NOT FOR PUBLIC USE

INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 83/130

10:00 a.m., September 6, 1983

J. de Larosière, Chairman

Executive Directors	Alternate Executive Directors
A. Alfidja	
	H. G. Schneider
	X. Blandin
	R. J. J. Costa, Temporary
R. D. Erb	
	T. Alhaimus
T. Hirao	T. Yamashita
	J. Reddy, Temporary
R. K. Joyce	M. Casey
A. Kafka	C. Robalino
G. Laske	G. Grosche
G. Lovato	C. P. Caranicas
	A. S. Jayawardena
Y. A. Nimatallah	J. E. Suraisry
J. J. Polak	T. de Vries
	K. G. Morrell
G. Salehkhou	
	E. I. M. Mtei
	M. Camara, Temporary
	S. E. Conrado, Temporary
	A. Lindø
	C. Taylor
Zhang Z.	Wang E.

L. Van Houtven, Secretary
S. J. Fennell, Assistant

Also Present

African Department: J. B. Zulu, Director; O. B. Makalou, Deputy Director; J. A. J. Bove, E. L. Bornemann, R. O. Carstens, F. d'A. Collings, Y. Fassassi, M. G. Fiator, R. A. Franks, A. Jbili, J. W. Kratz, H. R. Lorie, S. N'guiamba, B. R. H. S. Rajcoomar, M. Reichardt, I. C. Tandeciarz, U. Wilson, A. C. Woodward. Asian Department: H. O. Roden. Exchange and Trade Relations Department: C. D. Finch, Director; W. A. Beveridge, Deputy Director; S. Mookerjee, Deputy Director; H. Ghesquiere, S. Kanesa-Thasan. External Relations Department: D. Cheney. Legal Department: G. P. Nicoletopoulos, Director; J. G. Evans, Jr., Deputy General Counsel; G. F. Rea, Deputy General Counsel; J. K. Oh, S. A. Silard. Research Department: W. C. Hood, Economic Counsellor and Director; R. R. Rhomberg, Deputy Director; C.-Y. Chu, N. M. Kaibni, E. A. Milne, T. K. Morrison. Secretary's Department: A. P. Bhagwat. Bureau of Statistics: T. T. Luu. Personal Assistant to the Managing Director: N. Carter. Advisors to Executive Directors: S. R. Abiad, A. A. Agah, T. A. Connors, S. El-Khouri, P. Kohnert, H.-S. Lee, P. D. Péroz. Assistants to Executive Directors: E. M. Ainley, H. A. Arias, M. B. Chatah, G. Ercel, C. Flamant, I. Fridriksson, G. Gomel, V. Govindarajan, N. U. Haque, M. Hull, M. J. Kooymans, P. Leeahtam, W. Moerke, V. K. S. Nair, J. K. Orleans-Lindsay, G. W. K. Pickering, E. Portas, J. Schuijer, Shao Z., D. I. S. Shaw, J. C. Williams.

1. TOGO - STAND BY ARRANGEMENT - MID-TERM REVIEW

The Executive Directors considered the staff report on the mid-year review under the stand-by arrangement for Togo (EBS/83/168, 8/10/83).

The staff representative from the African Department remarked that a Fund staff member had taken up his position as resident representative in Lomé in the previous week. Preliminary indications were that the performance criteria for end of June 1983 had been met; in particular, domestic arrears had been reduced by about SDR 25 million.

Mr. Alfidja stated that serious financial imbalances had emerged in Togo in the mid-1970s, largely as a result of a public investment program, which, with the benefit of hindsight, appeared overambitious, most notably with respect to the projected returns. The problems had been compounded by adverse developments in the export sector, which had affected export earnings and had reduced Togo's ability to service its debt. It was against that background that the authorities had undertaken a Fund-supported adjustment program.

At the time of the Executive Board's discussion of Togo's request for a stand-by arrangement, Directors had been particularly concerned about three major issues, Mr. Alfidja recalled: first, the pace and the strength of the adjustment effort; second, the likelihood of reaching a debt rescheduling agreement; and, third, the status and magnitude of the public investment program. Some Directors had suggested that, given the magnitude of the economic imbalances, the targets had not been strict enough and that greater adjustment should have been sought. It would be incorrect to suggest that the observance of the performance criteria under the present program was an indication that the initial targets had been insufficiently tight. The success recorded thus far reflected the authorities' determination in pursuing the adjustment effort despite the shortfall in export earnings and the decline in real GDP. The economic and social costs associated with the austerity measures--such as the reduction in public sector real wages--should not be ignored.

Togo had reached an agreement with Paris Club creditors in April 1983, and with commercial bank creditors in July 1983, Mr. Alfidja indicated. As the staff had noted, the terms of the Paris Club had been more favorable than anticipated, a clear indication of creditors' appreciation of the authorities' adjustment effort. The authorities had applied the additional resources available as a result of the debt rescheduling to the retirement of some of the domestic payments arrears, which indicated their resolve to improve the country's economic situation.

Some Directors had also expressed concern about the lack of a medium-term investment program, Mr. Alfidja went on. An agreement had been reached with the World Bank on investment-related issues within the framework of a structural adjustment program. He had doubts that the adoption of more severe austerity measures, such as greater cuts in real government outlays, would quickly restore financial balance in the economy. A major sustained improvement in the terms of trade, together with more favorable debt rescheduling arrangements, would help to ease the debt burden. The Fund's support in that respect could not be overemphasized.

Mr. Blandin noted that, despite unfavorable external developments, such as the return of migrants from Nigeria and the severe drought, the adjustment program remained on track, undoubtedly as a result of the authorities' perseverance. Nevertheless, the medium-term prospects were not bright, and painful adjustment efforts would remain necessary in the years to come.

The results of the program were impressive, Mr. Blandin considered. On the fiscal side, the consolidated government deficit was forecast to be reduced to 2.5 percent of GDP, which was better than the 3.2 percent of GDP originally envisaged. In addition, the current account deficit should be less than anticipated. Those results stemmed, in part, from the favorable terms of debt relief from the Paris Club, amounting to CFAF 37.23 billion rather than the expected CFAF 29.9 billion. Those additional resources had not been used to relax financial conditions, but to settle some of the external payments arrears through net cash payments and to reduce domestic arrears by CFAF 11 million.

The economic situation was still far from good, Mr. Blandin observed. After two years of decline, real GDP would again be reduced by 3 percent in 1983--a slightly greater than projected decline because of the adverse impact of the drought. The medium-term projections for the balance of payments and the debt service ratio remained as bleak as they had been six months previously. In the following year, there would be no room for any relaxation of fiscal or monetary policies. Moreover, the present adjustment measures alone would be insufficient to achieve a sustainable balance of payments position in the medium term.

Structural reforms designed to widen the productive base and increase the volume of exports were necessary, and in that respect he welcomed the structural adjustment credit of $40 million approved by the World Bank, which should help the authorities to address a number of issues necessary to restore steady economic growth, Mr. Blandin went on. The authorities had already taken some courageous steps to improve the management of the public enterprise sector--such as closing a number of enterprises--but much still remained to be done to alleviate the burden on public finances. Revitalization of the agricultural sector was another important issue that needed to be addressed; in particular, a medium-term pricing policy providing sufficient incentive for producers should be developed. In conclusion, Togo had taken the first and more painful steps in the right direction, but the path toward a complete recovery would be a long one. It was particularly important that the authorities' efforts should be sustained by sizable amounts of assistance from the international community, and he was sure that donors would be encouraged by the success of the present program.

