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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 83/119

10:00 a.m., August 5, 1983

W. B. Dale, Acting Chairman

Executive Directors	Alternate Executive Directors
A. Alfidja	
J. de Groote	
	P. D. Péroz, Temporary
	C. A. Salinas, Temporary
R. D. Erb	
	M. Z. M. Qureshi, Temporary
	H. Kobayashi, Temporary
	Jaafar A.
	M. Casey
	H. Arias, Temporary
	G. Grosche
	C. P. Caranicas
	A. S. Jayawardena
	J. E. Suraisry
	T. de Vries
	R. Bernardo, Temporary
	H. Alaoui-Abdallaoui, Temporary
F. Sangare	E. I. M. Mtei
M. A. Senior	
	A. K. Juusela, Temporary
	J. Bulloch, Temporary
	Wang E.

J. W. Lang, Jr., Acting Secretary
R. S. Laurent, Assistant

Also Present

African Department: A. B. Diao, A. Doize, C. Enweze, T. P. McLoughlin. Exchange and Trade Relations Department: A. Abisourour, S. Kanesa-Thasan, F. L. Osunsade. Fiscal Affairs Department: R. R. Schneider. Legal Department: Ph. Lachman. Research Department: E. C. Meldau-Womack. Secretary's Department: A. Wright, Deputy Secretary. Advisors to Executive Directors: S. M. Hassan, Y. Okubo. Assistants to Executive Directors: L. Barbone, M. Camara, M. B. Chatah, M. K. Diallo, W. Moerke, J. A. K. Munthali, V. K. S. Nair, G. W. K. Pickering, E. Portas, J. C. Williams.

1. GUINEA - 1983 ARTICLE IV CONSULTATION

The Executive Directors considered the staff report for the 1983 Article IV consultation with Guinea (EBS/83/148, 7/19/83; and Cor. 1, 8/3/83). They also had before them a report on recent economic developments in Guinea (SM/83/167, 8/1/83; and Cor. 1, 8/3/83).

Mr. Sangare made the following statement:

I should like to express the appreciation of my Guinean authorities for the frank manner in which the staff conducted the discussions at Conakry last April for the Article IV consultation and to review the performance under the stabilization program for which a stand-by arrangement was approved in December 1982. My authorities are in broad agreement with the thrust of the staff report, which has identified many of the issues crucial to the formulation of the Government's overall economic strategy. They attach great importance to their continuing dialogue with the Fund, as it provides an avenue for a careful examination of their policies in the pursuit of economic development. Thus, despite the difficulties experienced in implementing the stand-by arrangement, my authorities have benefited from the exchange of views with the staff.

The staff report has underlined the principal factors shaping recent economic developments in Guinea, namely, the declared policy of economic liberalization of the authorities, which has increased the scope for market-oriented activities, and the continued difficult conditions in the world economy. As regards the former, it is important to note that the move toward a mixed economy comes after more than a decade of adherence to a highly centralized system of economic management, making the process of adjustment even more difficult.

The economic and financial imbalances that have emerged in Guinea in recent years continue to command the attention of my authorities, as evidenced by the efforts being made to revive economic growth and strengthen the financial position of the public sector. In this connection, the authorities believe that, owing to the structural nature of the problems that they face, policy actions must not only be geared toward finding short-term solutions for the immediate future but also address issues relating to the longer-term transformation of the economy. It is in this regard that there is some difference of view between the Guinean authorities and the staff as to the speed of action and the reliability of alternative instruments of adjustment.

In the agricultural sector, for example, while my authorities agree with the staff that the inadequacy of producer prices cannot be ignored, they believe that other factors have been equally, if not more, important in contributing to the overall weakness of the sector, despite increases in acreage under cultivation. In this regard, three factors, sometimes occurring concurrently, have adversely affected production. These are intermittent drought, and sometimes heavy rainfall which led to extensive flooding; lack of physical infrastructure such as feeder roads and irrigation facilities, which continues to impose a major constraint; and, last but not least, the inadequacy and at times unavailability of inputs such as fertilizer and spare parts for machinery, resulting from shortages of foreign currency. The authorities feel that, in the face of these constraints--which, in part, are beyond their control--it is unlikely that price increases alone could do much to improve agricultural performance.

In the industrial sector, the decline in value-added in recent years has also reflected the lack of imported inputs and spare parts. However, the closing of a number of state enterprises resulting from the Government's liberalization policy has temporarily depressed activity in this sector. In this connection, it is apt to point out that industrial output may take time to yield desired results.

My authorities believe that the move toward liberalization of the economy with an increase in private activities would, over time, provide an impetus to economic growth. To this end, farmers have been given the option of selling their produce to official procurement centers at administered prices or in the free market, where inputs can also be obtained. In the industrial sector, state enterprises have been given autonomy, which allows them to take timely decisions affecting employment and prices. Many inefficient entities have been closed down while others have been turned over to the private sector. In the meantime, the free market in goods and services has been revived, and the private sector can now engage in import and export activities.

