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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 83/153

10:00 a.m., November 7, 1983

W. B. Dale, Acting Chairman

Executive Directors	Alternate Executive Directors
	N. Toe, Temporary
	G. Ercel, Temporary
	X. Blandin
	C. A. Salinas, Temporary
R. D. Erb	
	S. R. Abiad, Temporary
	T. Yamashita
	I. R. Panday, Temporary
R. K. Joyce	
A. Kafka	C. Robalino
	G. Grosche
	C. P. Caranicas
	A. S. Jayawardena
	E. M. Ainley, Temporary
	T. de Vries
A. R. G. Prowse	
G. Salehkhou	
	E. I. M. Mtei
M. A. Senior	E. Portas, Temporary
	A. Linda
	T. A. Clark
Zhang Z.	

L. Van Houtven, Secretary
B. J. Owen, Assistant

Also Present

African Department: M. Sidibé. Exchange and Trade Relations Department: M. Guitian. External Relations Department: H. P. Puentes. Fiscal Affairs Department: F. L. Corfmat. Legal Department: J. V. Surr. Western Hemisphere Department: E. Wiesner, Director; S. T. Beza, Associate Director; P. Ewenczyk, J. Ferrán, Z. Hodjera, A. S. Linde, J. P. Pujol, L. M. Valdivieso. Advisors to Executive Directors: H.-S. Lee, W. Moerke, P. D. Péroz. Assistants to Executive Directors: H. Alaoui-Abdallaoui, H. A. Arias, V. Govindarajan, D. Hammann, C. M. Hull, J. M. Jones, A. K. Juusela, H. Kobayashi, G. W. K. Pickering, A. A. Scholten, S. Sornyanyontr, J. C. Williams.

1. HAITI - 1983 ARTICLE IV CONSULTATION, AND STAND-BY ARRANGEMENT

The Executive Directors considered the staff report for the 1983 Article IV consultation with Haiti and a request for a stand-by arrangement in an amount equivalent to SDR 60 million (EBS/83/222, 10/11/83). They also had before them a report on recent economic developments in Haiti (SM/83/209, 10/19/83).

Mr. Kafka made the following statement:

My Haitian authorities are in full agreement with the views expressed by the staff in the consultation report. After several years of economic and financial difficulties, my Haitian authorities in fiscal year 1981/82 adopted and began to implement an economic program supported by a 15-month stand-by arrangement with a view to attaining two basic objectives: (i) to reduce the overall deficit in the balance of payments from $55 million in 1980/81 to $25 million in 1981/82 and $10 million in 1982/83; (ii) and to reduce the public sector deficit financed by nonconcessional credit from 6.5 percent of GDP in 1980/81 to 2.5 percent of GDP in 1981/82, and to 1.5 percent of GDP in 1982/83.

Haiti's financial performance has been fully in observance of all the targets of the financial program. Central to the dramatic turnaround achieved was the authorities' decision to strengthen public finances through strict expenditure control, improved tax administration, and the introduction of new revenue measures. In this reform, Haiti enjoyed the technical assistance of the Fund. The fiscal results were even better than expected and accordingly the overall balance of payments showed a smaller deficit than targeted while the existing external payments arrears were virtually eliminated.

The new program for which the support of the Fund is requested calls for a consolidation of the goals achieved as well as a continued improvement in the financial performance of the public sector and strengthening of the international reserves of Haiti. The public sector deficit financed from nonconcessional borrowing is to be reduced further to about 0.6 percent of GDP in 1983/84. In pursuit of this target my Haitian authorities have introduced additional tax measures, including a new tax on telephone services, cable television, and mining activities, and an upward adjustment in nontax fees. They will continue strengthening the administration and management of taxes. Furthermore, technical assistance from the Fund continues to be provided in the tax area, particularly in connection with new income tax and sales tax legislation. Tight control over government expenditures will be maintained.

In the monetary field, my authorities will proceed to implement the complete separation of the National Credit Bank from the Central Bank. This will not only mean an improvement in accounting, it should also facilitate closer monitoring of credit developments and solidify the National Credit Bank as a financial intermediary. But my authorities will also continue tightening credit policies in order to complement the restraints in fiscal policy and to strengthen the balance of payments position.

My Haitian authorities are conscious that net international reserves should be strengthened, and the program before the Executive Board should make this possible. My authorities believe that the policies set forth in the program are adequate to achieve the above objectives, and they are prepared to continue cooperating with the Fund. I hope that my colleagues can give their support to Haiti's request.

Mr. Clark remarked that when Haiti's previous stand-by arrangement had been discussed in the Executive Board (EBM/82/103, 8/9/82), doubts had been expressed about the member's ability to resolve the problem of its fiscal imbalance. Those doubts had been dispelled, and the performance criteria had been met, in particular those relating to public sector finances. Welcome steps had been taken to improve revenue, the monthly monitoring and control of expenditure seemed to have worked well, and the external current account deficit had been reduced from about 11 percent to about 4.5 percent of GDP. But that being said, and recognizing that Haiti was in a peculiarly difficult position as the poorest country in the Western Hemisphere, he nevertheless had some serious concerns about the follow-on program that was proposed under the new stand-by arrangement.

He was concerned about both the substance and the presentation of the program, Mr. Clark continued. On the substance, there was an apparent lack of improvement in the external sector. Although there might be good reasons for a stabilization program extending over three years, Haiti was not burdened by a significant stock of external debt, and he wondered whether, if the momentum of adjustment had been maintained, another one-year stand-by arrangement would not have been more appropriate. Furthermore, under the proposed program, the Fund's resources would be devoted largely to building up gross reserves. Yet net international reserves would deteriorate from about minus $20 million in 1982 to about minus $40 million at the end of 1984. Total external debt, including net use of Fund resources, would continue to rise, and the debt service ratio, although remaining comparatively low, was projected almost to double between 1982 and 1986.

The issue was how far the program was helping to point the external sector of Haiti's economy in the right direction, and how well placed Haiti would be to repay the Fund when the time came, Mr. Clark added. Although the proposed stand-by would cover the period until September 1985, there were unfortunately no overall balance of payments projections for 1985. The staff projected an overall balance of payments surplus of about $8 million for 1984, which was not a particularly large surplus, compared with expected imports of $380 million and a trade deficit of $180 million. He believed that the overall external balance remained vulnerable.

During the Board discussion in 1982, his chair had asked for some analysis by the staff of the appropriateness of the exchange rate, Mr. Clark recalled. He was grateful for the effort that had been made, and particularly for Chart 1, which showed that the real effective exchange rate had fluctuated significantly over the past eight years, and that it had appreciated by 20 percent to 25 percent since 1978. The rate had most recently stood at its present level during a few months in 1976 and in 1977, when Haiti's trade deficit had been growing rapidly. He was aware that the Haitian gourde had been pegged to the U.S. dollar for many years, and that many of Haiti's exports were commodities whose prices were mostly determined in U.S. dollars. But more than 50 percent of Haiti's exports were now light manufactures, most of which were exported to the United States and to Europe. Trade competitiveness therefore mattered a great deal more than it had in the past, and a change in the exchange rate, particularly in relation to the U.S. dollar, could be expected to yield significant effects on the trade account. Comparisons with the past, when Haiti had depended much more on bauxite and when manufactures had been relatively less important, might not be the best guide to the future. He would therefore urge the authorities and the staff to consider again the appropriateness of the exchange rate. The U.K. authorities viewed the exchange rate as an important instrument in adjusting more rapidly the current account and reinforcing the process of stabilization.

On the domestic side, Mr. Clark noted that little was said in the staff paper about the impact of the program on real incomes. Consumption had fallen from about 100 percent of GDP in 1981 to 95 percent of GDP in 1983, but no further reduction was expected for 1984. Gross domestic investment was a fairly healthy 15 percent and 16 percent of GDP respectively for those two years. But again, he wondered whether some adjustment to the exchange rate might not bring about a more appropriate distribution of income and demand.