Mr. Erb recalled that his chair had not been able to support Togo's request for a stand-by arrangement in March 1983. He had been concerned about four elements of the proposed adjustment program, namely, that there was inadequate fiscal adjustment, an inadequately defined investment plan for 1983, and uncertainty with regard to donor assistance and the necessary debt relief. Three of the four concerns had been dealt with. An investment program for 1983 had been adopted and structural adjustment credit had been approved by the World Bank. Official and private debt had been rescheduled on terms that were more favorable than expected.

Furthermore, budget grants had been nearly twice the original estimates, Mr. Erb observed. However, despite the smaller overall fiscal deficits, greater fiscal adjustment was required. His chair had commended the authorities in March 1983 for the steps taken to strengthen the fiscal position, but had stressed that more was required, especially in allocating resources to more productive activities. Although the fiscal deficit was now projected to reach only 2.7 percent of GDP compared to the target of 3.2 percent of GDP, that improvement was primarily due to the higher than projected foreign grants. If those grants were excluded, the fiscal deficit would be equivalent to 6.1 percent of GDP. He hoped that the assignment of a Fund representative in Togo would help to prevent further deterioration in the fiscal situation. He shared the staff's view that the delay in adopting the tax reform proposal was regrettable, and he urged the authorities to undertake the proposed reform in September 1983. Could the staff indicate the present status of the tax reform measures?

He was also disturbed about the authorities' delay in taking action with regard to the parastatal enterprises, Mr. Erb remarked. In particular, the failure to take necessary decisions regarding the steel mill, the oil refinery, and the government trucking industry would remain an unnecessary drain on Togo's resources. The nature and magnitude of Togo's problems indicated that considerable structural adjustment, debt relief, and donor assistance were essential to achieve a sustainable balance of payments position. Progress had been made, but it was imperative that the authorities should persevere and consider strengthening their adjustment measures. The Fund had a critical role to play in providing technical assistance and as a catalyst vis-à-vis creditors and donors.

Togo should receive its financing primarily from development assistance, including debt restructuring, Mr. Erb said. Fund assistance should be used only in instances where the financing problem was temporary and where the authorities would be able to repay without taking destructive measures. Finally, in spite of his concerns, he could support the proposed decision.

Mr. Laske observed that Togo had met the performance criteria. The authorities had introduced most of the measures under the adjustment program, and their resolve had shown positive results; in particular, the current account of the balance of payments and the overall budget position had improved. Although weather conditions and political instability had been detrimental to the adjustment effort, the international community had generously granted debt relief on favorable terms. Moreover, Togo had been granted least developed nation status, an action that would ensure sympathetic consideration in the future. The better than expected terms of the Paris Club rescheduling had provided some additional leeway in the budget area, and he was especially pleased that the authorities intended to reduce considerably the external arrears. He welcomed the authorities' decision to use the additional resources available from the debt rescheduling to reduce domestic arrears, rather than to relax public spending.

The outlook for Togo was not bright, mainly owing to weak demand for its export products, Mr. Laske noted. Even under the assumption of continuous debt relief, the debt service ratio would remain at about 50 percent in the medium term. Given those dire prospects, the authorities should persevere with their adjustment efforts, particularly in the areas of public finance and the state economic enterprises.

He hoped that the tax reform proposal would be implemented promptly, and that the reform of the state economic enterprises would not be delayed further, Mr. Laske stated. The authorities' determination with regard to current public expenditure, especially wage increases, was welcome. In conclusion, he could support the proposed decision.

Mr. Taylor noted that Togo's situation had improved, owing in part to the relatively generous rescheduling arrangements, but also to the fiscal and structural adjustment measures taken earlier in 1983. Nevertheless, the improvements were not sufficient to alter Togo's somber medium-term prospects. There had been some setbacks that were attributable to the drought and the general deterioration in the economic and political conditions of major West African countries. Some economic factors had actually worsened in the previous six months; for example, output was lower and inflation higher than expected. It would be useful to have a medium-term picture of developments in the economy. Could the staff indicate whether the effects of the drought were expected to be largely overcome by 1984, given reasonable rainfall in the region?

There had been an apparent improvement in the fiscal situation, Mr. Taylor observed, but it should be noted that most of the improvement had come about through the larger than expected foreign grants. Could the higher level of grants be expected to continue in 1984 or did they represent an acceleration of previously committed aid programs?

Like other Directors, he was concerned that revenue was falling short of earlier estimates despite higher than expected inflation, which undoubtedly reflected the weakness of activity and also the delay in implementing the tax reform, Mr. Taylor went on. The tax reform proposal should be implemented as soon as possible. Could the staff indicate whether the benefits expected from the tax reform would be large enough to bring about an improvement in the economic situation in 1984? Had the recently introduced measures begun to operate effectively?

The reduction in the overall balance of payments deficit was encouraging, although much of that improvement was due to debt rescheduling, Mr. Taylor remarked. There were some signs for optimism in the terms of trade, in particular because of the higher world prices for cocoa, cotton, and coffee. What was the staff view of the prospect for the trade balance beyond 1983? Had the drought had any effect on the level of food imports? Was there any prospect of increased demand for phosphates in 1984?

The debt service ratio remained uncomfortably high, Mr. Taylor considered. The depreciation of the CFA franc would help to improve the competitiveness of exports, but could the staff comment on the sustainability of the debt service profile? External arrears on a net basis had risen in the first part of 1983 despite the larger than expected cash payments. He wondered whether agreement had been reached with the private as well as the official creditors, in which case total outstanding arrears would henceforth be significantly reduced. The authorities were making significant progress toward reaching their target for the reduction of arrears in 1983.

He could support the staff appraisal and endorse the prosposed decision, Mr. Taylor indicated. The authorities had made reasonable progress in their adjustment effort and the performance criteria had been observed thus far. However, a sustained adjustment effort would still be required, and further action was needed to reform the parastatals and restructure investment priorities.

Mr. Polak recalled that at the time of Togo's request for the stand-by arrangement he had supported the decision on condition that further purchases should be contingent upon three factors: a coherent medium-term investment strategy, an investment program for the second half of 1983 supported by the World Bank, and evidence of effective public expenditure control. He had indicated that the review should also focus on the rescheduling of debt due in 1983 and the progress in eliminating external arrears. Progress since March 1983 had been sufficient to justify a further purchase. An investment plan for 1983 had been approved by the World Bank, and reviews by the World Bank would control the release of further money under the structural adjustment credit.

On the fiscal side, the overall government deficit was now projected to decline to 2.7 percent of GDP, which was less than the planned 3.2 percent of GDP, Mr. Polak observed. That improvement was due in part to more generous than expected foreign grants. Expenditures had been contained, with economies achieved particularly in personnel expenditure. As a result of the delay in implementing the tax reform, revenues should fall short of target in 1983. However, that shortfall was compensated for by lower than expected expenditures. In addition, there would be a significant reduction of arrears in 1983.

Although he approved the proposed decision, he was concerned about the longer-term prospects for Togo, Mr. Polak stated. Togo's massive debt was related to low-yielding or, perhaps, nonyielding investment.

The burden of debt service payments therefore fell heavily on the agriculture sector. In that respect the Fund could play only a limited role. It was a problem primarily for aid donors, and he wondered whether the aid donors' conference planned for late 1984 or early 1985 could be advanced.