However, the promotion of a more liberal economic system has not been without pitfalls, as new problems and realities have been brought to the fore. My authorities have acknowledged that an appropriate institutional framework is lacking, and strains on the Government's administrative resources have intensified. The staff report indicates that, although private sector operations are becoming substantial, they have not been comprehensively recorded in the national accounts. The authorities recognize the need to improve their statistical coverage of economic activity and to develop their administrative capacity to extract tax revenue from an expanding private sector in view of the loss in revenue resulting from the closing of several public sector enterprises.

Directors will recall that the initiatives toward gradual liberalization of the economy beginning in 1979 set the stage for an adjustment that was to be supported by the stand-by arrangement. Directors felt that the authorities had made commendable progress by putting in place a reasonable package of measures that could rekindle growth. The financial program was unfortunately frustrated by certain transitional difficulties associated with the changing system, and aggravated by an adverse external environment that was characterized by weak demand for Guinea's exports. As a consequence, the program went off track. Nevertheless, the authorities were successful in meeting some of the quantitative targets, including domestic credit and the sub-ceiling on borrowing by the Government from the banking system.

Prospects for the near term are still worrisome, as the external payments situation is expected to remain tight. The authorities are keenly aware of the financial imbalances and the need for a revival of economic growth, including accelerated development of the country's richly endowed agricultural and mineral sectors. They are undertaking internal consultations with a view to determining how the objectives of the adjustment program could best be achieved. Meanwhile, efforts have been made to strengthen the planning process by establishing a central office for project appraisal within the Office of the President, which should help to improve the use of external aid.

With regard to agriculture, a decision has been taken to gradually eliminate government involvement in the FAPA program with a view to developing self-supporting production units. Producer prices of a wide range of agricultural products were raised early in 1982 and again in 1983.

A ministry has been established to oversee the promotion of small and medium-scale enterprises in the private sector. A Chamber of Commerce is also being established to assist in promoting these activities.

In the fiscal sector, the authorities intend to consolidate the gains made in revenue in 1982, which reflected increased tax efforts. For the 1983 budget, the authorities intend to reduce the overall deficit to GS 0.453 billion compared with a deficit of GS 4.074 billion in 1982. They are hopeful that with the curtailment of transfers to state enterprises by about a third of the 1982 amount, the fiscal targets should be achieved. It is to be noted that part of the substantial outlays to state enterprises in 1982 were to cover the cost of plant rehabilitation undertaken with assistance from the World Bank and other donors, and to retire the debts of certain public enterprises that were liquidated in keeping with the government policy of liberalization. The retirement of the debts by the Central Government was unavoidable because, in compliance with procedures in the centrally planned economy, no public enterprise in Guinea had been permitted to retain financial reserves on an individual basis. Instead, all public enterprises were required by law to transfer all their tax surpluses to the Government. In turn, the Government had to meet their costs of amortization, rehabilitation, and any losses that should have otherwise been covered by the normal financial reserves. Thus, the Guinean authorities feel that these transfers should not be interpreted as mere subsidies. However, it is conceivable that such centralization of financial resources of public enterprises could prevent ailing enterprises from making the necessary effort to improve their operations. The Guinean authorities recognize this problem; they have consequently decided to discontinue the practice and have granted greater autonomy to individual enterprises. As noted by the staff, these transfers were, in part, to regularize the previous year's expenditure. As such, the authorities feel that they are exceptional and should not recur.

Developments in the monetary sector continue to reflect the operations of the Central Government as well as those of the parastatals. However, efforts aimed at rationalizing these state enterprises should ease the need for domestic bank financing of the budget deficit. With regard to credit policy, it may be noted that lags have been experienced in extending credit to the growing private sector. However, further efforts are being made in this regard, and, to this end, authority has already been given for private participation in the banking sector. The authorities accept the principle of a regular review of interest rates. However, they feel that further adjustments should be considered in light of the need to revive private sector activity. They also believe that more reliance should be placed on expanding banking facilities in the rural areas.

There remains a lack of understanding on measures to be taken on the exchange rate. The Guinean authorities feel that one of the problems that has to be considered is the impact of an exchange rate change on the cost of living. Although there have been sharp price increases over the past three to four years, as reported by the staff, the Guinean authorities have firmly stood their ground in resisting pressure to grant across-the-board increases in public sector wages. Real wages in the public sector have declined considerably. I am sure that Directors will appreciate the position of the Guinean authorities that it would be practically impossible to implement the Fund's recommendations on exchange rate without upward adjustments in wages and salaries. Nevertheless, the authorities are continuing to reflect on the matter. They also expect to make further progress in opening up the exchange and trade system. Finally, my authorities have taken note of the need for an orderly reduction and eventual elimination of external arrears.