The rather thin coverage of some areas in the staff reports was a serious concern, Mr. Clark considered, especially as there had been no previous review of the 1982/83 program, nor did there appear to be any reviews planned under the proposed arrangement until the end of 1984. Since the authorities and the staff had decided to propose a two-year arrangement, he would have preferred reviews at six-month intervals, to give some indication of medium-term developments, the sustainability of the current account, and the impact of the program on the real economy.

One question not fully discussed in the staff report, Mr. Clark observed, was the level of interest rates. From the report on recent economic developments, it could be seen that lending and deposit rates in Haiti were well above Eurodollar rates, and were highly positive in real terms. Based on his remarks about the exchange rate and the need to stimulate investment in productive sectors, he wondered whether real rates might not actually be too high.

If there was indeed a strong case for a program lasting two years, he would have expected fuller projections in order to give an idea of the pattern of developments in the second year, Mr. Clark observed. Haiti's debt service payments had been projected in Table 9, but there was little indication of expected developments in 1985, and, in the absence of a mid-term review, not much would be known for another year. Consequently, he found it rather hard to come to a proper assessment of whether or not the Fund should be committing resources for two years.

In conclusion, Mr. Clark said that he doubted whether the proposed program was the best that could be designed for Haiti in the present circumstances. He wondered why the momentum of adjustment that had been maintained in 1982 and 1983 could not be sustained in 1984 and why a two-year program was being proposed.

Mr. Erb noted that the Haitian authorities had been more successful in the implementation of the program under the just completed stand-by arrangement than had been expected by most observers, including his own authorities. The performance had been impressive, but of particular importance were the substantial reduction of the public sector deficit, the reduction in the overall balance of payments deficit, accompanied by the almost total elimination of external payments arrears, and the achievement of real growth in GDP following a two-year decline. The key to success in the 1982/83 program was the strong performance of government revenue, and tight control of expenditure. It was essential that the authorities continue the effort to consolidate and strengthen public finances in the context of the proposed arrangement if the recent improvements in the underlying economic trends and international confidence in Haiti were to be maintained and enhanced.

It was because of Haiti's performance that he was prepared to support the program put before the Executive Board, Mr. Erb continued, although his authorities had some serious concerns with the arrangement, both in terms of the substance and in terms of the presentation. First, the lack of a more explicit medium-term analysis in the staff papers was extremely disturbing. In the past, his chair had been especially assertive in asking the staff, even in the context of a one-year program, for a medium-term analysis of the prospects of an economy. Such an analysis should focus in particular in Haiti's case on the future role of the Fund, and the respective roles of the World Bank, bilateral donors, and multilateral development agencies. To the extent that the Fund's financing role was phased out as envisaged, the Fund's role as a provider of information and analysis of macropolicies and trends in Haiti could be expected to take on added importance. He hoped that an enlarged role for the World Bank in Haiti would ensue from the presentation that the Haitian authorities intended to make at the time of the next meeting of the Caribbean Group for Economic Cooperation and Development, to be chaired by the World Bank. The authorities should begin to direct their efforts toward more structurally oriented policies designed to improve the supply side of the real economy. For that purpose, direct World Bank involvement in the form of structural and sectoral lending would be appropriate and desirable. It went without saying that his authorities expected close collaboration between the World Bank and the Fund as the World Bank's role in Haiti expanded.

Although he agreed with the emphasis given to strengthening the foreign reserve position of the Central Bank, Mr. Erb continued, he questioned the adequacy of the net reserve buildup during the course of the two-year program. As Mr. Clark had pointed out, it would leave Haiti with a quite significant negative net reserve position at the end of the program. The staff had commented that Haiti's gross reserve position at that time would restore the relationship to imports that had existed prior to the recent decline in the Haitian economy. The question was whether to look at net reserves or gross reserves; his feeling was that more attention also should be paid to the net reserve position. On the related matter of whether Haiti's net reserve position before the recent deterioration in the economy had been adequate, it seemed necessary to consider the criteria for setting the net reserve objective for a small economy like Haiti's in light of the contingencies that could afflict it.

He had also noted, like Mr. Clark, the virtual absence of detailed projections or targets for the second year of the two-year arrangement, Mr. Erb said. He recognized that the Haitian authorities had requested that the arrangement be for two years, but he would appreciate the staff's views on why it felt that a two-year program was appropriate.

As a general matter for consideration, Mr. Erb asked whether, when the Executive Board was requested to make a two-year commitment without having an adequate base for judging the second year of the program, it should not be made much more explicit in the decision itself that the commitment for the second or for the third year of a stand-by arrangement was highly contingent. In some cases in the past, the Board had approved a commitment for one year of a program but had at the same time understood--the understanding having been recorded in the minutes--that there was likely to be a follow-on program, thereby making an implicit commitment. But the Executive Board was being asked to make a commitment to Haiti for the second year of a program about which it knew little. He was looking for a way to avoid giving the impression that the Executive Board was in effect committing itself for a two-year period as it did for a one-year program, but in a way that went beyond an implicit commitment in the Executive Board for a follow-on program. It would seem helpful to include such a contingent commitment for a follow-on program in the decision approving a program for one year rather than putting forward a two-year program.

Mr. Panday commended the Haitian authorities for the successful implementation of the stabilization policy adopted in 1982, with support from the Fund. Looking at the strong commitment that they had shown to the adjustment program and the progress that they had achieved, he had no difficulty in supporting the request for a two-year stand-by arrangement, together with a waiver under Article V, Section 3. He agreed with the staff that the program presented by the authorities deserved the Fund's support because it was adequate to meet the need to strengthen Haiti's balance of payments and to consolidate the gains achieved so far in order to create an environment conducive to sustained growth.

He could discern the structural nature of Haiti's economic problems, Mr. Panday observed, not only in the dismal performance of public savings, which had been explicitly mentioned in the staff report, but also in the relatively low and declining level of private savings in recent years. The decline could of course be explained in part by drops in output and in income in 1981 and 1982, but inadequate financial policies and incentives to savers also seemed to have been instrumental in bringing about that unsatisfactory situation. He would like to have the staff's view on the extent to which the current financial program could be expected to address that issue.

Mr. de Vries said that he had no difficulty in supporting the proposed stand-by arrangement. Although the program might not be the best that could be designed, as Mr. Clark had suggested, it was certainly satisfactory and in general fully met the requirements of the Fund's basic policy decision. He had been impressed by the reduction in the public sector deficit, the decline in the external deficit, the resumed growth in national income, and the adoption of an effective interest rate policy. Some financial stability had been re-established, and Mr. Kafka had said that the present program was designed to consolidate the progress already achieved. He noted that Haiti had benefited from the technical assistance of the Fund on expenditure control and tax administration, practical assistance by the institution that was most helpful to member countries.

To a large extent, the stability had been achieved by demand restriction, and, while consolidation was indeed necessary, the authorities also needed to look into the medium term and longer term to see how the economic structure could be improved and incomes increased, Mr. de Vries continued. At that time, the Fund would have a smaller role and the World Bank might well have a larger one, as Mr. Erb had said. With the re-establishment of stability, it became important to take a longer view. A distinct improvement had already been achieved in the steady increase in the exports of light industry. A continued rise in exports of manufactures was projected from about 40 percent of total exports in 1979 to over 50 percent in 1984, a development that augured well for the future of the economy.