Mr. Camara indicated his support for the proposed decision. The authorities had taken difficult measures in order to meet the performance criteria under the current program. The fiscal deficit was likely to be less than foreseen, and the balance of payments projections were expected to be in line with the targets. The authorities had introduced important fiscal measures in 1983 to complement the structural adjustments made in 1982. Nevertheless, the medium-term outlook remained unfavorable. The balance of payments position was unlikely to improve because the high debt service ratio continued to impose a large burden and because exports remained sluggish. Continued adjustment efforts were needed to ensure a well-balanced financial system. Finally, he welcomed the World Bank-sponsored investment program and the assignment of a Fund representative in Lomé.

The staff representative from the African Department stated that the staff intended to discuss the tax reform with the authorities at the time of the proposed Article IV consultation in October or November 1983. It was estimated that the benefits from the reform would amount to CFAF 2-3 billion a year. Measures introduced to ensure more efficient tax collection had been effective. There had been some delay in implementing the reforms with regard to the parastatals, but he was hopeful that the assignment of a World Bank resident representative in Lomé would advance the reforms.

As to the effects of the drought, there had been some reduction in food output, but the staff had received no information on food imports, the staff representative went on. The volume of agricultural exports, particularly of cocoa, had declined, but most of the financial impact would not be felt until 1984.

It was difficult to predict whether the level of foreign grants would be maintained because those received in 1983 included exceptionally large grants from the European Development Fund, totaling nearly CFAF 5 billion, the staff representative continued. He could only hope that similar contributions would be forthcoming in the following year. Changes in the trade balance were also difficult to predict because of the volatility of commodities markets. On the import side, it was unlikely that there would be a surge in volume, and it was therefore probable that the trade deficit would continue at the same level. The staff had projected that phosphate exports would stay at about 2 million tons a year in future years. The medium-term debt profile was somber. It was difficult to determine whether Togo would be in a position to service its debt, but, if fiscal austerity and the adjustment efforts were maintained, a sustainable position might be reached in a few years. The increase in arrears in the first half of 1983 had occurred because the rescheduling arrangements had not been concluded until April 12, 1983. However, there had been no net increase in arrears that were not subject to rescheduling.

The World Bank and the United Nations were organizing the donors' conference, the staff representative from the African Department stated. At a preliminary conference held in Lomé in June 1983 at the time of the Fund mission, they had decided that it would be unwise to schedule the conference too early. It was, therefore, unlikely that the Fund could advance the date of that meeting.

Mr. Erb noted that the West African Monetary Union had raised interest rates by 2 percentage points to 7 percent for medium-term loans and 9-11 percent for long-term loans. In view of the projections for inflation, the interest rate on savings deposits was still negative in real terms; could the staff comment on what impact that feature might have on savings?

The staff representative from the African Department remarked that it was unlikely that there would be any reduction in lending activity by the banks because the banks in Togo were overliquid. Lomé had become a kind of regional banking center because of the instability in other countries within the region.

Mr. Alfidja stated that he felt slightly more at ease having heard the comments of Executive Directors. In the past, Directors had been too critical of Togo. He was not saying, however, that Togo's economic problems were settled; there was still a long way to go before the country would recover from the economic difficulties that it was experiencing.

He disagreed with Mr. Erb on the adequacy of fiscal adjustment, and he did not believe that further adjustment was possible, Mr. Alfidja went on. At the time of Togo's request for a stand-by arrangement, his chair and the staff had pointed out that the tax burden was already much greater than in other countries. The expression "tax reform" was somewhat misleading. Although the revenues were expected to increase by CFAF 2-3 billion in 1984, the impact on revenues in 1983 would be only about CFAF 250 million. Based on recent discussions with the Minister of Finance of Togo, he believed that the tax reform measures would be implemented in the near future.

The problem of implementing the reform of the public sector enterprises was a complex one, Mr. Alfidja remarked. The authorities were not able to stick to a timetable to return some enterprises to the private sector and to abolish others, owing to the lack of suitable takers. In other instances, they were seeking advice from the World Bank or from other sources. After talking with the Minister of Finance, he was confident that action in that area would be taken soon. In response to Mr. Erb's comment on the burden of the public enterprises on the budget, even if all enterprises were either returned to the private sector or closed, the budget would still have to support the inherited debt burden for many years. Solutions to the Togolese debt problem could not be found through the Paris or London Clubs.

Some Executive Directors had suggested that because Togo had been classified as a least developed nation it might receive additional concessional aid from donor countries, Mr. Alfidja recalled. His authorities were more cautious in that respect. A number of countries with the status of least developed nation had not yet experienced improved flows of concessional aid. The availability of concessional aid was limited, and the Executive Board should not assume that such aid would be forthcoming. On a related point, Togo had not received favorable debt rescheduling terms merely because of its status as a least developed country.

He agreed with Executive Directors that Togo's medium-term prospects were somber, Mr. Alfidja said. If there were an improvement in the world economic situation, Togo's terms of trade could also improve. Furthermore, Togo's financial situation would not be as strained as it was, had the country not been obliged to provide up to one year's credit in order to export its phosphate to some countries. However, some progress in that respect had been made in the previous few months. Finally, the fall in revenues had occurred, in part, because of low activity not only in Togo but in neighboring countries, and, in part, because of the reduced volume of exports.

The Executive Board then took the following decision:

Review Under Stand-By Arrangement

1. Togo has reviewed the progress of the program with the Fund in accordance with paragraph 4(b) of the stand-by arrangement for Togo (EBS/83/30, Sup. 1, 3/7/83) and paragraph 15 of the letter of the Minister of Economy and Finance dated January 20, 1983, attached thereto.

2. The letter dated August 4, 1983 from the Minister of Economy and Finance shall be attached to the stand-by arrangement for Togo, and the letter from the Minister of Economy and Finance dated January 20, 1983 shall be read as supplemented and modified by the letter of August 4, 1983. The Fund finds that no further understandings on any changes in performance criteria are necessary.

Decision No. 7514-(83/130), adopted
September 6, 1983

2. BENIN - 1983 ARTICLE IV CONSULTATION

The Executive Directors considered the staff report for the 1983 Article IV consultation with Benin (SM/83/149, 6/30/83; and Cor. 1, 8/8/83). They also had before them a report on recent economic developments in Benin (SM/83/179, 8/12/83).

Mr. Alfidja made the following statement:

The performance of Benin's economy during the four years 1979-82 has generally been satisfactory. An annual average real growth in GDP of about 6 percent was recorded, with a deceleration trend noted toward the end of the period. The contribution to real economic growth originated mainly from increased activity in commerce in 1980, construction in 1981, and agriculture in 1982. The implementation of projects such as the oil refinery, the sugar and cement plants, and the extension of the Cotonou port have contributed to the expansion of total output, particularly in the construction sector. It is to be noted that the deceleration in overall economic activity, except in the agricultural sector in 1982 was largely a reflection of the completion of the aforementioned major investment projects.

In order to avoid a further slowdown in economic activity in the medium term, the Beninese authorities have prepared a Five-Year Development Plan for 1983-87 following the implementation of the 1978-80 Development Plan and two interim plans for 1981 and 1982. The new Plan places emphasis on the development of the agricultural sector with the dual view of achieving self-sufficiency in domestic food supplies and creating a surplus for exports to the food deficit markets within the ECOWAS region. To this end, increased efforts will be made to improve agricultural production methods as well as input supplies.

In the area of prices and income, the authorities will continue to pursue their objective of achieving a sustained income growth along with a low rate of inflation. They will continue to follow their system of fixing profit margins in such a way as to ensure sufficient and steady supplies of foodstuffs and basic essential consumer goods at relatively stable prices.

