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AGENDA**

EBS/86/192
Correction 1

CONFIDENTIAL

September 18, 1986

To: Members of the Executive Board

From: The Secretary

Subject: Mauritania - Staff Report for the 1986 Article IV Consultation,
Review Under Stand-By Arrangement, and Request for Arrangements
Under the Structural Adjustment Facility

The following corrections have been made in EBS/86/192 (8/19/86):

Page 3, Table 1, column 3, line 6: for "--" read "2.0"

Page 49, last para., line 6: for "UM 2,400 million" read "UM 1,800 million"

line 8: for "UM 2,000 million." read "UM 1,700 million."

Corrected pages are attached.

Att: (2)

Table 1. Mauritania: Fund Position During the Stand-By Arrangement Period

| | Outstanding at beginning of arrangement | 1986 | | | | 1987 | Total |
|--|---|--------------------------|--------------|---------------|---------------------|----------------|-------------|
| | | April | May- Aug. | Sept- Nov. | Dec. 86- Feb. 87 | March April | |
| (In millions of SDRs) | | | | | | | |
| Transactions under tranche policies (net) | -- | <u>0.4</u> | <u>0.5</u> | <u>0.1</u> | <u>1.6</u> | <u>0.8</u> | <u>3.5</u> |
| Purchases | -- | <u>1.2</u> | <u>2.7</u> | <u>2.7</u> | <u>2.7</u> | <u>2.7</u> | <u>12.0</u> |
| Ordinary resources | -- | <u>1.2</u> ^{1/} | <u>2.7</u> | <u>2.7</u> | <u>2.7</u> | <u>2.7</u> | <u>12.0</u> |
| Borrowed resources | -- | -- | -- | -- | -- | -- | -- |
| Repurchases | -- | <u>0.8</u> | <u>2.2</u> | <u>2.6</u> | <u>1.1</u> | <u>1.9</u> | <u>8.5</u> |
| Ordinary resources | -- | -- | <u>2.0</u> | <u>0.9</u> | <u>0.9</u> | <u>0.9</u> | <u>4.6</u> |
| Borrowed resources | -- | <u>0.8</u> | <u>0.2</u> | <u>1.7</u> | <u>0.2</u> | <u>1.0</u> | <u>3.9</u> |
| Transactions under special facilities (net) | -- | -- | -- | 6.8 | -- | -- | -- |
| Total Fund credit outstanding (end of period) | <u>26.9</u> | <u>27.3</u> | <u>27.9</u> | <u>34.8</u> | <u>36.4</u> | <u>37.2</u> | |
| Under tranche policies | 26.9 | 27.3 | 27.9 | 28.0 | 29.6 | 30.4 | |
| Under special facilities | -- | -- | -- | 6.8 | 6.8 | 6.8 | |
| (As percent of quota) | | | | | | | |
| Total Fund credit outstanding (end of period) | <u>79.4</u> | <u>80.7</u> | <u>82.2</u> | <u>102.6</u> | <u>107.4</u> | <u>109.8</u> | |
| Under tranche policies | 79.4 | 80.7 | 82.2 | 82.5 | 87.3 | 89.7 | |
| Special facilities | -- | -- | -- | 20.1 | 20.1 | 20.1 | |

Source: IMF, Treasurer's Department.

^{1/} Initial purchase on the stand-by arrangement becoming effective.

worsened terms of trade, the impact of which were exacerbated by inappropriate policies, including expansionary fiscal and credit policy, inappropriate pricing policies, unfavorable performance of public enterprises, an increasing overvaluation of the currency, and an excessively large and unproductive public investment program, which led to an unsustainable debt burden.

Owing to adverse climatic conditions together with inadequate producer prices, the traditional production of cereals on nonirrigated land was reduced from about 100,000 tons in late 1960's to less than 30,000 tons during the 1984/85 (June-May) crop year. In the mining sector, until recently the leading sector of the economy, iron ore production required new and costly investments as easily exploitable mines were being depleted; copper production ceased in 1978. Attempts by the Government to set up viable manufacturing enterprises failed, and many Government-owned industries like the oil and sugar refineries had to be closed down. In the fishing sector, although the authorities adopted a new policy in 1979 aimed at increasing their control of fishing activities in Mauritania's coastal waters, the net foreign exchange receipts from fishing remained small and the value added by the sector remained low. As a result of these structural problems, GDP grew at an average annual rate of only about 1 percent over the period 1981-84 in spite of high investment ratio which reached 47.1 percent of GDP in 1982, reflecting the very low rate of economic return.

Along with the stagnation of the production, there emerged large fiscal and balance of payments imbalances. By 1984, the Government's consolidated overall fiscal deficit (on a commitment basis and including external grants) was equivalent to 11 percent of GDP (Table 2). Excluding external grants, the deficit amounted to 25 percent of GDP. This large fiscal imbalance, coupled with the deterioration of the terms of trade and the negative savings of the rest of the economy, resulted in an even larger balance of payments imbalance. By 1984, the deficit of the current account (including public transfers) was equivalent to 22 percent of GDP. Excluding public transfers, the deficit amounted to 36 percent of GDP. As a result of these large deficits, domestic and external arrears were accumulated and amounted at end-1984 to UM 0.7 billion and UM 7.7 billion (SDR 105 million) respectively. By end-1984, the outstanding foreign debt was about US\$1.4 billion, equivalent to 174 percent of GDP.