A marked appreciation of the real effective exchange rate, of about 15-20 percent from 1979 to the present, was visible in Chart 1 of EBS/83/222, Mr. de Vries observed. The staff had explained that appreciation to him as being a result of the link between the gourde and the U.S. dollar; most exports to the nondollar sector were apparently of coffee, for which there was a market price; moreover, much of the coffee went to France, and the relationship between the French franc and the U.S. dollar accounted for part of the appreciation without having much effect on exports because the coffee would be sold as long as it was available at the market price. He had not been fully reassured by that explanation, and he wondered whether certain improvements in the competitive position of Haiti might not be necessary. He would not conclude from that that the exchange rate should be changed immediately; for a country like Haiti, there was much to be said for the stability that had been established between the exchange rate of its currency and that of a large nearby neighbor. But he would not be surprised to discover minor shortcomings in Haiti's competitive position. In that case, there were some internal measures that could be taken to improve the competitive position.

A question had been raised about the appropriateness of the period for which the Fund was to commit resources to Haiti, Mr. de Vries observed. He had always felt that unless important matters of principle were involved, much weight should be given to the wishes of the member country concerned, as long as it was clearly understood that Fund resources would not become available during a period in which clear agreements with the country had not been reached. He doubted that there was any misunderstanding between the Fund and the Haitian authorities on that score.

Mr. Joyce recalled that deep concern had been expressed from his chair during the Board discussion of Haiti's previous request for a stand-by arrangement about the authorities' ability to implement the program because of what appeared to be technical weaknesses in administration. For that very reason, he was particularly pleased that Haiti had succeeded in completing the program under that stand-by arrangement, a performance that would undoubtedly color the Board's approach to the present request for a two-year stand-by arrangement.

He was broadly in agreement with the staff's analysis of recent economic developments in Haiti, Mr. Joyce continued. Among certain aspects of Haiti's economic situation that had a bearing on the request and on the Executive Board's consideration of it, there was first of all the member's record of long and continuous use of Fund resources. On the one hand, that record tended to suggest that the balance of payments difficulties were not merely temporary; on the other hand, Haiti was one of the poorest countries in the region, and the rate of increase in real GDP had barely matched the rate of increase in population. Moreover, the payments imbalances generated by the government sector and by the external sector were not particularly large. The overall balance of payments deficit stood at present at less than $6 million, compared with a deficit of $55 million in 1981. The overall fiscal deficit was 3.5 percent of GDP, compared with 5 percent in 1982. Considerable progress had thus been made, and no doubt it could be argued that there was not a strong case for a program under a further stand-by arrangement. But the facts were, first, that Haiti's financial situation was still extremely fragile; the country was heavily dependent on concessional aid, with all the uncertainties that accompanied its provision. Second, the gains made, particularly on the fiscal side, needed to be consolidated. Third, reserves were abysmally low, representing on a gross basis only about three weeks' imports. For all those reasons, he supported the program, noting that its main purpose was to replenish reserves to the level existing in the late 1970s. However, if the rebuilt reserve position was to be sustainable, the overall balance of payments would have to return to surplus, and public sector finances would have to be further strengthened. Only then would there occur the restoration of confidence needed to ensure a stable reserve position.

In addition to reducing substantially the overall public sector deficit, the authorities had introduced a number of fiscal reforms, Mr. Joyce observed. Tax collection had been strengthened and new taxes had been introduced. Yet, in congratulating the authorities for what had been achieved, he also found it necessary to remind them to remain extremely vigilant. Indeed, one of the aims of the program was to consolidate the strengthening of public finances. He had noted from Table 7 of EBS/83/222 that current Treasury outlays would increase by 12 percent between FY 1983 and FY 1984 owing mainly to an increase in maintenance costs, according to the explanation in the text. Could the staff explain the need for what seemed to be a fairly substantial increase in those costs? His concern was heightened by the fact that current Treasury outlays had in fact exceeded program targets for the past two years, which in itself indicated the need for somewhat tighter controls. The nonconcessional borrowing requirement of the Government was estimated to be only 1 percent of GDP in FY 1983, and to fall to 0.6 percent in FY 1984. Again, the high dependence on concessional external borrowing to finance the public sector deficit called for care on the part of the authorities to ensure that, at the very minimum, the timing of their budgetary outlays did not get out of step with receipts of concessional financing.

The overall stance of monetary policy appeared to be consistent with the balance of payments target, and the current interest rate structure should help to encourage domestic savings, Mr. Joyce said. The separation of the functions of the National Credit Bank from those of the Central Bank remained an important step in rationalizing monetary policy. The separation had begun in 1979, and the authorities should strive to make the changeover, which was not yet complete, as soon as possible. In addition, close monitoring of the activities of the National Credit Bank would be necessary for some time to ensure that the proposed change in lending practices did in fact lead to a reduction in the volume of nonperforming loans.

He welcomed both the progress made toward eliminating arrears and the projections for an overall balance of payments surplus of $8 million in FY 1984, Mr. Joyce stated. As for the exchange rate, he realized that differing views were possible, and that the authorities themselves apparently were not anxious to make a fundamental change in exchange rate policy. Nonetheless, despite Haiti's success in increasing its exports of manufactured goods, the question could be asked, as it had been by others, whether some devaluation of the gourde might not be appropriate to make Haitian exports more competitive in markets other than the United States. A number of external restrictions had already been removed; he hoped that that process would continue and would be accelerated as the reserve position improved.

Haiti's debt service ratio was not unduly alarming, Mr. Joyce commented. The projected increase from 10 percent in 1983 to about 16 percent in 1986 might prove to be lower if in fact Haiti were able to reschedule the large commercial debt associated with the new sugar mill. But he would register his concern that, if the rescheduling did take place, the authorities should not become unduly complacent. Standing behind those comparatively comfortable debt service ratio figures was the fact that, in a situation of great dependence on concessional aid flows, any substantial increase in commercial indebtedness could be extremely dangerous.

On the duration of the stand-by arrangement, in general there was something to be said for entering into a two-year understanding with the Haitian authorities, Mr. Joyce remarked. However, the commitment for the second year had to be premised upon good performance and indeed be subject to review at all stages. As he understood them, Mr. Erb's and Mr. Clark's concerns were not assuaged by the formal provision in the arrangement that understandings should be reached with the Fund before October 25, 1984 on the second year of the program. Their concerns derived, as did his own, from the fact that there was little sense in the staff report of the medium-term prospects and of what an appropriate medium-term policy mix for Haiti might be. To proceed with the program in a sensible way, the Executive Board would have to turn to the matter once the staff had had a chance to examine in greater detail with the authorities the medium-term prospects for the economy; it could then consider what could realistically be achieved in the second year of the program that would give grounds for belief that Haiti's position would be more sustainable after the completion of the program. He supported Mr. Clark's suggestion for a review in six months' time, which would not be too soon, because the Fund would have to reach understandings with the authorities by the end of October 1984. The staff itself might benefit from a review held well in advance of the discussions with the authorities on those understandings.

Mr. Grosche commended the Haitian authorities for having quite successfully implemented an initial stabilization program, which had been supported by the Fund with a 15-month stand-by arrangement. The overall public deficit had indeed been reduced substantially, as had the deficit on the overall balance of payments. Trade restrictions had been eased, and external payments arrears had virtually ceased to exist. All performance criteria had been met, and economic activity was showing some signs of recovery. Despite that performance, Haiti still had a long way to go toward an internal and an external balance that would be sustainable over time. Therefore, he welcomed the authorities' intention to continue policies of adjustment and to ask for another stand-by arrangement in support of their efforts.

His impression, like that of Mr. Clark and Mr. Erb, was that the new program was not sufficiently embedded in a medium-term, structurally oriented framework, Mr. Grosche noted. Considering that the new program, taken together with the previous one, would run over a three-year period, he would have expected more information about the objectives of the program over the whole period and a plan indicating how they were to be achieved. He was not asking for the standards of an extended Fund arrangement to be applied, but he would have liked, for instance, more information about the balance of payments objectives. Further analysis of the current account would have been useful, at least for 1985, since the stand-by arrangement would last until the end of that year. In 1984, the current account was expected to deteriorate further, a development that would be less worrisome if its financing through concessional flows were secured and if the resources were used for purposes of investment. Reference was made in the staff report to the projected increase in concessional assistance, but a more detailed and medium-term analysis of the overall balance of payments would have been welcome. That also held true of the development of exports, imports, and service receipts; imports in 1984 were expected to grow faster in absolute terms than exports, and the tourist balance would merely show no improvement. He would have liked a deeper analysis of Haiti's competitive position and a more fully developed rationale for apparently ruling out an adjustment of the exchange rate to remedy the external imbalance.