The fiscal performance in Benin has been characterized by a substantial imbalance between revenue and expenditure that has led to the overall government deficit exceeding the equivalent of 10 percent of GDP each year during 1980-82, compared with 4 percent in 1979. Although the deterioration in the financial operations of the Central Government stemmed almost entirely from the implementation of the aforementioned development projects, the Beninese authorities are concerned and intend to pursue a policy of restraint in the future. In the course of preparing and executing the budget, they will be guided by the actual instead of the projected rate and amount of revenue collections. In particular, at the beginning of each year, virtually all outlays, except for wages and salaries payments, are blocked. Authorizations to undertake these nonwage outlays are granted only when revenue becomes available to meet them. As regards investment expenditure, my authorities recognize the need to prepare realistic estimates and to undertake an expeditious implementation of the relevant projects. For 1983, the overall fiscal deficit is projected to decline rather sharply from 21 percent of GDP in 1982 to 7 percent, reflecting the completion of the major development projects as well as the effects of tighter expenditure control measures. On the whole, the Beninese authorities share the staff view that the budgetary process needs to be improved.

In monetary policy, the Government intends to pursue a more restrained course. Indeed, following a relatively expansionary credit policy in 1982 which was dictated by the demands of expanding domestic economic activity in both the public enterprises and the private commercial sector, the authorities have reverted to a more restrictive policy stance in 1983. In this context, the rate of expansion of domestic credit is expected to slow down substantially from 42 percent in 1982 to 12 percent in 1983, on account of a lower rate of activity in the private sector; the volume of credit to the Government remaining broadly the same in 1982 and 1983 at CFAF 11-12 billion.

Concerning interest rate policy, my authorities do not fully share the views expressed by the staff. However, the staff's proposals will be re-examined at the appropriate time in the context of Benin's membership of the West African Monetary Union (WAMU).

In the external sector, in recent years, Benin's terms of trade have steadily deteriorated, a development that has adversely affected the current account position, which worsened from about 14 percent of GDP in 1981 to 24 percent in 1982. This development was also due to the increase in imports of capital goods for the major projects. Staff projections show that the current account position will improve to the equivalent of 8 percent of GDP in 1983, largely as a result of a 64 percent drop in imports.

Finally, it is to be noted that the absence of a centralized statistical system and, hence, of coherent and reliable data has created in some instances difficulties for making a comprehensive evaluation of the country's economic performance and for formulating and implementing appropriate economic and financial policies. My authorities are cognizant of these problems and intend to take appropriate measures. They have created a unit (Comité de Conjoncture), which is to form the basis for establishing a permanent secretariat to centralize and coordinate economic planning and statistical information from the relevant public organizations. They intend to ensure that this initial step leads to a substantial improvement in the organization of coherent and consistent statistical framework for economic and financial decision making in Benin.

Mr. Blandin welcomed the Article IV consultation with Benin, particularly since nearly two years had elapsed since the previous consultation in October 1981. He strongly endorsed the staff view that improvements in the statistical system were required; he wondered whether the Fund would be assisting the authorities in that respect by providing technical assistance. A reliable statistical system would enable the authorities to monitor their economic and financial policies.

The Beninese economy was highly dependent on external factors, Mr. Blandin remarked. In the agricultural sector, prices, production, and exports were greatly influenced by developments in the region. The commercial sector was also characterized by high dependency, since the bulk of exports were ultimately directed to Nigeria and, to a lesser extent, Niger. Furthermore, 75 percent of budget receipts came from customs duties. In the industrial sector, two of the three projects were joint ventures with Nigeria. In addition, the port extension had been initiated because of the projected increase in traffic with Nigeria. It was not surprising, therefore, that the Beninese economy had been affected by the difficulties in Nigeria. The three industrial projects had been financed almost exclusively through foreign sources, and the corresponding increase in foreign debt servicing requirements had had a detrimental effect on the economy.

Re-exports had declined together with budget receipts, and, in 1982, the overall public sector deficit had soared to an unsustainable level of 21 percent of GDP, Mr. Blandin went on. Even though such a figure should be considered with caution as the exact amount of GDP was unknown, the absolute level of the public sector deficit was itself significant. However, the situation seemed to have improved somewhat since the beginning of 1983 with the completion of the large development projects, which had reduced the pressure on the public sector. Nevertheless, the existing financial imbalances still called for vigorous action to bring the economy back on track. Sustainable growth in the medium term would not be achieved as long as gross domestic savings remained negative, as they had since 1980. Adjustment was all the more necessary now that it was evident that the three industrial projects would not generate the foreign exchange required to repay the loans by which they had been financed. Consequently, the debt service ratio, which had remained low until 1982, would rise abruptly to 30 percent in 1984 and might stay at that level for a number of years, putting a heavy strain on the balance of payments. The authorities were well aware of the difficult economic situation, and he was confident that they would take the necessary steps to achieve more autonomous development.

The emphasis on the agricultural sector in the 1983-87 Development Plan was commendable, Mr. Blandin remarked. A number of foreign agencies, including the World Bank, were already active in that sector, but there was a need for increased coordination between the various aid donors. Measures had been taken to improve the financial position of the public enterprises, but much remained to be done if those enterprises were to provide a source of savings.

As for fiscal policy, it would be appropriate to enlarge the tax base so that revenues would be less dependent on income tax and customs duties, Mr. Blandin said. On the expenditure side, it would be unwise to continue hiring all the university graduates into the public sector as such a policy would create an unsustainable burden on the budget. He wondered whether the authorities would request the use of Fund resources to support their adjustment efforts. It was regrettable that the next Article IV consultation would not take place before March 1985, and he recommended that the date should be advanced.

Mr. Mtei indicated his support for the proposed decision and his agreement with the staff appraisal. The Beninese economy had performed relatively well in the past, reflecting the uranium boom in Niger and the oil boom in Nigeria. But recently the economy had suffered a serious setback as those neighboring countries had experienced economic difficulties due to the reduction in world demand for their exports. Real growth in GDP had fallen to half the rate achieved during the previous two years. The overall fiscal deficit had risen sharply, and the public sector deficit was provisionally estimated to have more than doubled to the equivalent of 21 percent of GDP. A substantial part of economic performance had not been considered in the staff analysis because of the inadequate availability of official data. Would the uncollected data have provided a more positive view of developments in Benin? He agreed with the staff that the authorities should improve their economic monitoring and statistical systems.

There was little hope that a uranium or oil boom would occur in the near future, Mr. Mtei commented. The authorities should therefore be more innovative in finding alternative ways to achieve economic development. He welcomed projections that one million barrels of oil would be produced in 1983 and that cement production would reach near-maximum capacity in the future. However, much more needed to be done, particularly if there were a drought in the 1983/84 season, causing a serious shortfall in agricultural production. The emphasis in the 1983-87 Development Plan on agriculture and agriculture-related industries was a welcome sign of the authorities' efforts to broaden the economic base.

On fiscal policy, while an improvement in tax collection could increase revenues, it was probably more urgent for the authorities to prepare reliable revenue estimates, Mr. Mtei considered. He welcomed the restraint on expenditure, but stressed that realistic estimates would be necessary in that area as well.

As for monetary policy, the interest rate action recommended by the staff would be difficult to achieve, Mr. Mtei remarked. Benin was a member of a monetary union, so that it was difficult for the authorities to take action independently of the other members, particularly since the CFA franc was adjusted in line with the French franc. The recent establishment of coordination committees and the staff recommendations regarding interministerial committees were welcome. The Beninese authorities had always had a positive approach to the country's economic problems, and lately they had displayed considerable interest in and responsiveness to World Bank assistance, which he hoped would yield fruitful results.