Mr. Erb commented that his authorities were disturbed by Guinea's unsatisfactory performance under the adjustment program with the Fund, especially by what appeared to have been a lack of credible efforts by the Guinean authorities to achieve the program's objectives. He had noted with satisfaction from Mr. Sangare that the Guinean authorities were in broad agreement with the thrust of the staff report and attached great importance to a continuing dialogue with the Fund. However, there was a need to move beyond dialogue and debate: resolute and sustained actions by the authorities were needed to reduce their economic problems. As Mr. Sangare had reminded Executive Directors, considerable progress had been made in laying the foundations for economic growth, but, as he himself had emphasized when Guinea's stand-by arrangement had been reviewed in the Board, much remained to be done to reinforce and build on the progress that had been achieved. Regrettably, the poor performance under the stand-by arrangement might result in a substantial loss of momentum.

Being in agreement with the staff appraisal, he fully endorsed the policy recommendations made by the staff to the Guinean authorities, Mr. Erb continued. In particular, he would emphasize the recommendations on exchange rate policy, interest rate policy, and the reduction of external arrears. There was also a need to rationalize public enterprises, especially to discontinue transfers from the Government to cover operating losses. In conclusion, there was an urgent need for the authorities to adopt and implement the policy recommendations of the staff, and he could support the proposed decision.

Mr. Senior observed that Guinea faced serious economic and financial imbalances, which, because of their structural nature, needed to be corrected as part of a medium-term adjustment. As a result of both external and internal factors, the imbalances had recently become even greater. Domestically, the dominant imbalance appeared in the financial position of the public enterprises, whose operating performance had deteriorated sharply. The consequent budget transfers from the Central Bank to public enterprises had resulted in substantial increases in public sector spending. Although the authorities had made progress in raising revenue, particularly by collecting additional taxes, those gains had been offset in 1982 by a substantial drain of resources to state enterprises. The drain could have been the result of special circumstances, and it was encouraging that the Guinean authorities recognized the problem and were committed to solving it. Nevertheless, he agreed with the staff that substantial efforts were needed. In combination with other means to increase revenue and prompt institutional actions to improve the implementation of credit policy, the rationalization of public enterprises would contribute toward creating a sounder basis for further progress toward liberalizing the economy.

Given the nature and magnitude of the imbalances in Guinea, a gradual approach to adjustment was appropriate, Mr. Senior considered. However, determined actions in the fiscal and credit fields should be taken promptly, so as to avoid a further deterioration of the imbalances.

Institutional arrangements should be adopted promptly to allow the necessary adaptation of the financial sector to the increased participation of private enterprises. Finally, an improvement was needed in the provision of statistical information; weakness in that field had recently caused difficulties for the authorities in carrying out institutional changes. He agreed with the staff that suitable technical assistance was required; he encourgaged the authorities to seek such assistance from the Fund, the World Bank, and other multilateral institutions. He could support the proposed decision.

Mr. de Vries recalled that, just as Executive Directors had been glad that a stand-by arrangement had been concluded between the Guinean authorities and the Fund in December 1982, they were equally sad to note that the stand-by arrangement had become inoperative so quickly. The staff papers made it clear that the authorities had taken some basic steps toward adjustment, and that they needed to implement a number of important measures clearly delineated in EBS/83/148. He fully endorsed the staff appraisal.

Mr. Casey noted that there was no decision, as such, relating to the review of the stand-by arrangement with Guinea: although the staff papers did in fact review the stand-by arrangement, the title of the paper merely mentioned the 1983 Article IV consultation with Guinea. The same title appeared in the work program and was misleading. He was in broad agreement with the staff appraisal, especially in relation to the exchange rate for the syli, the speed of liberalization, the question of transfers to public enterprises, and the partly related question of external arrears.

While sympathizing with Mr. Sangare's concern that a devaluation of the syli might worsen inflation in Guinea and jeopardize the good wage policy currently in place, Mr. Casey continued, he tended to agree with the staff's recommendation for two reasons. First, in practice many transactions were already occurring at the unofficial--i.e., devalued--exchange rate. Consequently, the inflationary effects that some feared would be transmitted by a devaluation were probably coming through anyway, although in a disguised fashion. Thus, official action on the exchange rate would merely validate what had already been occurring. For example, after a major official devaluation of the Uganda shilling, the inflationary consequences had been slight, because the Ugandan people had already been paying high prices for goods on the black market long before the devaluation. He would encourage the Guinean authorities to examine the case of Uganda. Second, Guinea had much to gain by shifting its impressive agricultural and mineral resources into the export sector. Unfortunately, there did not seem to be agreement between the authorities and the Fund on the difficult exchange rate question, and, partly because of the lack of agreement, the program agreed with the Fund had been inoperative for some time. Indeed, Guinea had drawn only SDR 11.5 million out of the total of SDR 25 million. In most such cases, the national authorities would probably have canceled the program, and he wondered why those in Guinea had not done so. Mr. Sangare's statement that the authorities were continuing to reflect on the question of the exchange rate might imply that there was still a chance for agreement with the Fund on that issue.

The poor statistical base compounded the difficulties of the Guinean economy, Mr. Casey said. Some aid donors were prepared to provide funding and technical assistance to improve Guinea's statistics on the condition that the Fund drew up appropriate terms of reference. How much progress had the staff made in drawing them up?