To conclude, Mr. Grosche remarked that even though he was not fully satisfied with the program, he could support the proposed decision, mainly for three reasons. First, Haiti's financial performance under the previous stand-by arrangement had been fully in conformity with the targets and had demonstrated the authorities' commitment. Second, the new program centered rightly on further strengthening the public finances. Third, and last, Haiti was seeking enlarged access to the Fund's resources up to only 87 percent of quota in each of the two program years. In that connection, higher amounts would have made it even more pressing to analyze the balance of payments well into the repurchase period to show that progress toward a viable balance of payments position was being achieved so that Haiti could make the repurchases without strain. He joined Mr. Clark in suggesting a review of the program in six months' time, to provide an opportunity to discuss a program for 1985 that would help to consolidate the adjustment made so far.

Mr. Portas expressed his support for Haiti's request for a two-year stand-by arrangement. It was clear from the staff paper that the results of the current financial program had been highly satisfactory. The marked improvement of the balance of payments and fiscal position, which had been better than expected, was possibly due to the forceful and timely adoption of a series of measures in several areas, particularly in controlling public expenditures strictly, improving tax administration, and obtaining new revenue. The fiscal reform, which had set the basis for continuing the process of strengthening the public finances under the new program, had been accompanied by prudent monetary and financial policies. The authorities should be commended for that effort.

The new program correctly emphasized the need to consolidate the progress already achieved in improving the public finances as a key element of continued progress toward an improved financial and balance of payments position, Mr. Portas added. The continuation of the fiscal reform would again be complemented by cautious monetary and financial policies. Of special importance would be the move to separate completely the National Credit Bank from the Central Bank, thereby improving the efficiency of the banking system.

In light of the measures already adopted and those to be carried out during the program period, Mr. Portas said, the objectives of improving the international reserve position and strengthening the public finances, as contemplated in the new program, seemed to be feasible and attainable within a two-year period. It would be extremely important that the projected financing from development agencies, as well as from donor countries on concessional terms, should materialize in order to facilitate the progress of the Haitian authorities toward a viable balance of payments position.

Mr. Prowse considered that the achievements of the Haitian authorities under the program being completed offered important reassurance about the prospects for the program proposed under the new stand-by arrangement. He believed that a two-year arrangement was appropriate for the development of the type of fiscal reform and administrative structure being planned, and he would join others in supporting Mr. Clark's suggestion for a review six months into the arrangement.

His main concerns, like those of others, Mr. Prowse continued, related mainly to the external situation. It was indeed surprising to find no real discussion in the staff report of exchange rate management policy or its effects. There was prima facie evidence in Chart 1, which showed a much higher real effective exchange rate than for a number of years, of the need for a thoroughgoing review of whether or not the rate was appropriate at present. The appropriateness of Haiti's exchange rate arrangements could be considered if a six-month review were scheduled.

The target for the balance of payments was to limit the pressure on debt service and to rebuild reserves, Mr. Prowse noted, objectives that he could support. But it was extraordinary to set those targets without an extremely thorough review of exchange rate management. Import quotas were still in widespread use, and some were even called "permanent," a practice that also provided evidence, on the face of it, that the exchange arrangements might not be very satisfactory.

He had been interested to note that the target for inflation was to maintain the current rate, Mr. Prowse went on. He wondered how easy it was to decide which rate of inflation to maintain; for instance, would the rate be the same as in the United States, or in France, where Haitian coffee was sold? Perhaps the authorities should be aiming at a different objective than merely maintaining the rate of inflation.

The proposed separation of the Central Bank from the National Credit Bank was important, and he wondered why it had taken so long to carry out, Mr. Prowse said. The staff should pay particular attention to progress in completing the separation when the program was reviewed. There were quarterly ceilings on the net domestic assets of the consolidated balance sheet of the Central Bank and the National Credit Bank, an interesting feature, if the authorities' intention was to separate the two banks as fully as possible. But there was no performance criterion for the net domestic assets of the banking system as a whole. The staff had made the point that there was a lack of experience with the operations of the National Credit Bank under the new arrangements; perhaps it would have been more difficult to formulate a performance criterion than to set a target. However, had the staff considered establishing a ceiling on net domestic assets for the banking system as a whole, and if not, why?

He had noticed with satisfaction that there were quarterly ceilings on Treasury expenditures, Mr. Prowse continued, but he had also read that it was proposed that those ceilings be adjusted upward or downward depending on the actual behavior of revenue. How mechanical would that adjustment be? It was not evident to him that expenditure should necessarily rise if revenue rose, or indeed that expenditure should in all cases fall pari passu with a fall in revenue.

Interest rates were expected to remain competitive with those prevailing abroad, according to the staff report, Mr. Prowse observed. If that meant competitive with the rate prevailing in the United States, it was not clear that the resulting rate structure would be right for the Haitian economy. Mr. Clark had already suggested that real interest rates might be too high. Gross national savings were estimated to be about 5 percent of GDP; although Haiti was not a high-income country, did the staff have in mind any course that the authorities might pursue by way of stimulating the mobilization of domestic savings?

According to the summary balance of payments projections in Table 2 of EBS/83/222, Mr. Prowse observed, exports of light manufactures were projected to increase by about 20 percent in 1984, a stepping up in the rate of growth of those exports. Evidently, much would depend on economic growth in the United States, but international competitiveness might be an important factor because many other developing economies were also seeking to increase their exports of light manufactures. With Haiti's appreciated exchange rate, the staff projection might be optimistic.

In conclusion, Mr. Prowse expressed his support for the stand-by arrangement. Haiti's program was worthwhile and was not an expensive one for the Fund to support.

Mr. Blandin said that he broadly endorsed the staff appraisal and had no real difficulty in supporting the proposed decision. Haiti was one of the poorest countries, if not the poorest country, in the world. It had a vital need to restore confidence among the financial community and to take the structural and adjustment measures that were necessary for a sustained and balanced pattern of development. A two-year stand-by arrangement with the Fund seemed to be the cornerstone of such an overall program, the more so that, after having faced some major economic and financial difficulties and experiencing difficult relations with the Fund, Haiti seemed to have been successful in meeting the objectives of the previous 15-month stand-by arrangement. That favorable momentum had to be sustained and strengthened.

The program under the proposed stand-by arrangement was broadly appropriate, Mr. Blandin remarked, although some of its features could probably have been improved at certain points. The Haitian authorities were to be commended for having taken strong action aimed at reducing the public sector deficit financed by nonconcessional credit, and the further reduction envisaged from 1.5 percent to 0.6 percent of GDP seemed realistic and appropriate. The new tax measures and the process of concentrating all public sector operations in the Central Bank also seemed appropriate.

While he had no major difficulty with the external side of the program, Mr. Blandin went on, he had to admit that it was not the program's most convincing or appealing part. That was why it seemed all important for Haiti, at a minimum, to meet all of the external objectives fully. He had no doubt at the present stage about the achievement of those objectives, not because they were insufficiently ambitious, as others had implied, but rather because they appeared fully consistent with the other aspects of the program. He would nonetheless like to suggest that the authorities--and of course the staff--should keep a close eye on the external side of the program and, should the opportunity emerge, try to exceed the present objectives.