The staff representative from the African Department explained, with regard to statistical inadequacies, that a major proportion of Benin's exports had not been recorded. Estimates of unrecorded re-exports could be made on the basis of export data from Benin's supplier countries. It was, however, difficult to estimate exports of local products--in particular, agricultural products--to Nigeria. Furthermore, much of the expected agricultural production might have been effectively included in the figures for GDP. Although no major agricultural census had yet been carried out, the authorities had drawn up plans for which they were seeking financial support. He was confident, however, that there had been a slowdown in production in 1982 and 1983, as indicated by the staff estimates, even if there remained considerable doubt about the levels of GDP, imports, exports, and other economic aggregates quoted in the paper.

The staff had also had considerable difficulty in determining capital flows, the staff representative said. There was a significant parallel currency market in Benin, in particular for the Nigerian naira, and there was no way of recording or estimating transactions--either trade or financial--through that market.

In his statement, Mr. Blandin had suggested that the Fund should provide technical assistance for improving Benin's economic monitoring and statistical system, the staff representative from the African Department recalled. The Fund had already provided technical assistance in compiling government statistics. There were other sources of assistance available to Benin; the European Communities were providing assistance with trade data, and the United Nations was providing assistance in other areas. But it was the staff's view that one of the major problems was the failure of the authorities to give priority to the statistical problem or to coordinate external assistance. The staff had made some proposals and, according to Mr. Alfidja's statement, the authorities were beginning to take action along the appropriate lines.

The Deputy Director from the Exchange and Trade Relations Department stated that the staff had recommended that the next Article IV consultation with Benin should be conducted before March 1985, which would put Benin on an 18-month cycle. It had not meant to imply that there would be no contact with Benin. Clearly, there would need to be further contact on the matter of technical assistance and, if the Executive Board considered it desirable, the staff would hold an earlier consultation with the authorities.

The Chairman commented that in the case of countries with particular adjustment problems, Article IV consultations were generally held on a 12-month to 15-month cycle. It would be preferable to hold an Article IV consultation with Benin before the end of 1984.

Mr. Alfidja stated that the Executive Board should not take any final decision at the present meeting on the date of the next Article IV consultation with Benin, because it was a matter that should be considered by the Fund management and the Beninese authorities. He agreed with the Chairman's suggestion of putting Benin on a 15-month cycle for Article IV consultations. In addition, he would urge his authorities to begin discussions with the staff concerning the use of Fund resources.

His authorities agreed that the Beninese economy was highly dependent on, and had strong ties with, Niger, Nigeria, and Togo, Mr. Alfidja noted. However, they considered that the staff had not stressed enough the projects that had been undertaken to increase exports to countries other than Nigeria and Niger. Regarding flows of capital between Benin and Nigeria, although the Beninese were investing outside the country, the authorities did not believe that investment was directed toward Nigeria. There was no doubt, however, that Nigerians were investing in Benin.

The Chairman made the following summing up:

Executive Directors noted that, following a period of strong growth, economic activity in Benin weakened considerably in 1982 and 1983. They agreed with the staff's view that the Beninese economy faced serious problems in the near and medium term and that the authorities should take resolute measures, particularly to reduce the fiscal and external imbalances.

They noted that the substantial external bororwing by Benin since 1979 on harder terms had increased sharply the vulnerability of the economy to adverse external developments.

Directors believed that the main orientation of the new plan, with its emphasis on developing agriculture and agroindustry, were in the right direction. They emphasized the critical role of appropriate price policies in improving incentives and ensuring optimum allocation of scarce resources.

They commended the authorities on the recent measures taken to reform the public enterprise sector. They stressed the need for improved control of budget expenditure, including more cautious personnel recruitment, the need for measures to strengthen the tax base and improve revenue collection.

Finally, they supported the staff's view on the need to improve Benin's economic monitoring and statistical system, for which the Fund could provide technical assistance, in order to provide policymakers with a coherent and consistent framework and structure for the necessary and difficult decisions ahead.

It is expected that the next Article IV consultation with Benin will be held before the end of 1984.

The Executive Board then took the following decision:

Decision Concluding 1983 Article XIV Consultation

1. The Fund takes this decision in concluding the 1983 Article XIV consultation with Benin, in light of the 1983 Article IV consultation with Benin conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. The Fund notes with satisfaction that Benin continues to maintain an exchange system which is free of restrictions on payments and transfers for current international transactions.

Decision No. 7515-(83/130), adopted
September 6, 1983

3. COMPENSATORY FINANCING FACILITY - REQUIREMENT OF COOPERATION

The Executive Directors considered a text, put forward by the staff, interpreting the requirement of cooperation under the compensatory financing facility for drawings above or below 50 percent of quota (EBS/83/171, 8/12/83).

Mr. Polak stated that his authorities strongly supported the maintenance of the compensatory financing facility, which had been introduced so that members could rely on the Fund's resources on a temporary basis and would not have to hold such a high level of reserves. It was true, as Mr. Erb had said a few weeks previously, that some part of export fluctuations was foreseeable, but he did not agree that the cooperative function of the Fund should be abolished and that members should ensure that they held a commensurately larger amount of reserves.

Compensatory financing should be available promptly, and, therefore, drawings under the facility should not normally be subject to special conditions, Mr. Polak considered. However, when a country was also facing structural problems causing more lasting balance of payments difficulties, it would be difficult for the member to repay the Fund unless it tackled the other problems. The Fund's resources were extremely limited, and it would, therefore, be advisable to concentrate resources available under the compensatory financing facility on the most deserving cases: those countries experiencing purely an export shortfall and those of the other cases where the member was prepared to tackle its more general payments problems. He could therefore go along with the thrust of the staff's suggestion that when a member's problem was not simply that of an export shortfall, access to the compensatory financing facility, even below 50 percent of quota, should require some demonstration that the member was ready to face its other balance of payments problems. However, the implementation of that principle in the way proposed by the staff did not give the member enough certainty of prompt assistance.

He was concerned about two points in particular, Mr. Polak went on. First, the existing policies of almost any member were, to some degree, deficient, and therefore a member pursuing "deficient policies" should not necessarily be required to take special action before making a drawing under the compensatory financing facility. Second, there was the risk of a disagreement between the Fund and a member country as to whether the member's actions did or did not "give a reasonable assurance that the policies needed for the balance of payments will be adopted." The text should be amended. The word "seriously" should be inserted before "deficient" in the text on drawings below 50 percent of quota. The word "actions" would be better stated in the singular and described as constituting "a significant first step toward the correction of the balance of payments." Finally, he would replace "management" by "the Fund" for consistency with the language of the compensatory financing facility decision.

It might be desirable to state what the Fund expected of the member country more directly, Mr. Polak continued; the change could be made on the occasion of a future amendment of the decision. A final suggestion would be to eliminate the words "demonstrate its good faith by" and state instead that "management will expect the member to take action."

With respect to drawings above 50 percent of quota, he supported the text put forward by the staff, Mr. Polak indicated. Conditionality for drawings in the upper 50 percent of quota under the compensatory financing facility was similar to the conditionality applied to the upper credit tranches. He would suggest, however, that the word "broadly" should be inserted before "satisfactory" on line 9, so that it would be clear that absolutely satisfactory performance was not required in all cases.