The longer the authorities of Guinea delayed adjustment, the more entrenched their problems were going to become, Mr. Casey considered. He hoped that Guinea would enter into a new program with the Fund, and that the negotiations would not be too lengthy. There had been other cases in which negotiations had been quite time consuming, so that the staff had been under considerable pressure. A general analysis of the question should be undertaken to see whether the Fund needed to streamline its procedures. In conclusion, he hoped that Guinea would speed up its voluntary or discretionary adjustment before the more painful automatic adjustment took hold, as it inevitably would.

Mr. de Groote expressed concern about the failure to review the stand-by arrangement with Guinea, approved in December 1982, at the same time as the 1983 Article IV consultation. Mr. Sangare and the staff had both said that the Fund's mission to Conakry the previous April had been designed to consider both the Article IV consultation and the review of the stand-by arrangement. Some elaboration on the difficulties experienced in implementing the stand-by arrangement would be welcome.

As in other African countries, the problems confronting the authorities of Guinea were largely structural, Mr. de Groote considered. One basic question was whether the Guinean authorities had fully committed themselves to making an overall change in their economic policies, or whether they still intended to shelter some important sectors of the economy from the operation of the free-market system, thereby courting the dangers of incoherence and misallocation of resources. He understood that the projected reorientation from a centrally planned system to a liberalized system would take longer than expected, since great uncertainties remained with respect to some of the transmission mechanisms. However, the low economic growth experienced by Guinea, the slow improvement in domestic finances, and the present official exchange rate system demonstrated the need for the authorities to redouble their efforts to create conditions under which a revival of economic growth would be possible.

Imbalances in the agricultural sector, which accounted for 50 percent of GDP, had created several problems, Mr. de Groote noted. The minimal growth of agriculture had necessitated substantial food imports into Guinea and had thus increased the pressure on the balance of payments. He agreed with other Executive Directors that a more flexible pricing policy, including exchange rate policy, together with an increase in the momentum of structural adjustment in agriculture, might help to eliminate those large imbalances. On the other hand, as Mr. Sangare had pointed out, important factors were also at work that were beyond the authorities' control: drought or heavy rainfall, lack of infrastructure and irrigation networks, and insufficient agricultural inputs, had all adversely affected agriculture as well.

The trend toward liberalization of the Guinean economy had been accompanied by an expansion of private financing activities between individuals and enterprises into channels that were largely outside the control of the Central Bank and the monetary authorities, Mr. de Groote stated. Would it not be better for the authorities simply to recognize the existence of those parallel financing activities and try to bring unofficial transactions within the purview of the monetary authorities, by means of suitable adjustments in exchange rate and in interest rate policies? The existing institutional framework and economic structure of Guinea were not such as to make it easy to carry out an active interest rate policy. Did the staff consider that a high interest rate was necessary to improve the allocation of resources and savings? On the other hand, given the present inflation rate and the difficulty of acting through the banks, might it not be better simply to close the gap between the rate of inflation and interest rates, even though the latter might still remain negative in real terms? The staff would have to discuss that fundamental question with the authorities before more concrete arrangements could be adopted. Furthermore, he was concerned about the lack of statutory limits on central bank credit, minimum reserve requirements, and liquidity ratios. What was the use of the Fund imposing conditions with which the authorities did not have the tools to comply?

Despite the difficulty of calculating the effective exchange rate for the syli in the absence of price figures, the staff had made a reasonable estimate that the currency had appreciated by about 80 percent by the end of 1982 in trade-weighted terms, Mr. de Groote remarked. The appreciation had been considerable, exceeding any of which he was aware, even that of the Rwanda franc. He could not understand how Guinea's internal financial mechanisms could function in view of the deterioration of the terms of trade for its commodity exports. The policy orientation of the authorities ran directly counter to the direction of the adjustment required; it was an article of faith in the Fund that all member countries should pursue the goal of realistic exchange rates for their currencies. The unrealistic exchange rate of the syli was especially harmful to a country that had already suffered greatly from unavoidable decreases in export proceeds.

The inoperative stand-by arrangement had included a separate performance clause requiring the Guinean authorities and the Fund staff together to make a detailed study of the exchange markets and to reach an understanding on Guinea's exchange rate policy by the end of February 1983, Mr. de Groote recalled. He hoped that a better understanding would be reached in the coming months and that the staff would be able, in further negotiations, to pursue the objectives that were basic to the doctrines of the Fund.

Mr. Grosche expressed support for Guinea's efforts to reorient its economy away from a centrally planned system and toward a more liberalized one. Some success had been achieved, but the economic and financial situation had remained difficult in the recent past. The lack of economic efficiency inherent in the transition from one system of economic organization to another made even greater effort necessary. However, the steps taken hitherto toward a more liberal system were so small that they were inadequate to enable the country to take full advantage of its large agricultural and mineral resources.