Mr. Salinas expressed his support for Haiti's request for the use of Fund resources under a stand-by arrangement. The quite satisfactory performance of the Haitian economy under the stabilization program implemented by the authorities through September 1983 had permitted them to redress a severe deterioration of the economy by achieving a marked improvement in the fiscal position and the balance of payments. Despite the remarkable progress already made, Haiti's balance of payments position remained weak, and the fiscal situation still provided room for further improvement. Within that context, the authorities had framed a new program, for which they were requesting the Fund's support, in order to consolidate the gains made and to strengthen confidence in the economy through the restoration of an appropriate level of international reserves.

The program had been designed mainly in an effort to further reduce the overall fiscal deficit through the implementation of several fiscal reforms that would lead to a significant increase in government revenues, Mr. Salinas noted. Insofar as access by the public sector to domestic bank credit would thereby be limited, the availability of resources to the private sector would be increased, an element which, combined with an adequate interest rate structure, might encourage private activity and allow for a better allocation of resources.

The improvements already registered and those projected in the balance of payments position, as well as the elimination of arrears, might contribute to a prompt reduction in current trade restrictions and to complete freedom of exchange transactions, Mr. Salinas considered. Such a welcome development would also allow a reduction of pressures on the gourde and promote the restoration of confidence in the economy. Finally, the Government's intention to pursue a cautious external public borrowing policy, in the hope of maintaining a relatively low debt servicing ratio, was to be commended.

The staff representative from the Western Hemisphere Department noted that the Haitian authorities had requested the two-year arrangement largely to demonstrate their commitment to a continuing process of fiscal reform. They had already been making an effort in that regard for several years, but the advances had been slow at times; their intention was to pursue those efforts more vigorously over the next two years. The reforms called not only for increasing the revenues of the public sector, but also for laying the administrative foundations to ensure that the increase in revenue would be permanent and that the procedures for making expenditures become more orderly. At the same time, the Haitian authorities had indicated their firm commitment to improving the balance of payments position and strengthening international reserves. In framing the program for 1984, the authorities had programed a balance of payments surplus of about $8 million with a commitment for a surplus of a similar or larger order of magnitude for 1985. Over a number of years, the authorities were committed to achieving balance of payments surpluses, which, although they might not appear to be so large, were nevertheless quite important for a country the size of Haiti and with its type of external relationships.

In that connection, questions had been raised about the relationship between the reserve position and the current account of the balance of payments, the staff representative noted. Much of the support for Haiti's balance of payments came in the form of assistance on highly concessional terms from foreign donors. The current account deficit was mostly determined by the size of those aid flows; without the concessional assistance, the volume of imports would fall, and the trade deficit would not materialize. The reason for the slight widening of the current account deficit foreseen under the program for 1984 was the increase in financial inflows directly linked to certain investment projects that Haiti had been carrying out with the assistance of the donors in question. Thus, the Haitian authorities were not fully in control of developments in the current account; rather, the willingness of the donor countries to extend assistance would determine the size of the current account deficit. The relationship between the external reserve position and imports was similarly affected by the rate of disbursements on externally financed projects. In the program, the staff foresaw that, by the end of 1984, gross reserves would be equivalent to about two months' imports. That would be close to the ratio that had prevailed during earlier periods in which it had been considered that Haiti had no major balance of payments problems, although of course the country had never been in a really strong external position.

Haiti's use of the Fund's resources under the program was designed to cushion gross reserves to permit the Central Bank to function on a normal basis while a gradual accumulation of net international reserves took place, the staff representative added. The expectation under the program was that if Haiti had an overall balance of payments surplus of about $8 million in 1984 and 1985, and if it continued to record surpluses of from $8 million to $10 million for several years, then it would be in a position to meet repurchases as they fell due without any deterioration in its gross reserves in relation to imports.

Mention had been made of Haiti's long relationship with the Fund in the form of stand-by arrangements, the staff representative noted. Haiti had in fact entered into many arrangements with the Fund under which it had made no use of the Fund's resources, but it had been able to demonstrate, by the presence of a Fund program, that cautious fiscal policies were being followed. Donors were thereby reassured that the funds made available for various purposes were being properly used.

In that connection, the staff representative explained, as indicated in EBS/83/222, the World Bank and the Haitian authorities had been discussing a presentation to a group of donors, under the aegis of the Caribbean Group for Economic Cooperation and Development, precisely in order to try to establish certain priorities in the investment program and to coordinate various projects under way. Haiti had been emphasizing the consolidation of ongoing projects in an attempt to complete them. One of the problems encountered over the past few years had its roots in the financing on commercial terms of certain ambitious projects that had sometimes proved to be more costly and less profitable than the authorities had originally expected, thereby contributing to some of the fiscal difficulties experienced in the recent past. The goal under the program was therefore to seek financing from international agencies and foreign donors that would give the more carefully selected investment projects a greater chance of success.

As for exchange rate policy, the staff representative continued, there had been a stable relationship between the Haitian gourde and the U.S. dollar since the early part of the twentieth century. The U.S. dollar still circulated freely in Haiti and was accepted as a means of payment in transactions. The Haitian economy had also been closely related in many ways to the U.S. economy. The pressures that had developed on the balance of payments, as reflected in the size of the deficit in 1981--$55 million--and in 1982 were the result of fiscal difficulties, which the authorities were trying to redress.

Labor costs were relatively low in Haiti and had made the development of light manufacturing quite attractive, the staff representative observed. The Government had encouraged the establishment of such industries. Wage developments had not led to pressures on costs. Most of the inflation in Haiti in recent years could be attributed to developments in prices abroad, in particular for certain imports, such as petroleum products. Traditionally, Haiti's rate of inflation had not departed greatly from that of the United States--the major trading partner--and the target under the program was basically to maintain that situation.

In response to sharp changes in interest rates abroad, the Haitian authorities had increased domestic interest rates in order to encourage capital to remain in the country, the staff representative noted. At present, although interest rates abroad had dropped, Haitian rates had been maintained at a higher and more competitive level precisely in order to mobilize financial savings for domestic purposes.

Under the previous stand-by arrangement, the staff representative recalled, a monthly ceiling had been placed on the expenditures of the Treasury, which accounted for only a portion of public sector spending, but the most important part, and the one directly under the control of the Ministry of Finance. Although the monthly ceiling had been useful to the authorities for controlling fiscal outlays, it had tended to create inflexibility in the procedures for managing expenditures. It had therefore been decided to move to a quarterly ceiling, which would still make it clear that expenditures would be kept under tight control but offer more flexibility. At the same time, even though the authorities anticipated a significant increase in revenue over the coming year, as a result of steps taken in tax policy and administration, they did not wish to project expenditure on the basis of revenue that might not materialize fully. A certain portion of the increase in revenue would depend largely on administrative measures, and the immediate results were sometimes difficult to measure. Therefore, the authorities had preferred an adjustable ceiling, enabling them to increase expenditures somewhat if resources materialized as expected, not by the full amount of the increase but by two thirds, as established in the program. If the increase in revenue turned out not to match the conservative estimates in the budget, the authorities were prepared, as in the preceding two years, to cut expenditures sufficiently to remain within the overall ceilings on the public sector deficit that had been agreed in the program.

During the past two fiscal years, Treasury expenditures had been reduced by 25 percent, the staff representative from the Western Hemisphere Department observed. In a number of areas, the cuts had fallen on maintenance expenditures, impeding efforts to carry out the program. In addition, in the budget for 1983/84, certain maintenance costs, particularly those of a recurring nature, which had in the past been included in the investment budget, had been more correctly included in the category of current expenditure. A number of investment projects that had been carried out with the assistance of international agencies and foreign donors also generated recurring expenditures, which in some cases had not been sufficiently provided for in the budget. An attempt had been made in the budget for 1983/84 to make specific allocations for some of those expenditures.