Mr. Nimatallah said that he had been disturbed by the recent trend toward increasing the conditionality of the compensatory financing facility, particularly for drawings below 50 percent of quota. There should be a clear distinction in the test of cooperation between drawings below and above 50 percent of quota. The staff's interpretation of cooperation in the lower 50 percent of quota was too strict; a more lenient approach was vital in order in ensure quick disbursement of resources under that facility. He suggested the following alternative to the text proposed by the staff:

> Where management considers that the existing policies of the member in dealing with its balance of payments difficulties are seriously deficient or where the country's record of regular consultation with the Fund has been unsatisfactory, management will expect the member to demonstrate its willingness to consider, and when possible take, approppriate measures designed to correct its payments imbalance.

Mr. Joyce remarked that he could support most of the suggestions put forward by Mr. Polak. However, his thinking was more in line with Mr. Nimatallah's proposal. He agreed that the staff interpretation of the requirement of cooperation for requests below 50 percent of quota was too strict. The distinction between drawings in the lower and upper 50 percent of quota was difficult to determine from the proposed wording. For drawings of less than 50 percent of quota, it was too extreme to insist that action should be taken prior to making the request, even if a country was pursuing seriously deficient policies or if its record of cooperation had been unsatisfactory. In order to maintain the quick-disbursing nature of the facility, the Executive Board should not restrict access unduly in the lower 50 percent of quota.

As to drawings in the upper 50 percent of quota, he could accept Mr. Polak's suggestions, Mr. Joyce stated. He welcomed the inclusion of the sentence that "the existence or the conclusion of an arrangement is not a prerequisite." His authorities believed that most, if not all, drawings in the upper 50 percent of quota under the compensatory financing facility should be accompanied by a Fund program, but the Fund should make it clear that such a program was not mandatory.

Mr. Robalino remarked that he could not agree with the staff's proposal, which implied a far-reaching change in policy. In the past, the Executive Board had had a simple criterion defining the requirement of cooperation under the compensatory financing facility. For drawings below 50 percent of quota, the Fund had to be satisfied that the member country would cooperate with the Fund. The previous record of cooperation was not important. Rather, the Fund should be concerned about the credibility of a member's promise to cooperate in the future. The staff proposed that drawings below 50 percent of quota should be subject to the same requirement of cooperation as drawings in the upper 50 percent of quota, namely, that the member should take prior action before requesting compensatory financing. In other words, the member country had to have already cooperated with the Fund in order to prove that it would cooperate in the future. By introducing that requirement, the staff was assuming that the authorities had been uncooperative when, in fact, there might only have been a difference of opinion between the member and the Fund. Although Mr. Polak's proposal did not change his basic position, he would need more time to examine it closely.

Mr. Conrado commented that, like previous speakers, he could not agree with the staff interpretation of the requirement of cooperation, which confirmed his belief that the staff wished to increase conditionality. There was no argument to support the view that the requirement of prior action was in line with present Fund policies. For drawings below 50 percent of quota, the benefit of the doubt should be given to the member country, and he could not accept any proposal that required the authorities to take action prior to requesting compensatory financing. However, he could support the staff's interpretation of the requirement of cooperation for drawings above 50 percent of quota. He would consider the alternatives suggested by Mr. Polak and Mr. Nimatallah, although he was not yet fully satisfied with either of them.

Mr. Reddy stated that he regretted the tightening of conditionality that was implicit in the staff interpretation of the test of cooperation. There was no difference in the requirement of cooperation for drawings either below or above 50 percent of quota; in either case, members would be required to undertake corrective measures if their policies were inappropriate, before drawing under the facility.

As for the proposed text for purchases below 50 percent of quota, he was concerned that the last sentence was a distortion of Decision No. 6224-(79/135), according to which the test of cooperation was met so long as the Fund was satisfied that the member would cooperate in an effort to find solutions to its balance of payments problems, Mr. Reddy went on. The staff had suggested that in all cases where the member country was pursuing inappropriate policies, the request for a drawing should not be considered until corrective measures had been taken by the authorities. He rejected the staff's proposal since it was not the correct interpretation of paragraph 2 of the earlier decision on the test of cooperation.

He supported the views expressed by Mr. Polak at EBM/83/105 (7/18/83) that drawings in the lower 50 percent of quota under the compensatory financing facility should simply initiate discussions between the member and the Fund, Mr. Reddy said. He had argued that conditionality for drawings of less than 50 percent of quota should be lenient, since those drawings constituted only a small part of total drawings. He could support the alternative draft proposed by Mr. Nimatallah.

As for the requirement of cooperation for drawings greater than 50 percent of quota, he would like the proposed text to incorporate three principles, Mr. Reddy stated. First, the interpretation should make absolutely clear that no conditionality was attached to drawings under the compensatory financing facility in cases where the size of the export shortfall was approximately equal to the balance of payments deficit. Even in cases where the balance of payments deficit was slightly higher--say by 15 percent or 20 percent--the member should not be required to undertake any policy changes. Such a principle would recognize the temporary and reversible nature of the export shortfall. Although that point had been made by the staff on page 1 of EBS/83/171, it had not been considered in the proposed interpretation.

Second, in all those cases where the balance of payments deficit was substantially greater than the export shortfall, the member should not be expected to make any policy changes if existing policies were aimed at achieving export substitution and growth, and if they were likely to result in a significant improvement in the balance of payments position in the medium term, Mr. Reddy considered. Part of the balance of payments deficit could be due to policies that were intended eventually to strengthen the balance of payments position, in which case it would not be prudent for the Fund to ask member countries to change their policies. Third, conditionality was relevant only when the balance of payments deficit was large in relation to the export shortfall, where there was significant evidence of highly expansionary policies, and where the medium-term prospects for the balance of payments were not bright. Resources should then be made available on condition that the member would either enter a stand-by arrangement with the Fund or change its policies. He could not accept the staff proposal since it did not accommodate those three principles.

Mr. Schneider remarked that in view of the liquidity position of the Fund it might be necessary to restrict access to the compensatory financing facility. Nevertheless, the Fund should not be too strict in interpreting the test of cooperation under that facility. He supported the alternative draft put forward by Mr. Polak regarding drawings of less than 50 percent of quota. But he would prefer the last sentence to read, "...a reasonable assurance that the policies needed will be adopted." In addition, he had no difficulty with the suggestion put forward by Mr. Polak regarding drawings of more than 50 percent of quota.

Mr. Laske indicated his preference for the text proposed by the staff, which was a welcome attempt to interpret clearly the requirement of cooperation. However, he could also go along with Mr. Polak's amendment, although he was not clear on the difference between a "deficiency" and a "serious deficiency." Those words might pose some problems of interpretation when a request for a drawing under the compensatory financing facility was considered by the management and the staff.

Mr. Lovato said that he was in broad agreement with the staff proposal, particularly with respect to the text for drawings that were greater than 50 percent of quota. However, he had some difficulties with the proposal for drawings that were less than 50 percent of quota. The semiautomatic character of the facility should be preserved, and in that respect he would support an amendment of the last sentence as suggested by Mr. Polak.

Mr. Morrell commented that the view of his chair on the issue of cooperation had been indicated at length at EBM/82/39 (4/2/82). He fully supported the original objective of the compensatory financing facility, which was to provide quick financial assistance to members suffering from balance of payments difficulties arising from an export shortfall that was temporary and largely attributable to circumstances beyond the member's control. It was most important that those essential characteristics of the facility would be retained. He supported the amendments to the staff proposal suggested by Mr. Polak.

