SM/84/71
Correction 1

CONTAINS CONFIDENTIAL
INFORMATION

May 24, 1984

To: Members of the Executive Board

From: The Secretary

Subject: Somalia - Staff Report for the 1983 Article IV Consultation

The following corrections have been made in SM/84/71 (4/2/84):

Page 4, 1st full para., line 14: for "the border conflict with Ethiopia" read "regional hostilities"

Page 5, line 4: for "the border conflict with Ethiopia" read "regional hostilities"

Corrected pages are attached.

Att: (2)

Other Distribution:
Department Heads

Table 1. Somalia: Selected Economic and Financial Indicators, 1980-83

	1980 Actual	1981 Actual	1982 Actual	1983 Review proj.	1983 Prelim. estimates
	(Growth rate in percent unless otherwise specified)				
Consumer price index	59.4	44.3	23.7	12.0	35.0
Trends in central government finance					
Total revenue and grants	5.1	41.8	41.4	18.0	15.1
Total expenditure	-3.8	18.8	44.2	0.1	5.8
Overall deficit/Total expenditure	39.2	27.5	28.9	16.2	22.6
Deficit (excluding grants)/Total expenditure	54.6	39.2	48.6	40.2	42.1
Trends in monetary aggregates					
Money and quasi-money	20.2	30.8	15.9	-5.4	-13.0
Net domestic credit	31.2	17.2	10.5	5.4	5.4
Government (net)	54.5	18.3	-6.7	-13.1	-13.1
Private	14.6	16.1	27.3	18.6	18.6
Net domestic assets	29.7	32.7	33.4	5.8	7.6
Interest rates					
Commercial bank lending rate (public enterprises)	7.5	10.0	12.0	12.0	12.0
Commercial bank lending rate (private enterprises)	9.5	10.0	12.0	12.0	12.0
Commercial bank maximum deposit rate	7.0	9.0	11.0	11.0	11.0
Development bank maximum lending rate	7.5	14.0	14.0	14.0	14.0
Trends in external sector					
Exports, f.o.b.	25.5	-14.3	14.9	10.7	-22.9
Imports, c.i.f.	17.0	-8.5	13.3	-1.5	-14.9
Nominal effective exchange rate (depreciation -)	0.3	-5.0	-27.9	...	-11.8
Real effective exchange rate (depreciation -)	36.7	21.0	-20.7	...	8.9
	(In millions of U.S. dollars unless otherwise specified)				
Current account balance	-136.0	-95.0	-131.0	-87.0	-107.0
Current account, excluding grants	-279.0	-245.0	-288.0	-234.0	-255.0
Overall balance of payments	-28.0	-13.0	-49.0	-40.0	-57.0
ross official reserves	25.0	42.0	14.0	30.0	29.0
(In weeks of cash imports)	(3.9)	(10.7)	(3.7)	(6.8)	(9.0)
External debt, including IMF	694.6	886.8	1,056.5	1,180.0	1,202.5
Debt service ratio	4.6	14.2	12.2	17.9	17.0
External payments arrears	44.6	15.5	--	--	--

Sources: Data provided by the Somali authorities; and staff estimates.

increased from about one month of cash imports 1/ at end-1980 to over two months of cash imports at end-1981 and external payments arrears were reduced to about one third of their end-1980 level mainly through rescheduling.

To maintain the growth momentum of the economy, to reduce inflation further, and to move toward a sustainable external sector position, the Somali authorities continued with their adjustment efforts during 1982, supported by an 18-month stand-by arrangement that came into effect on July 15, 1982. 2/ Under the new program, a number of measures were taken to stimulate supply, notably the further devaluation of the Somali shilling (17 percent on the export side and 34 percent on the import side in foreign currency terms), the unification of the dual exchange rate system that had been in effect since mid-1981, the pegging of the Somali shilling to the SDR, the further easing of controls on private sector imports, and the liberalization of marketing and pricing policies. These supply-oriented policies were reinforced with tight fiscal and monetary policies, including a further increase in interest rates. Despite the recurrence of regional hostilities, the budgetary deficit was kept to about 29 percent of total expenditure, about the same ratio as in 1981. This reflected partly additional improvements in tax collection procedures, changes in customs valuation procedures, a further intensification of expenditure control procedures to eliminate unnecessary or deferrable expenditures, and a virtual freeze on government wages and salaries. 3/ With the almost tripling of the foreign financing of the deficit in domestic currency terms, the Government was able to reduce its net indebtedness to the banking system by 7 percent. Domestic credit expansion was therefore reduced to two thirds its rate in 1981, even though credit to the non-government sector was allowed to grow at almost double the 1981 rate in order to stimulate private sector economic activity. The expansion in domestic liquidity was reduced to half that of 1981.