Another impediment was the splitting of the economy into an official and an unofficial sector, Mr. Grosche observed. The latter appeared still to be growing. While the reunification of the economy was urgently needed, it would take time, Guinea's economic problems being mainly long term and structural. Therefore, the authorities should determinedly pursue the new policy of increasing the scope for market-oriented activity. Considering the lack of success in reducing the large imbalances in the economy, sector adjustment and a redoubling of efforts by the authorities seemed to be called for, Mr. Grosche went on.

As the staff had clearly pointed out, Guinea's record under the stand-by program could only be regarded as poor, Mr. Grosche said, and the uncertain prospects for renewed adjustment by the authorities were disappointing. The principal policy measures under the stand-by arrangement were well founded, and could still serve as the base for a reactivation of the program. When the Board had discussed Guinea's request, Executive Directors had not regarded the conditionality in the program as excessively tight, and they had considered that the measures already taken by the authorities at that time demonstrated a strong commitment and justified some optimism. That the program had turned out not to have been a success appeared largely due to factors within the authorities' control. He wondered, however, whether Executive Directors might have underestimated certain difficulties that were unavoidable during the initial phase of transforming an economy. In conclusion, he was in broad agreement with the staff's policy recommendations and could support the proposed decision.

Mr. Alfidja remarked that during the past few years, especially in 1982, financial and economic developments in Guinea, a country well-endowed in agricultural resources and minerals, had been less than favorable. Real economic growth had been about 2 percent a year during 1980-82, significantly below the 3 percent growth rate of the population. Institutional rigidities, bad weather, and a shortage of inputs and consumer goods had played a major role in the stagnation of agricultural and livestock production. The prolonged recession in industrial countries had also unfavorably affected the demand for Guinean minerals, particularly bauxite, the country's largest source of foreign exchange. Large financial imbalances had also emerged; in 1980, the public sector deficit had reached a record 21 percent of GDP, although by 1982 it had fallen to about 9 percent of GDP. In the external sector, a relatively weak current account combined with an unfavorable capital account position had led to large overall balance of payments deficits, pronounced declines in international reserves, and the accumulation of payments arrears.

In mid-1982, the Guinean Government had undertaken a Fund-assisted financial program designed to abate inflation, reduce monetary expansion, restore viability in external accounts, and decrease external arrears, Mr. Alfidja recalled. Although Guinea's achievements under the program had been mixed, the policies pursued had gone in the right direction. After all, until recently, modern economic activity had been almost entirely organized along centrally planned lines, with little room for the expansion of local private initiative.

In the real sector, the legalization of private trade and the related decline in the role of the public sector in commerce--through the closure of certain public enterprises and the abolition of marketing quotas--might stimulate production and ease the shortage of some commodities, Mr. Alfidja stated. The increasing cooperation between the Government and foreign institutions, including the World Bank, for the development of livestock, fishing, and mining, deserved encouragement. More progress could also be expected in data collection. As in many developing countries, the lack of adequate data in Guinea needed to be addressed urgently by the authorities, since the performance of the real and financial sectors could not be reliably monitored without such information.

He welcomed the recent attention being given to the situation of public enterprises, for transfers from the Government to those enterprises had been a major contributing factor to the deterioration in the fiscal position, Mr. Alfidja noted. He hoped that the restructuring of the public sector through closure, rehabilitation, and increased operational autonomy would lessen the drain on scarce government resources. Several public enterprises were selling their goods and services below cost, so that greater flexibility in their pricing policies could prove to be well advised. Developments in the public sector in Guinea mirrored the dominant role played by governments in virtually all centrally planned economies. Yet internal and external viability could not be restored unless the authorities made a determined effort to prune public expenditure, especially the transfers to public enterprises. While he could understand the need to absorb some of the workers displaced by the closure of such enterprises, he wondered about the effect on morale and productivity of unusually long periods of wage freeze at a time of sustained inflation.

He welcomed the decision to relax some foreign trade restrictions by allowing private traders to export many commodities and to import several others by using their own foreign exchange, Mr. Alfidja continued. That relaxation, together with a pragmatic approach to the exchange rate, might prove beneficial.

Guinea's external debt service ratio, stagnant in recent years at about 25 percent, was forecast to deteriorate slightly to 27 percent in 1983, Mr. Alfidja noted. Likewise, an increase in external interest payments from about 2 percent to 6 percent of exports was projected for 1983. The combination of that outlook with a near doubling of external payments arrears in two years to about SDR 160 million deserved serious attention. In conclusion, he was encouraged by the Guinean authorities' intention to continue addressing their difficult structural problems.

Mr. Suraisry expressed general agreement with the staff appraisal and supported the proposed decision. Guinea continued to face serious economic and financial problems; performance under the recent stand-by arrangement with the Fund had not been satisfactory, and immediate prospects were not encouraging. Economic growth was slow, inflation was high, the financial position of the public sector was deteriorating, and sizable external arrears had accumulated. If the economy was to recover, the authorities would have to take firm corrective measures in several areas.