Mr. Erb considered that the staff report had been useful; it had provided not only an interpretation of conditionality associated with compensatory financing facility, but also an introductory background that demonstrated clearly the problems associated with the test of cooperation, particularly when the export shortfall was embedded in a larger balance of payments maladjustment. The whole issue was linked to the basic requirement of the Articles of Agreement that the Fund should safeguard the temporary character of its resources. It was therefore important to have clear criteria on how the test of cooperation should be interpreted when the overall balance of payments deficit was larger than the export shortfall.

He supported the staff proposal on the requirement of cooperation for drawings both below and above 50 percent of quota, Mr. Erb went on. In the text regarding drawings in the upper 50 percent of quota, he would have preferred the staff to state that a Fund program would "normally" be considered as providing evidence of cooperation. He agreed with the statement that "the existence or the adoption of an arrangement is not a prerequisite" if it was clear that the economic policies pursued by the authorities would also address the overall balance of payments problem.

A member country usually had a period of three to five years in which to repay the Fund, Mr. Erb observed. However, a country utilizing the early drawing procedure might be required to repurchase in a much shorter period of time if the export shortfall based on actual data was lower than the compensated amount. In such cases, the application of the requirement of cooperation would have to be stricter since the repurchase period was shorter. With that one qualification, he could go along with the staff proposal.

With respect to Mr. Polak's suggested language, he had a problem with the inclusion of "seriously" because it did not stress enough the need for the Fund to be reasonably assured that the country would deal with the overall balance of payments problem within the period that was normally expected when the use of Fund resources was involved, Mr. Erb explained. Finally, he could go along with the other changes suggested by Mr. Polak.

Mr. Taylor considered that it was important to clarify the meaning of cooperation in relation to the compensatory financing facility, and that the Executive Board should be willing to offer more guidance in that respect. He could generally endorse the text proposed by the staff for drawings below and above 50 percent of quota. He did not favor Mr. Nimatallah's less precise formulation, but he could support Mr. Polak's suggestion, although he would prefer the word "seriously" to be omitted and the staff's wording of the last sentence in the text on drawings below 50 percent of quota to be retained. With regard to the text for drawings of more than 50 percent of quota, he suggested that the word "actions" be used in the singular. In addition, it would be preferable to refer to the "adoption" of an arrangement rather than the "conclusion" of an arrangement.

More generally, it was worth bearing in mind, in view of some of the doubts expressed by Directors at EBM/83/127 (8/31/83), that the two-tier system for drawings under the compensatory financing facility had been implemented successfully, Mr. Taylor observed. If demands on the compensatory financing facility began to exceed the availability of resources, it might be necessary to restrict access, although he hoped that such a restriction would not occur. A progressive recovery in commodity prices could lead to declining demand for resources under the facility. Mr. Erb had suggested that the requirement of cooperation might oblige members to anticipate a cyclical trough in years of buoyant export earnings. A study of those more general observations would be useful.

Mr. Salehkhou stated that he had supported the discussion of the paper on the requirement of cooperation under the compensatory financing facility as a separate issue from the policy on access. The scheduling of the discussion before the Annual Meetings was hardly justified, particularly because the paper was presented primarily to provide information and did not require the Executive Board to take a formal decision. More important, although the staff's interpretation was supposedly based on actual procedures and practices, it implicitly introduced extra elements of conditionality that went beyond previous guidelines for the use of compensatory financing. He was especially concerned about the staff's proposal that, for drawings of less than 50 percent of quota, a member should demonstrate its good faith by taking action prior to submission of its request. The staff interpretation should not be regarded as general Fund policy on the requirement of cooperation. If the staff proposal were approved by the Board, it would confirm and strengthen the undesirable trend recently introduced that aimed at integrating drawings under the compensatory financing facility with credit tranche transactions and also at stripping the special facilities of their intended purpose and unique character, namely, to provide additional and timely assistance in cases of emergency.

Mr. Alhaimus recalled that a similar attempt to codify practice with respect to the test of cooperation under the compensatory financing facility had been discussed by the Board in April 1982 (EBM/82/42, 4/5/82). At that time, strong views had been expressed by some Executive Directors against such codification in light of the flexibility needed in applying the test of cooperation, as well as the absence of major difficulties in previous applications of the test.

The new interpretation proposed by the saff in its paper (EBS/83/171, 8/12/83) did not seem to be totally reconcilable with the spirit of the decision. For example, in the case of purchases of less than 50 percent of quota, the decision stated that the Fund should be satisfied that "the member will cooperate with the Fund in an effort to find, where required, an appropriate solution for its balance of payments difficulties." That willingness-to-cooperate criterion had been interpreted by the staff to mean that actions should be taken by the member prior to the submission of a request for the purchase. The requirement of prior action introduced a complicating element that was not in line with members' expectations of timely assistance. Furthermore, it constituted a hardening of conditionality. Instead of prior actions, the Fund should be satisfied with reasonable assurances submitted by the member concerned. Another useful improvement was that those assurances should be called for when members' policies were not simply deficient, but seriously deficient, and when their record of cooperation in the recent past had been unsatisfactory. Of the alternative wording suggested, Mr. Nimatallah's draft was more helpful.

For drawings of greater than 50 percent of quota under the compensatory financing facility, the staff had noted that, in the absence of a Fund program, the test of cooperation would be satisfied if the country had met the criteria for the use of resources in the credit tranches, Mr. Alhaimus observed. Could the staff clarify which credit tranche it was referring to, as the proposed draft might also include the first credit tranche? Aside from that ambiguity, the explicit association made by the staff between the criteria governing the special facilities and those governing the more conditional facilities was not in conformity with the flexibility required of management in making judgment on a case-by-case basis. Members might follow viable adjustment courses that did not necessarily conform to Fund practice.

Mr. Hirao indicated that his first preference was for the staff interpretation of the requirement of cooperation. However, Mr. Polak's suggestion was an acceptable modification, although he was unsure about inserting the word "seriously" before the word "deficient."

Mr. Mtei stated that, like some other Directors, he was concerned about the staff's restrictive interpretation of the requirement of cooperation under the compensatory financing facility. The quick-disbursing character of that facility should be preserved. He agreed that in principle, when making a purchase, a member should cooperate with the Fund in order to find solutions to its balance of payments problems. However, it would be wrong to use the test of cooperation to make the compensatory financing facility more conditional.

Was it the staff's view that a member should be required to take corrective action prior to making a purchase of less than 50 percent of quota, Mr. Mtei inquired? If so, that interpretation was very restrictive and he could not support it. The authorities' stated intentions to undertake policies to improve the balance of payments position should be sufficient assurance. Experience demonstrated that the compensatory financing facility had functioned more or less successfully thus far, and he saw no reason to increase conditionality.

In sum, once the staff verified that the balance of payments problem had been caused by a temporary export shortfall due to circumstances beyond the member's control, the authorities should receive assistance--of up to 50 percent of quota--from the Fund without delay, Mr. Mtei went on. For drawings in the upper 50 percent of quota, the Fund had to be satisfied that the member's policies were appropriate to solve its balance of payments problems. However, the adoption of a stand-by or extended arrangement should not be a prerequisite. The compensatory financing facility was intended to meet a special balance of payments problem, and any restrictive interpretation of the decision was not compatible with that basic feature.