The staff representative from the Exchange and Trade Relations Department said that in considering whether or not a two-year stand-by arrangement was appropriate, the staff tended to give weight to the wishes of the authorities, particularly where their performance had been satisfactory. In Haiti, there were two other reasons why a two-year arrangement seemed to be the proper vehicle. First, there was the potential impact on the flow of aid from donors. To the extent that Haiti's commitment under a program agreed with the Fund gave donors the assurance of satisfactory management of the economy, aid flows were likely to increase. Second, the program envisaged large enough balance of payments surpluses during the entire period of the arrangement and in the following years to allow Haiti to increase its gross reserves as imports and the economy grew, and to repay the Fund. That was possibly a classic example of the type of balance of payments outcome over the medium term that should be sought under most stand-by arrangements.

Responding to the desire expressed by several Executive Directors for a six-month review, the staff representative from the Exchange and Trade Relations Department noted that reviewing programs had benefits and costs, including the cost of a larger number of staff missions. When formulated as performance criteria, reviews provided an opportunity to exercise judgment on the progress made under the program. Quantitative ceilings, on the other hand, served to gauge the performance of the economy and thus to provide assurance that it was on track. When reviews and quantitative ceilings were both made performance criteria, there was always a danger that the procedure might undermine the credibility of the quantitative elements of the program by giving the impression that the criteria were not sufficient indicators of performance. Of course, it was standard practice in a stand-by arrangement to include provision for a consultation review that the Fund could call whenever it judged it to be necessary, and not only when performance criteria were not being met.

Commitments of resources by the Fund for periods beyond one year were highly contingent, the staff representative explained, as was made explicit in the provisions of the stand-by arrangement. The advantage of a multiyear commitment was the assurance that it gave to members that large amounts would be made available for a longer period if the country's performance under the stand-by arrangement was satisfactory. Those principles were embedded in the Executive Board's decisions on the extended Fund facility and the policy on enlarged access, and also in the guidelines on conditionality. The need to safeguard the revolving character of the Fund's resources was deemed to have been met when a country submitted a quantified policy program for a 12-month period. The disbursement of amounts to be drawn under the arrangement in the second or third year was contingent on a review and agreement on quantified policy conditions being reached for the period in question. As Mr. Erb had suggested, there was a thin line between a two-year arrangement, and a one-year arrangement accompanied by the intention of following it with another arrangement. But the important issue for consideration by Executive Directors was the value that members attached to the commitment made by the Fund over several years.

The Acting Chairman commented that the lack of quantification by way of targets for the second year and in the medium term might be one of the problems Mr. Erb had with the program.

Mr. Erb confirmed that he was looking not for specific quantitative targets for the second year as much as for a medium-term analysis by which to judge whether or not the adjustment period was likely to be completed at the end of the two-year period. Such an analysis would also give some sense of the type and the magnitude of the policy adjustments in the second year, even if they were not spelled out in precise detail. A commitment for a two-year period went a step further than a commitment for one year with an implicit intention to continue the commitment. That intentional step called for the staff to provide more background.

The objective for the reserve position was important to those framing the provision of longer-term development assistance, Mr. Erb commented. If adequate attention were not paid to building up the net reserve position in the planning of longer-term financial flows, the country might be faced with problems if there were unforeseen contingencies of whatever nature. The staff representative had mentioned that gross reserves would be built up to the level attained in previous years when the balance of payments had been judged to be in a reasonably good position. But reserves were held partly for precautionary reasons, and an assessment of their adequacy should be based not only on the performance of the economy in normal years but also on whether or not there were enough reserves to see the country through the bad years. A general aspect of reserve management that should be considered in all countries was the need to use good years to build up a reserve position that would leave the country in the strongest situation to deal with any fluctuations in its balance of payments that were likely to occur.

The staff representative from the Western Hemisphere Department responded that the staff was conscious of the need to build up net international reserves. That was why a target had been set for an increase in reserves of $8 million in 1983, and of at least a similar amount in 1984, on the understanding that the buildup would continue into the future. Haiti had had a record, during certain periods, of accumulating up to $10 million of reserves yearly, as it had done in the period preceding 1980. The fiscal situation had been under control at that time, whereas, from 1980 to 1982, it had been particularly poor, and reserves had been depleted. The intention of the authorities was to accumulate net reserves of $8 million to $10 million over four years so that net international reserves were no longer negative. That was why the authorities also intended to continue to strengthen their fiscal situation so that it would not be a source of pressure on the balance of payments.

In response to the question raised earlier by Mr. Prowse on the credit ceiling, the staff representative explained that in many programs no ceiling was placed on the domestic assets of the banking system as a whole, but that one was placed on the net domestic assets of the monetary authorities, as in Haiti. The rest of the Haitian banking system comprised basically the commercial banks, most of which were foreign-owned; they were engaged largely in lending operations, and their performance was influenced by the confidence that they had in the system. The fact that the National Credit Bank was being separated from the Central Bank was introducing a further change in the system, and the ceiling had therefore been kept on the consolidated accounts of the two banks as the equivalent of the net domestic asset ceiling imposed in the past. A separate set of ceilings had been placed on the net domestic assets of the National Credit Bank, but since those were included in the overall ceiling for purposes of the program, it had not been considered necessary to make them a performance criterion.

The objective had been to find a way to enable the Central Bank to give some guidelines to the National Credit Bank on what its credit policies should be in the year ahead, the staff representative from the Western Hemisphere Department concluded. It had not been considered necessary or practical from the point of view of following up on the program to have a ceiling on the net domestic assets of the banking system as a whole.

The staff representative from the Exchange and Trade Relations Department added that in formulating credit ceilings in stand-by arrangements, the staff still followed, broadly speaking, the guidelines set out in the paper on that subject issued in 1971 (SM/71/145, 6/11/71; EBM/71/118, 11/22/71). The policy guideline essentially was that the ceiling should be as comprehensive as possible, and would therefore be based on the banking system whenever the institutional arrangements permitted. A degree of flexibility had been included to deal with countries where the monetary authorities' decisions on credit policy related only to their own credit operations; in those cases, ceilings could be established on the net domestic assets of the central bank only. Conceptually, there were arguments for and against a central bank ceiling. Such a ceiling implied that there was a stable relationship between central bank monetary liabilities (reserve money) and a broader concept of money; in a sense, such a relationship ensured that the control of the central bank over its credit expansion also served to control banking system credit as a whole. In principle, he saw considerable merit in retaining the flexibility in the guidelines.

Mr. Prowse asked the staff to clarify whether it faced a practical difficulty in Haiti in establishing a ceiling to monitor domestic assets in the system as a whole, or whether it believed that the relationship between the assets of the Central Bank and the National Credit Bank and the broader volume of credit was stable, so that the money supply and the impact on the economy as a whole would not be influenced significantly by the independent operations of the foreign commercial banks.

The staff representative from the Western Hemisphere Department replied that in the past there had been a relatively stable relationship, and the staff had had no difficulties in using a central bank ceiling. As for the practical problems that might arise if a ceiling on the banking system as a whole were used, information from the commercial banks was received with a longer delay.

In response to a question by the Acting Chairman about how long it took to reconcile the two parts of Table 8 in EBS/83/222 on the consolidated accounts of the National Credit Bank and the Central Bank, and the banking system as a whole, the staff representative said that fairly reliable preliminary figures on the Central Bank and the monetary authorities were available through September 1983. The data were on an aggregate basis rather than on a detailed one but were available every fifteen days. The latest available data on the commercial banks would be for the end of August. During the Fund's long relationship with Haiti under a series of stand-by arrangements, the staff had found the relationship between the assets of the monetary authorities and the banking system as a whole to be fairly stable.

Mr. Prowse remarked that that relationship could always change.

Mr. Jayawardena asked the staff whether, in referring to the long and close relationship between the Haitian gourde and the U.S. dollar, it was inferring that the close link of the two exchange rates was appropriate. He raised the question because of the number of other countries in the region that were Haiti's competitors for exports to the United States and to other markets, and whose currencies had been depreciated significantly. If the staff contention was that Haiti had no exchange rate option, because of the integration of its economy with that of the United States, the question became one of how viable continued adjustment would be, under whatever other instruments were available.