2. The process of adjustment, 1985-86

To reduce the major imbalances and effectively address structural problems facing the Mauritanian economy, early in 1985 the Government embarked on a comprehensive adjustment program, which stressed both demand management and substantial structural adjustment measures. This program was supported by a 12-month stand-by arrangement approved by the Executive Board in April 1985. The adjustment effort was continued and strengthened in the framework of a new program for 1986, which is supported by the current stand-by arrangement.

Code and a liberalization of pricing and import regulations in order to encourage economic activity.

3. As regards fiscal policy, the recovery program seeks to achieve balance in the consolidated budget, including grants, by 1988 and to register a surplus in 1989. These targets are consistent with the improvement in the balance of payments; they imply an increase in the surplus of the Treasury, and an increase in the proportion of the investment program that is financed by grants. In line with the improvement in the Central Government's financial situation, bank credit to the Government will not be increased, so that the expansion of total credit may be devoted in its entirety to the productive sector. The expansion of credit to the economy will be kept in line with the real growth rate of GDP and the programmed rate of inflation.

4. The annual program for the July 1986-June 1987 period, which represents the first year of the three-year period for which an arrangement is requested within the framework of the Structural Adjustment Facility, incorporates the objectives and measures for 1986 described in the letter of February 4, 1986 from the Minister of Economy and Finance and the Governor of the Central Bank of Mauritania and in the memorandum on economic and financial policies attached to that letter, as updated by the letter of June 26, 1986 regarding the review of the stand-by arrangement.

The main objectives for 1987 are (i) to achieve a growth rate of GDP of about 4 percent, (ii) to reduce the rate of inflation to 6 percent, (iii) to reduce the current account deficit to about 6 percent of GDP and the overall balance of payments deficit to about SDR 70 million, and to achieve some increase in reserves. The financing need would be covered by further debt relief, possible disbursements under the Structural Adjustment Facility, the Structural Adjustment Credit of the Bank and some exceptional assistance.

In the first half of 1987, the Government plans to pursue a rigorous fiscal and credit policy and to make significant progress in the implementation of structural reforms. In view of the objective set forth in the Economic and Financial Recovery Program to reduce the consolidated budget deficit in 1987 by more than 1 percent of GDP, the Treasury's surplus should rise to about UM 1,800 million in the same year. This would be reflected by a Treasury surplus from July 1986 to June 1987 of about UM 1,700 million. On the revenue side, steps will be taken to reduce customs duty exemptions and an effort will be made to expand the base for direct taxes. The new Investment Code will enter into effect before mid-1987, but certain changes in exemptions will be introduced in the Finance Law for 1987. Tax reform in the fisheries and mining sectors will be implemented on the basis of recommendations in World Bank studies scheduled for completion by end-1986, and after consultation with the Fund. Changes will also be introduced for the tax on business profits. On the revenue side, the increase in personnel

expenditure will not exceed the projected rate of inflation and there will be no nominal increase in expenditure on subsidies and military spending. In order to enhance the efficiency of the administration, a civil service census will be completed in the early months of 1987 and the reorganization of career paths and the structures of ministries will be implemented with assistance from the World Bank.

5. As in 1986, credit to the Central Government will not increase during the first half of 1987. The rate of increase in credit to the private sector will be maintained within a limit of about 8 percent in accordance with the financing requirements for new investments; this corresponds to an increase in domestic credit of approximately UM 1,700 million between end-December 1985 and end-March 1987 and of about UM 2,000 million between end-December 1985 and end-June 1987.

During the period July 1986-June 1987 the Government will not contract or guarantee nonconcessional loans with less than 15-year maturities; no external payments arrears will be accumulated.

The targets through June 1987 as regards the Treasury surplus, the expansion of overall domestic credit and credit to the Central Government, nonconcessional borrowing and external payments arrears represent benchmarks for program monitoring.

6. As regards agricultural policy, a study of the entire grain sector, including the structure of production and marketing costs, will be completed by end-1986 and will serve as a basis for a readjustment of producer and consumer prices in March 1987. The role of the private sector in marketing and processing domestic agricultural output will be gradually expanded and the existing monopolies on the marketing of food products will be reviewed. Some rice mills will be privatized. In 1987, the present channels for distributing fertilizers and other inputs and supplies will be privatized in connection with the establishment of new credit facilities, thereby easing the role of SONADER. The reorganization of the Food Security Agency will continue in order to cut costs and improve its management. This should make it possible to free a greater proportion of the sales proceeds from food aid for use in project financing by the Common Fund for food aid counterparts.

7. An in-depth study on the fisheries sector and the steps necessary to promote its expansion and integration into the national economy is now under way; it will be completed by September 1986. On the basis of the results of the study, steps will be taken to promote expansion of the fishing fleet as well as to improve the supply of the on-shore processing facilities with a view to increasing value added.

8. In order to promote the development of the small industry and crafts sector, implementation of the reform of the incentive system under the Investment Code will start in the first half of 1987 on the basis of a study now in progress. The price liberalization policy begun in 1985 and 1986 will be continued. This will make it possible to prevent monopolistic situations and to encourage greater efficiency on