The authorities were to be commended for the steps taken so far toward opening up the economy and expanding the role of the private sector, Mr. Suraisry went on. He encouraged them to continue to move in that direction. Although there had inevitably been transitional problems, the benefits should be considerable over the medium term. He hoped that the authorities would also strengthen the machinery for development planning in order to derive the full benefit from the country's abundant natural resources. The authorities had taken a useful step in the right direction by establishing a central office for project appraisal, with assistance from the World Bank.

There was clearly a need for further adjustment on the fiscal side, Mr. Suraisry observed. Despite an annual growth in revenue of 18 percent since 1980, the overall public sector deficit remained high as a proportion of GDP. He therefore welcomed the authorities' intention to reduce the deficit in 1983, a task that would require a determined effort to reduce current expenditure, which had exceeded the limits set under the stand-by program by a wide margin. It would be particularly important to streamline the operations of the public enterprises, which were a major drain on the Government's limited financial resources. Measures might also be needed to broaden the revenue base.

In the external sector, Mr. Suraisry said, he had noted that the authorities differed from the staff on the feasibility, appropriateness, and timing of an adjustment in the exchange rate for the syli. While it was a difficult time for the authorities, gradual adjustments in the exchange rate--particularly when it was out of line--could give the authorities room to raise producer prices to more realistic levels. In turn, an increase in producer prices could boost agricultural production and increase the volume of exports through official channels.

He had been glad to note that the authorities remained committed to phasing out external arrears, Mr. Suraisry remarked. However, progress had been slow, and the authorities should give priority to establishing a realistic timetable for the elimination of arrears, a move that would help to restore external confidence and stimulate much-needed inflows of foreign capital. The restoration of external confidence would also require extremely cautious debt management policies, in view of the heavy burden of debt service payments in the near term. As suggested by the staff, multilateral debt renegotiations could be one way of alleviating the immediate pressures on the balance of payments. In brief, with courage and determination, the authorities could overcome their economic and financial problems.

Mr. Péroz agreed with the staff appraisal and was prepared to support the proposed decision. The staff report and Mr. Sangare's statement gave a full description of the pitfalls encountered during the authorities' attempts to liberalize an economic system after so many years of almost total central control. He greatly regretted the authorities' inability to observe the performance criteria of the present stand-by arrangement with the Fund. Unfortunately, the report did not suggest that the prospects for reactivating the stand-by arrangement were bright. Perhaps his main worry was that there were signs of a weakening in the authorities' resolve to move toward an economic system more likely to make efficient use of the country's vast potential. In several areas, serious doubts were justified about the status of the authorities' commitment to further action.

There had been no question at the time that the Fund had concluded the present stand-by arrangement with Guinea that the issue of the exchange rate would have to be addressed before the end of February 1983, Mr. Péroz recalled. The authorities appeared not to share the conclusions of the staff and to believe that such action on the exchange rate, as recommended by the staff, would be inopportune. He suspected that the use of the term "inopportune" could well mean that any action in that field had been postponed indefinitely. Furthermore, developments in other areas appeared to substantiate this view that the authorities were reducing their commitment to the path of adjustment previously agreed upon. They were committed to external trade liberalization and to support for loss-making public enterprises. He hoped that the divergence of views between the authorities and the staff about the budget outlook could be clarified. As shown by the staff projections, the absorption of resources by the public sector in 1983 was likely to be such that he found it hard to understand how the development of private sector activities, as desired by the authorities, could take place to any significant extent. However, the authorities had indicated that they needed more time to reflect further on the different scenarios as well as on their broader implications. He therefore hoped that, at the very least, the repeated discussions that had taken place between the staff and the authorities during the past two or three years would continue. Finally, he hoped that the fruitful dialogue that had led to Guinea's first use of Fund resources under a stand-by arrangement would again prove valuable.

Mr. Qureshi expressed agreement with the thrust of the staff paper. Economic conditions remained difficult in Guinea, as low growth and financial imbalances had persisted. For some time, the authorities had recognized that, in addition to exogenous factors such as bad weather and a worldwide recession, Guinea's unsatisfactory economic performance was related to certain major structural weaknesses within the economy that called for policy action. For several years, they had been pursuing a program of liberalization aimed at promoting the role of the private sector as well as improving the functioning of public sector enterprises through decentralization and greater competition. In 1982, the authorities had further underlined their commitment to economic change by adopting a one-year adjustment program supported by a stand-by arrangement with the Fund.

Guinea's liberalization adjustment had permitted some notable gains in recent years, Mr. Qureshi considered. For instance, the scope of private sector activity had expanded appreciably, especially in agriculture and trade. The authorities had introduced significant reform measures to improve the performance of public enterprises, including the granting of greater operational autonomy to individual enterprises and the disbanding of persistently loss-making units. They had maintained firm control of wages while exercising greater flexibility in determining prices, particularly producer prices for a range of agricultural products. Nevertheless, progress in improving the growth rate and reducing financial imbalances had been slow and limited, short of the expectations contained in the 1982 adjustment program.