The Acting Chairman commented that the fact that an exchange rate policy was a longstanding one did not make it the right policy. But the Haitian authorities had a long record of being willing to make the necessary adjustments--whether in wages, public sector operations, monetary policy, or a combination thereof--in such a way as to support and in effect validate the exchange rate.

The staff representative from the Western Hemisphere Department noted that in large part, the fluctuations in the exchange rate shown in Chart 1 were a reflection of the fluctuations in the U.S. dollar in the world market. The issue was therefore in effect the maintenance by Haiti of a policy of pegging the gourde to the U.S. dollar. In the past, as indicated by the Acting Chairman, the Haitian authorities had been willing, and continued to show their willingness, to make the necessary adjustments to maintain the exchange rate relationship by means of changes in fiscal and in other internal policies. Under the circumstances, the staff had not felt that a change in the exchange rate at the present time would be any better than proceeding with the type of policies that the Haitian authorities had proposed to follow. A different conclusion would not of course be precluded if there were to be at some time a fundamental disequilibrium in the balance of payments. The cause of the recent disequilibrium having been identified as a large fiscal imbalance, which the authorities were continuing to correct, it was necessary to view the question of a change in the exchange rate, which was by no means a decision to be taken lightly in that context. It might be worth noting that although there was a parallel rate for the gourde, the spread had been narrowing and in the past few months had practically disappeared.

Mr. Clark said that he endorsed Mr. Erb's remarks on the nature of the review of the program. It was important not only as a review per se, but as a way for the Executive Board to express its views on the shape of the program for 1985.

The Acting Chairman noted that provision was made in the text of the stand-by arrangement for a review by September 30, 1984. Performance criteria for 1985 would have to be agreed by that time if Haiti was to make any further drawings under the arrangement.

Mr. Clark explained that he had in mind a review at a time that would allow the Executive Board to influence the program for the following year.

Mr. Caranicas noted that the staff representative from the Exchange and Trade Relations Department had mentioned the important question of the revolving character of the Fund's resources. It was not clear to him that the question was of any relevance in considering whether a stand-by arrangement should be for one or two years. Was the revolving character of the Fund's resources more assured under a shorter rather than a longer arrangement?

He did not take issue with the length of the arrangement proposed for Haiti, Mr. Caranicas remarked. He also had an open mind about the proposal for a review after six months, although he could consider it only if it were acceptable to Mr. Kafka.

The staff representative from the Exchange and Trade Relations Department responded that his only reason for mentioning the revolving character of the Fund's resources had been to assuage the concerns expressed about the duration of the stand-by arrangement, possibly because of a feeling that there was not enough of a safeguard about the revolving nature of Haiti's use of Fund resources. He had therefore pointed out that the objective under the program was to achieve balance of payments surpluses over a period of time. It was not a question of whether the use of the Fund's resources would be more or less revolving depending on the length of the arrangement. The basic issue was how much of an adjustment could be made in one year; for Haiti, it had seemed reasonable to spread the adjustment over two years.

Among the techniques for conducting reviews of the kind sought by Mr. Clark, the staff representative explained, there could be a review as a performance clause, meaning that the staff's report on the review would be discussed by the Executive Board. Provision for a review with management could also be made, but it would not constitute a performance clause; however, a report could be issued for the information of the Executive Board. In both instances the reports would provide essentially the same analysis, the only difference being one of form. Mr. Clark had in fact suggested a review as a formal matter because the choice was between a review as a performance clause requiring Board consideration and a review without such a requirement but which would still examine progress in implementing the program and explore the prospects for the economy.

Mr. Erb said that he had not asked for another review in the course of the first year of the program. As he had stated, he was prepared to support the program as it stood, given the record of the Haitian authorities over the past year. But he believed that the staff should frame the second year of the program within a medium-term context, if indeed a commitment was to be made for another two years.

The Acting Chairman said that the program for the second year would clearly have to be drawn up based on a balance of payments projection for the medium term.

Mr. de Vries said that as he understood the proposal before the Executive Board, the stand-by arrangement for Haiti would be in an amount equivalent to SDR 60 million, to be available until September 30, 1985, but that less than half of that amount--SDR 28 million--would be available, in phased drawings, until September 1984. No additional drawings would be possible after that until a staff mission had submitted a report to the Executive Board, which would be required to adopt a decision on the review.

The Acting Chairman confirmed Mr. de Vries's understanding, which was made legally clear in paragraph 4(b) of the text of the proposed stand-by arrangement. In effect, after September 30, 1984, Haiti would not be able to make further drawings, beyond the SDR 28 million drawn in the first year of the arrangement, unless performance criteria had been agreed for the ensuing period.

Mr. Joyce explained that his support for the proposal made by Mr. Clark extended to all multiyear programs, not necessarily only to programs under longer stand-by or extended arrangements. He had understood Mr. Clark to be seeking an opportunity for a discussion--under any guise, and a review seemed to be a logical one--so that the views of the Executive Board could be taken into account by the staff in the negotiation of the performance criteria for the second year of a stand-by arrangement, or in the case of an extended Fund arrangement, for the third year.

Mr. Erb asked what the involvement of the Fund would be, in the Caribbean Group Consultative Meeting, in laying out the medium-term prospects. It seemed to him that the Fund could play a useful and important advisory role vis-à-vis the donors in assessing the medium-term external implications of their plans for aid flows and other assistance. He viewed the consultative process as an iterative one in which the Fund should be involved as the thinking of the World Bank and other donors evolved.

The staff representative from the Western Hemisphere Department responded that the Fund was normally a participant in the meetings of the Caribbean Group for Economic Cooperation and Development. The staff had been in touch with the Haitian authorities and the World Bank, which was making preparations for the discussion of Haiti's projects and the priorities to be assigned to them.

Mr. Kafka observed that Haiti's basic problem had been described starkly by Mr. de Vries and Mr. Erb, who had mentioned respectively the heavy emphasis of the program on demand restriction and the need for greater cooperation with the World Bank. The raw facts were that Haiti was an atrociously poor country; its real per capita income had been declining in the past three years, although at a falling rate; and the economic base for the existence of nearly 6 million people had been literally eroding because of overuse of the soil. The main problem was to obtain an infusion of resources, under the appropriate control, so that further soil erosion could be prevented and additional productive capacity be built up. Otherwise, Haiti would face a demographic catastrophe in spite of the high rate of emigration. It was because of the abject poverty in which the country lived that domestic savings were not higher. Raising the rate of domestic savings from zero to 5 percent of GDP had been a major effort.

The issue of net and gross reserves was largely a technical one of definition, Mr. Kafka considered. The general rule of the Fund was to regard borrowing by a country at 12 months as a liability, which was deducted from gross reserves to get net reserves, whereas borrowing at 13 months was not. Drawings on the Fund and certain other borrowings over 12 months were excepted. The dividing line between short term and long term was thus a fine one.

As to whether the stand-by arrangement for Haiti should have been for one year with the hope of a second year, or for two years, Mr. Kafka pointed to the Fund's recent experience with the lack of liquidity on a commitment basis. It should not be surprising that a country engaged in a structural reform, particularly on the fiscal side, attached importance to being sure that the resources that it anticipated receiving would be available, irrespective of the Fund's ability to borrow.

The size of the economy should be taken into account in deciding whether or not a devaluation would be helpful, Mr. Kafka considered. Certain costs, such as transportation costs, were high, and although they were not a factor affecting exports to the United States, they might reduce the incentive yielded by devaluation for exports to more distant markets. For those and other reasons, he wanted to reaffirm that a devaluation was not appropriate.