Mr. Blandin stated that he welcomed the staff's reaffirmation that the conclusion of an arrangement was not a prerequisite for drawing under the compensatory financing facility. However, he was less pleased with the staff's implication that the member would be required to implement policies typical of those recommended by the Fund under a stand-by arrangement. The staff had conveniently left unclear the criteria for using resources in the lower 50 percent of quota under the compensatory financing facility, and he would be surprised if the application of the requirement of cooperation, in practice, would make any difference to the use of the facility. He could support the draft amendment proposed by Mr. Polak; it represented a substantial improvement over the staff's proposal. He was also quite attracted by Mr. Nimatallah's suggestion.

Mr. Lindå indicated his support for the staff proposal and for Mr. Polak's amendments.

Mr. Malhotra commented that the staff's interpretation of the test of cooperation under the compensatory financing facility, especially with regard to drawings of less than 50 percent of quota, represented a serious departure from the initial decision on that facility. The draft text proposed by the staff was therefore totally unacceptable to his chair. It was unfortunate that at a time when a large number of countries--in particular, exporters of primary products--were experiencing considerable strains on their economies due to sluggish export markets, the Fund was responding negatively to their needs. Given the difficult world economic situation, there was a case for further liberalization of the compensatory financing facility.

So far, that facility had operated successfully, primarily because the Fund had been flexible in interpreting existing guidelines, Mr. Malhotra said. He was concerned about the wording proposed by the staff. It suggested that the Fund was drafting a new law. With regard to drawings below 50 percent of quota, the original decision had stated that a member should indicate its willingness to cooperate with the Fund. For the drawings in the upper 50 percent of quota, the decision required that the country concerned should have been cooperating with the Fund. That wording had been deliberately adopted. The staff's interpretation had converted "will cooperate" into "has been cooperating." In other words, the issue of cooperation was the same for drawings both below and above 50 percent of quota. If the staff's interpretation were adopted, the facility would be seriously curtailed. If the objective was to change the nature of the facility, then the Executive Board should be discussing that matter openly rather than undermining the facility through interpretations that were not compatible with earlier decisions.

The changes proposed by Mr. Polak were in line with the staff's interpretation, Mr. Malhotra considered. Essentially, Mr. Polak had proposed that a country had to have introduced measures before making a request for compensatory financing. Such a requirement was bound to detract seriously from the quick-disbursing character of the compensatory financing facility. The Fund should continue to consider requests for drawings of up to 50 percent of quota according to the present guidelines, namely, that a member should be prepared to receive a Fund mission and to discuss seriously with the Fund its balance of payments difficulties so that the staff could advise the authorities on appropriate policies.

Mr. Nimatallah's draft was more helpful than the one provided by Mr. Polak, Mr. Malhotra commented. In his view, one of the chief merits of Mr. Nimatallah's draft was the loose wording of the text. Even so, he had reservations with regard to the reference to the requirement that action should be taken by a member prior to its request for compensatory financing.

It was an unfortunate time to announce to the world--especially the developing world--that access to the compensatory financing facility was going to be restricted, Mr. Malhotra considered. He hoped that the Executive Board would agree that there was no need to take a decision at the present meeting.

He appreciated that a stricter test of cooperation was necesary for drawings of more than 50 percent of quota, Mr. Malhotra said. However, in the recent past, it was likely that the staff had been insisting that, to make a drawing in the upper 50 percent of quota, the authorities had to have implemented an adjustment program. Such a requirement should not be a precondition. Furthermore, it was also inappropriate to insist that, in cases where a Fund program had not been requested or agreed, a country should have adopted policies that would be the same as those required under a stand-by or extended arrangement. A more flexible approach was necessary; the Executive Board should not forget that it was dealing with cases in which the deterioration in the balance of payments was due to exogenous factors. Approval for a request would only be given if the shortfall in exports was considered to be reversible. Therefore, it would seriously damage the compensatory financing facility to insist that a country should take action prior to making a request.

In his statement, Mr. Taylor had remarked as an aside that the two-tier system of the compensatory financing facility had been working well, Mr. Malhotra recalled. In his view, that system was not functioning well, as the conditions for drawings in the upper 50 percent of quota under the compensatory financing facility were becoming indistinguishable from the conditions attached to drawings in the credit tranches. He did not share Mr. Taylor's view that a two-tier system would be appropriate for access to the enlarged access policy.

Mr. Alfidja remarked that he was concerned about the staff approach to the requirement of cooperation under the compensatory financing facility. He shared the views of Mr. Mtei and Mr. Alhaimus, and agreed with Mr. Malhotra that no decision should be taken at the present meeting.

Mr. Zhang stated that the present practice should be continued for drawings below and above 50 percent of quota under the compensatory financing facility. Was the Executive Board supposed to take a formal decision on the issue at the present meeting, or would it not include the matter in the report to the Interim Committee?

Mr. Costa said that he did not support the proposed decision on access to the compensatory financing facility.

The Director of the Exchange and Trade Relations Department considered that the range of comments made by Executive Directors reflected policy differences to a large extent. In the staff's draft, the word "tranches" did include the upper tranches. The staff would regard the inclusion of the word "seriously" as acceptable; obviously, the staff had intended to imply that prior action would be required only when existing policies had reached a certain stage of seriousness.

The issue of the requirement of cooperation under the compensatory financing facility had been raised in connection with the report to the Interim Committee, but the staff report (EBS/83/171) would not be given to the Interim Committee, the Director of the Exchange and Trade Relations Department stated. On another point, when writing the proposal the staff had considered the Acting Chairman's summing up at EBM/82/40 (4/2/82); he had clearly indicated that in certain cases some kind of prior action would be required. In that respect, the staff proposal was not compatible with Mr. Nimatallah's draft, which seemed to be a step back from the agreement reached at the earlier Executive Board meeting. Mr. Polak's suggestions were more acceptable to the staff, although the staff prosposal was more differentiated.

The Chairman observed that a number of Directors would prefer no change in the interpretation of the requirement of cooperation. However, other Directors--representing 55 percent of the voting power--supported the staff's interpretation as amended by Mr. Polak. If the phrase "constitutes a significant first step toward" were replaced with "give a reasonable assurance that the policies," a greater consensus could be reached. He could support the inclusion of the word "seriously." All policies were deficient in some respect, but it was when they were seriously deficient that prior action would need to be taken. However, a number of Directors would prefer to have that word left out.

Mr. Polak commented that he would be more satisfied if the word "seriously" were included, but as it was such an important issue for some Directors it might be necesary to find totally different words, such as, "...where the member's payments problems extend beyond those attributable to the shortfall." He could not accept the staff's or Mr. Nimatallah's reference to "a reasonable assurance." That wording was imprecise, and it was difficult to know what would be considered a reasonable assurance.

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/83/129 (9/2/83) and EBM/83/130 (9/6/83).

4. SEYCHELLES - 1983 ARTICLE IV CONSULTATION - POSTPONEMENT

The Executive Board notes the request contained in EBD/83/228 (8/31/83). Notwithstanding the period of three months specified in Procedure II of the document entitled "Surveillance Over Exchange Rate Policies" attached to Decision No. 5392-(77/63), adopted April 29, 1977, the Executive Board agrees to extend the period for completing the 1983 Article IV consultation with Seychelles to not later than October 14, 1983.

Decision No. 7516-(83/130), adopted
September 2, 1983

5. APPROVAL OF MINUTES

The minutes of Executive Board Meetings 83/58, 83/59, and 83/60 are approved. (EBD/83/223, 8/29/83)

Adopted September 2, 1983

APPROVED: March 2, 1984

LEO VAN HOUTVEN
Secretary