Reflecting the policies implemented and continued favorable weather conditions, economic growth is estimated to have doubled in 1982, with GDP rising by about 10 percent in real terms. Agricultural production, in particular, benefited from the change in relative prices effected through the devaluation and the liberalization of pricing and marketing policies. The rate of inflation was nearly halved, falling to 24 percent. During 1982, exports increased by 15 percent, reflecting the favorable weather conditions and the policy measures taken. Nonetheless, the overall

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1/ Cash imports include foreign exchange, franco valuta, and external account imports.

2/ The stand-by arrangement was for an amount equivalent to SDR 60.0 million (173.9 percent of quota); EBS/82/105.

3/ The development levy on government salaries was abolished in 1982, resulting in an effective average increase of 10 percent in wages of government employees.

balance of payments deficit of US$49 million exceeded somewhat the program projection of US$38 million due to a large extent to an unexpected private capital outflow partly in response to political uncertainties arising from the recurrence of regional hostilities. The capital outflow was financed by workers' remittances through the parallel market. During 1982 Somalia did not contract any new nonconcessional public or publicly guaranteed debt and, at the end of 1982, had eliminated all of its outstanding external payments arrears. Due to rescheduling of foreign debt, Somalia's debt service payments in 1982 were contained to 12.2 percent of goods and services, compared with 14.2 percent in 1981.

III. Discussions on Economic and Financial Developments Under the 1983 Financial Program 1/

During 1983, the Somali authorities intensified their adjustment efforts by taking several supply-oriented measures and tightening further their financial policies. The performance of the Somali economy in 1983, however, was affected by the ban imposed in May 1983 by Saudi Arabia on cattle imports from Africa and other countries, after the discovery of rinderpest in some imported cattle and, to a lesser extent, by a deterioration in weather conditions, particularly during the second half of 1983. The severity of the impact of these two factors on the economy was, however, mitigated somewhat by the policies pursued by the authorities since mid-1981 and the new measures implemented during 1983. Somalia was able to observe all the quantitative performance criteria under its stand-by arrangement through September 1983 (Table 2). This section focuses primarily on economic and financial developments in 1983, while key policy issues, such as those relating to the exchange system, external debt, reform of public enterprises, and restructuring of the banking system are discussed in the next section.

1. External sector policies and developments

During 1983, the Somali authorities took a number of measures designed to curb the capital outflow that had emerged in 1982, encourage the inflow of workers' remittances through official channels, and avoid the gradual overvaluation of the Somali shilling. To this end, on January 1, 1983, a bonus scheme was instituted, providing a So. Sh. 5 per U.S. dollar premium (33 percent in domestic currency terms at the time) above the official rate, for workers' remittances and capital inflows effected by Somali nationals. 2/ Simultaneously, priority in the

1/ The discussion is based on preliminary data for 1983.
2/ The multiple currency practice arising from the bonus scheme was approved by the Executive Board through June 30, 1984, or the completion of the 1983 Article IV consultation with Somalia, whichever is earlier (EBD/83/332).

Table 2. Somalia: Quantitative Performance Criteria, June 1982-December 1983

(End of period)

	1982			1983			
	June	Sept.	Dec.	March	June	Sept.	Dec.
	(In millions of Somali shilllings)						
Net domestic credit 1/							
Ceiling	--	5,086.0	5,054.0	5,118.0	5,168.0	5,223.0	5,293.0
Actual	5,088.0	5,070.4	5,023.8	5,107.7	5,144.0	5,196.3	...
Net credit to Government 2/							
Ceiling	--	2,285.0	2,115.0	2,065.0	1,990.0	1,910.0	1,825.0
Actual	2,390.9	2,270.3	2,100.0	2,058.2	1,981.5	1,904.7	...
	(In millions of U.S. dollars)						
External debt 3/							
Ceiling	--	25.0	25.0	25.0	25.0	25.0	25.0
Actual	--	--	--	--	--	--	...

Sources: EBS/83/154; and data provided by the Somali authorities.

1/ Credit to Government, public enterprises, and private sector less government deposits with the banking system.

2/ The banking system's claims on the Government, less government deposits, plus any budgetary use of local currency counterpart in respect of purchases from the Fund.

3/ New commitments on public and publicly guaranteed external debt with a maturity of between 1 and 12 years, excluding any refinancing loans obtained through negotiations.