He was not in a position to accept a review as a performance clause without consulting his Haitian authorities, Mr. Kafka stated. It would not be helpful to delay the proposed decision so that such a consultation could be made, nor had he found much support for a consultation after six months as a performance clause. He felt sure that the Haitian authorities would have no objection to consulting with the Fund at some time in the course of the year ahead before the new program was brought to the Executive Board, although a consultation was probably less necessary in Haiti than in most member countries because the Fund had had a resident representative in the country for a long time and was consequently well informed at all times. The Managing Director could ask a member country to engage in a consultation whenever he deemed it appropriate, and it should be left to management to decide whether or not the outcome of such a consultation should be brought to the Executive Board. But the practical arguments made by the staff were in his view relevant. A thinly stretched staff, particularly in the Western Hemisphere Department, should not be overburdened by having to hold a consultation with a member that had been doing well under its latest stand-by arrangement.

Mr. Prowse said that he hesitated to raise the exchange rate issue again, but he remained unconvinced that the Haitian exchange rate regime was appropriate for the country. He was not sure whether the point made by Mr. Kafka about high transport costs and the closeness of the U.S. market was relevant. As had been mentioned during the discussion, it was in light manufactures that Haiti had prospects for a growth of exports, and its competitiveness with other countries exporting similar products would be affected by the rate of exchange between the gourde and the U.S. dollar. Tourism was already being affected; the market for the U.S. tourist dollar was competitive, and Haiti was at some disadvantage compared with other islands in the Caribbean that had devalued their currencies. Therefore, he urged the staff in the next report prepared on Haiti, whether in six months' time or later, to examine thoroughly the pros and cons of the historical rate of G 5 per U.S. dollar and to give the Executive Board its view on whether Haiti should not be pursuing a different exchange rate policy.

The Acting Chairman commented that in light of the discussion, the staff would look at the matter closely and present its judgment to the Executive Board on the next relevant occasion.

The Acting Chairman then made the following summing up:

Directors commended the determination of the Haitian authorities in the implementation of adjustment measures to stabilize the economy under the recently concluded Fund program. The reduction achieved in the public sector borrowing requirement had gone a long way to easing balance of payments and exchange rate pressures. Directors noted that the elimination of external payments arrears and the increased availability of credit for the private sector should help to restore confidence and improve economic prospects.

Most speakers remarked that despite these financial achievements Haiti's external position remains weak, and they agreed that for several years to come emphasis had to be placed on strengthening the balance of payments and the international reserve position. In this context, the absence of improvement projected in the external current account from 1983 to 1984 was viewed with some concern. The consolidation of the public finances through continued restraints over public spending and initiatives to improve tax collections were viewed by Directors as the key to the success of Haitian economic and financial policy. They also welcomed ongoing efforts to strengthen the financial position and improve the lending practices of the state-owned National Credit Bank as well as to complete the separation of the operations of that bank from the Central Bank. Some Directors noted the rise in real interest rates that had taken place and suggested that interest rate policy should be kept under review in light of the need to mobilize domestic savings.

Some Directors noted that the resources available to Haiti under the new arrangement, together with the programmed overall balance of payments surpluses, should provide the Central Bank with a more adequate reserve cushion to enable the economy to function more efficiently.

Noting the strong appreciation of the real effective exchange rate of the gourde since 1978 and the composition of Haitian exports, about half of which were manufactures, Directors stressed the need for Haiti to maintain a strong competitive position, and some Directors believed that the appropriateness of exchange rate policy should be kept under review. It was noted, however, that exports of manufactured goods have been growing vigorously and that the differential between the official and parallel exchange rates has recently disappeared.

On external debt management, Haiti was urged to be very cautious and to concentrate the thrust of the development effort on projects that can be financed with concessional assistance.

It is expected that the next Article IV consultation with Haiti will be held within the standard 12-month cycle. Directors emphasized the need for more substantive medium-term analysis in future staff reports on Haiti, including those on the review of the stand-by.

The Acting Chairman said that he understood that although Mr. Erb had raised questions about the two-year stand-by arrangement, and would have preferred it to be placed more in the framework of a medium-term analysis, he was nevertheless willing to support the proposed decision, in part on the strength of the provision in paragraph 4(b) of the arrangement, which made it clear that the Executive Board would have an opportunity to look at the new performance criteria to be proposed for 1985. On that occasion, the staff would do its best to provide the medium-term framework that Mr. Erb and some other Directors were seeking. In that way, the position of the Executive Board on the second year of the program would be safeguarded.

On the question of whether there should be a review after six months, the Acting Chairman observed that, as would be seen from Tables 1 through 4 in Attachment II to the stand-by arrangement, quantitative performance criteria had been provided for the first year of the arrangement. It would be redundant, and most unusual, to add at the present time a review as a performance criterion. Several Executive Directors had taken the view that it would be desirable for there to be a review in six months or before the negotiation of the program for the second year. If it would be helpful, he could undertake that the management would invoke, prior to that negotiation, the consultations to which reference was made in paragraph 17 of the letter of intent; the report resulting from a staff review held under such a consultation could be brought before the Executive Board. The disadvantage would be, as Mr. Kafka had mentioned, the need for two missions to Haiti in the next 12 months, one for the review and the second for the negotiation of the second year of the program.

Mr. Kafka said that he would not agree to such an undertaking's being given. In accordance with the Fund's usual procedures, it should be left to the discretion of the management to observe the situation in Haiti, on which it was kept well informed through a resident representative and through reporting requirements. If it was found to be necessary, management should authorize a mission that would report not only to management but also to the Executive Board.

Mr. Zhang considered that Haiti should be treated in the same way as all other members. He sought reassurance that any special procedure for a review in six months' time would not create a precedent.

Mr. de Vries said that he supported Mr. Kafka's view. Like Mr. Zhang, he would be worried if Haiti was treated any differently from other member countries. He was quite satisfied with the decision as proposed.

Mr. Caranicas remarked that it was customary, after listening to the various arguments, to accept the point of view of the Executive Director for the member country whose request was being considered. In the absence of Mr. Kafka's support, he would not accept any amendment to the text of the stand-by arrangement.

Mr. Blandin expressed his agreement with Mr. Kafka's position.

Mr. Grosche explained that he had joined in the expression of support for Mr. Clark's proposal as a way to prepare the program for 1985. Based on the Acting Chairman's explanation of paragraph 4(b) of the stand-by arrangement, and in the expectation of a thorough discussion of the program for 1985 before the end of the first year of the program in 1984, he would support the stand-by arrangement as proposed in EBS/83/222.

Mr. Ainley said that he fully supported Mr. Kafka's stand. He was swayed by the presence of a Fund resident representative in Haiti, and by the discretion that the management had to send a review mission, if necessary, before the agreed date if the program went off track.

Mr. Jayawardena added his support for Mr. Kafka's position.

The Acting Chairman assured Executive Directors that management would have very much in mind what they had said in exercising its discretion. The decision to undertake a consultation would arise if evidence accumulated that the trade system was becoming uncompetitive and that as a result the program stood in some danger of going off course.

Mr. Erb added that it was also essential for the Fund staff to work closely with the World Bank in the coming months, especially in preparation for the meeting of the Caribbean Group for Economic Cooperation and Development.

The Executive Board then took the following decision:

1. The Government of Haiti has requested a stand-by arrangement for the period from November 7, 1983 to September 30, 1985 for an amount equivalent to SDR 60 million.

2. The Fund approves the stand-by arrangement set forth in in EBS/83/222, Supplement 1.

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

Decision No. 7554-(83/153), adopted
November 7, 1983

DECISION TAKEN SINCE PREVIOUS BOARD MEETING

The following decision was adopted by the Executive Board without meeting in the period between EBM/83/152 (11/4/83) and EBM/83/153 (11/7/83).

2. EXECUTIVE BOARD TRAVEL

Travel by an Executive Director as set forth in EBAP/83/271 (11/3/83) is approved.

APPROVED: March 23, 1984

LEO VAN HOUTVEN
Secretary