The staff had highlighted several policy areas in which the pace of adjustment and reform needed to be expedited, Mr. Qureshi noted. Producer incentives could be further improved through price flexibility, the fiscal position could be strengthened by reducing the reliance of public enterprises on government transfers, and there could be adequate allocations of credit to the private sector and an adjustment in the exchange rate. He had been glad to hear from Mr. Sangare that the authorities also saw a need for further action in most of those areas and remained committed to pursuing the objectives of liberalization and adjustment. The main point on which the authorities appeared to differ from the staff was on the desired pace of change, rather than on the need for a change. In certain respects, the authorities' preference for a more gradual approach would be understandable, as the needed adjustment involved difficult structural measures. For example, the liberalization program represented a move toward a mixed economy from a system that had been highly centralized for an extended period. The difficulty of the transition was made more severe by limitations in Guinea's institutional and administrative capacity. However, within the overall liberalization and adjustment program, the authorities could consider taking quicker action when the need for change was as urgent as it had become. A clearer understanding between the authorities and the Fund on the pace and scope of adjustment could open the way to a new adjustment program better suited to solving Guinea's problems.

The staff had also noted that data on private sector activities were largely lacking, a shortcoming that prevented a fuller assessment of economic and financial developments in recent years, Mr. Qureshi concluded. For instance, the lack of data could result in a serious underestimation of the growth in private sector activity due to the authorities' efforts at liberalization. Technical assistance from the Fund could be useful in improving the data base. Assistance could also be provided in adapting the tax system to the growing role of the private sector. In conclusion, he noted the authorities' continued commitment to phasing out existing external payments arrears as soon as possible.

The staff representative from the Exchange and Trade Relations Department, responding to questions by Executive Directors, recalled that Mr. Casey had inquired about technical assistance in assembling economic statistics. The Guinean authorities had informed the staff that they were making bilateral arrangements with friendly governments to provide assistance in statistics; the Fund staff was working with colleagues in the World Bank to define the scope of those arrangements and to specify the areas dealing with the work of the two institutions. An improved statistical base would help the Fund staff in analyzing Guinea's budget statistics, external debt, and money and banking data. The staff hoped that in the next several months some progress would be made.

Another question had been why the title of the staff paper had not mentioned the review of the stand-by arrangement, the staff representative continued. The Fund staff had found it impossible to reach understanding with the Guinean authorities, especially on the central question of exchange rate policy. Therefore, the staff had had nothing to report on the review exercise. It would have been misleading to give any indication on the title page of the paper that the Executive Board might have to take a decision on a review of Guinea's progress under the stand-by arrangement. The staff had made it clear in the introductory section that the discussions held with the authorities, which had been reported to the Board, had dealt with a review of Guinea's performance under the stand-by arrangement, and in Section III the staff had analyzed Guinea's performance under the program.

One question asked by several Executive Directors, especially by Mr. de Groote, had to do with interest rate policy, the staff representative from the Exchange and Trade Relations Department recalled. The argument advanced by the staff was that, given the vast monetary expansion and the high rate of inflation in Guinea, intermediation by banks was being hampered. As the rate of inflation was some 30-40 percent a year and as the rate paid on deposits was about 10 percent a year, money holders found it unattractive to deposit their assets in banks. The banking system in Guinea being rudimentary, and official instruments of monetary and credit policy being rather limited, the question of an appropriate exchange rate under such circumstances was, of course, not easy to decide. Nevertheless, considering that the interest rate was perhaps the main instrument available to the authorities, the staff had felt that they should seek to be more active in using it.

The staff representative from the Legal Department observed, in reply to a question concerning the proposed decision, that, under a policy adopted by the Executive Board, decisions under Articles IV, VIII, and XIV were to be limited to those areas over which the Fund exercised its surveillance and approval jurisdiction. That was one reason why no mention was made in the decision on Guinea of any use of Fund resources.

The Acting Chairman said that, as mentioned on page 8 of EBS/83/148, a study of the exchange rate system of Guinea had been a performance criterion under the stand-by arrangement agreed with the Fund. It was to have been carried out jointly before the end of 1982, "with a view to making appropriate formal changes in the system before the end of February 1983." The staff report had gone on to note on page 23 that, almost immediately after the stand-by had been approved on December 1, 1982, the Fund had dispatched a mission to Conakry for the specific purpose of reviewing Guinea's exchange rate system. Had the staff mission been successful in completing the review, and had the Fund considered any action taken to have been appropriate, a paper would have come forward to the Executive Board for its consideration, presumably in February 1983. The results of the review had not been presented to the Executive Board because they had been unsatisfactory.

Mr. Sangare noted that there was still some room for the Guinean authorities to make a further effort, as they themselves recognized. In particular, there was a particular need for restoring the performance of public enterprises, adapting exchange rate policy, and improving statistics. He would like to reassure his collegues, particularly Mr. Péroz, that the authorities in Guinea were committed to undertaking adjustment and to pursuing the objectives of the program as set out in the stand-by arrangement approved by the Executive Board. However, efforts by the Guinean authorities alone could not result in full success; they would need to continue to be endorsed by certain friendly countries, to which the authorities were grateful.

