The inclusion of Tables 8 and 9 in EBS/83/140 were an attempt by the staff to prompt discussion, the staff representative indicated. The figures in those tables did not necessarily reflect the authorities' policies, but were an attempt by the staff to present a scenario and to highlight certain problems that were likely to arise. The projections for the years after 1984 had not been discussed in any great detail with the authorities. The staff had been cautious in projecting capital inflows and in forecasting the consequent impact on the debt service ratio. Perhaps the projections included in the tables would be helpful to donors at the conference later in 1983. The World Bank and the authorities were already actively working on preparations for the conference, although its precise date was still unknown.

There was certainly room for direct investment in Ghana, the staff representative considered. It was the authorities' intention to attract such investment, especially in the timber and gold sectors, and to be flexible and realistic on such matters as the transfer of profits.

The program was getting off to a somewhat slower start than the staff had hoped at the beginning of the year, partly because of the problems associated with the influx of a million Ghanaians and with the drought, the staff representative stated.

With respect to the stopgap monetary measures introduced by the authorities in 1982, the demonetized 50-cedi notes had not been exchanged for notes of smaller denominations at the time that they had been withdrawn, the staff representative remarked. In the meantime, however, the Government had decided to reimburse all the holders of 50-cedi notes. Individuals who were owed ¢ 500 or less would be reimbursed during fiscal year 1983. The amount to be reimbursed had been included in the budget, and repayment had already begun. Those individuals who were owed more than ¢ 500 were being repaid over five or six years in the form of stock. Deposits in excess of ¢ 50,000 were being frozen while the authorities tested for fraud and tax liabilities; however, those accounts would be unlocked after they had been vetted. The requirement that all payments be made by check had never been enforced, with the exception of payments in the cocoa sector. Cocoa farmers were still being paid by check, an amendment that was seen by cocoa farmers as an improvement over the previous practice.

The authorities recognized the need to streamline the operations and reduce the costs of the Cocoa Marketing Board, the staff representative noted. Their efforts would be monitored closely by the World Bank. A committee under the chairmanship of Ghana's Coordinating Secretary--a position similar to that of a Prime Minister--was reviewing operations in the cocoa sector. Some of the World Bank disbursements under the forthcoming export rehabilitation credit would be linked to institutional improvements in the Cocoa Marketing Board as well as in the timber sector. Furthermore, the authorities had assured the World Bank and the Fund that cocoa producer prices would be reviewed annually to ensure that there would be no future erosion in real terms.

Some commercial banks had provided bridge financing even before the letter of intent for the Fund stand-by arrangement had been agreed upon, the staff representative indicated. He expected that other banks would be more courageous and forthcoming in the future, particularly with regard to the trade financing but also with regard to financing of projects if the adjustment program were successful.

The item "Other" in Table 3 of EBS/83/140 included the stock equivalent of the 50-cedi notes withdrawn in 1982, the staff representative said. Financing by secondary banks--those that were not consolidated in the monetary survey, but which held some government paper--were also included. In the past, commercial banks had refused to accept deposits above ¢ 10,000, so that some individuals and enterprises had invested in government paper, which was also included in the item "Other."

It was unlikely that under the new exchange system the Central Bank would incur losses, the staff representative considered. However, if losses were to arise, there was a firm understanding between the authorities and the staff that they would be reflected in the government accounts and in the budget shortly after the calendar year, and that they would be included in the performance criteria--i.e., credit ceilings--of the stand-by arrangement.

The wage differential would be reduced from both ends, the staff representative from the African Department explained. Individuals with salaries at the low end of the range would receive increases greatly above the average, and individuals with high salaries would get increases that were greatly below the average. Finally, there was limited scope for an increase in personal savings in the short term; it was nevertheless important to introduce a realistic interest rate policy.

The Executive Directors agreed to continue their discussion in the afternoon.

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/83/116 (8/1/83) and EBM/83/117 (8/3/83).

2. 1975 OIL FACILITY SUBSIDY ACCOUNT - EXPERIENCE

1. Subsidy payments shall be made to the beneficiaries listed in Table 1 of EBS/83/94, Supplement 3, on the Fund's holdings of each member's currency subject to charges that were outstanding under the 1975 oil facility and eligible for subsidy for the period May 1, 1975 to May 11, 1983 at a rate (approximately 0.32 percent) that will fully utilize the remaining resources of the account.

2. These payments shall be made in U.S. dollars as soon as practicable after all charges due at the end of July 1983 in connection with the oil facility have been paid.

3. No charge shall be levied for the services rendered by the Fund in the administration, operation, and termination of the account.

4. After disbursement of subsidy payments under paragraph 2 above, the subsidy account shall be considered terminated.

Decision No. 7484-(83/117), adopted
August 2, 1983

3. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors as set forth in EBAP/83/198 (7/29/83) and by an Advisor to an Executive Director as set forth in EBAP/83/202 (8/1/83) is approved.

APPROVED: February 14, 1984

JOSEPH W. LANG, JR.
Acting Secretary