The Acting Chairman made the following summing up:

In their review of recent economic and financial developments in the Guinean economy, together with a discussion on Guinea's performance under the one-year stand-by arrangement granted by the Fund in December 1982, Directors were in agreement with the thrust of the analysis and appraisal in the staff report. Disappointment was expressed at the performance under the stand-by arrangement, and it was observed that financial imbalances had recently worsened. While welcoming the liberalization process that had been launched by the Guinean authorities, Directors emphasized the importance of accelerating, broadening, and sustaining this process and, more important, of implementing measures in this sphere as a means of strengthening the necessary incentives for the revival of economic growth. In this connection, it was considered important that official producer prices should be raised substantially, supported by appropriate changes in the exchange rate.

On domestic financial developments, Directors pointed to the continued deterioration of public finances, particularly in state enterprises. Directors stressed that it would be important for the Guinean authorities to reinforce their rationalization efforts with respect to state enterprises so as to minimize the financial drain imposed by these enterprises on the Government's budget. Directors also stressed the importance of the institutional and structural changes occurring in the Guinean economy.

On credit policy, Directors were of the view that the necessary adaptations should be made in Guinea's banking system to cover the genuine credit needs of the private sector. In this context, it was suggested that, with appropriate adjustments in interest rate and exchange rate policy, action might be considered to bring informal credit operations into the ambit of official action.

Directors emphasized that the process of policy formulation in Guinea would benefit from intensified efforts to improve the statistical base. In this connection, Directors encouraged Guinea to benefit from increased use of technical assistance from the Fund, the World Bank, and other external sources, particularly in the areas of banking and budget statistics.

In their discussion of external sector developments and policies, Directors noted the weak balance of payments situation that had prevailed for a number of years in Guinea and urged the Guinean authorities to take early action to correct the maladjustments in the economy. In particular, Directors were of the view that substantial modifications in Guinea's exchange arrangements were urgently needed. They considered it important for agricultural and mineral exports to be given support through the exchange rate. It was regretted that the stand-by arrangement with the Fund had become inoperative owing to failure to reach understandings with respect to the exchange rate.

Directors noted that it would be helpful to the authorities and to their international credit standing if their commitment to the phased elimination of external payments arrears could be pursued within an orderly multilateral framework. As to the trade and payments system, while noting the progress that had been made, Directors hoped that the Guinean authorities would make further progress in the elimination of restrictive practices.

In sum, while understanding the fundamental nature of the changes involved and their implications for the time required, many Directors strongly emphasized the necessity for the authorities to act more boldly and decisively in the process of reform, liberalization, and redressment that had been set in motion.

It is understood that the next Article IV consultation with Guinea would be held on the standard 12-month cycle.

The Executive Board then took the following decision:

Decision Concluding 1983 Article XIV Consultation

1. The Fund takes this decision relating to Guinea's exchange measures subject to Article VIII, Sections 2 and 3, and in concluding the 1983 Article XIV consultation with Guinea, in light of the 1983 Article IV consultation with Guinea conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. While generally continuing the trend toward liberalization, Guinea maintains a number of restrictive exchange practices as described in EBS/83/148. The Fund welcomes the progress made in Guinea in the pursuit of liberalization policy, but would urge the authorities to take early comprehensive action to correct the maladjustment in costs and prices in the Guinean economy and to accelerate progress in eliminating restrictive practices, including the external payments arrears and the bilateral payments arrangements with Fund members.

Decision No. 7489-(83/119), adopted
August 5, 1983

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/83/118 (8/3/83) and EBM/83/119 (8/5/83).

2. ANNUAL REPORT, 1983

The Executive Board approves the transmittal of Chapter 1, Revision 2; Chapter 2, Revision 2; and Chapter 3, Revision 1, and Appendices I-VIII to the 1983 Annual Report to the Board of Governors, under cover of the letter set forth in EBD/83/112, Supplement 1 (8/1/83).

Adopted August 4, 1983

3. 1983 ANNUAL MEETING - EXECUTIVE BOARD - REPRESENTATION EXPENSES

The Executive Board approves the recommendation set forth in EBAP/83/200 (7/29/83).

Adopted August 3, 1983

4. ADVISORS TO EXECUTIVE DIRECTORS - REMUNERATION

The Executive Board approves the recommendation set forth in EBAP/83/201 (7/29/83).

Adopted August 3, 1983

5. APPROVAL OF MINUTES

The minutes of Executive Board Meetings 83/37 and 83/40 are approved. (EBD/83/198, 7/28/83)

Adopted August 3, 1983

6. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors as set forth in EBAP/83/203 (8/3/83) is approved.

APPROVED: February 14, 1984

JOSEPH W. LANG, JR.
Acting Secretary