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August 31, 1982

To: Members of the Executive Board

From: The Secretary

Subject: People's Republic of the Congo - Staff Report for the 1982 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1982 Article IV consultation with the People's Republic of the Congo. A draft decision appears on page 14.

This subject will be brought to the agenda for discussion on a date to be announced.

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INTERNATIONAL MONETARY FUND

PEOPLE'S REPUBLIC OF THE CONGO

Staff Report for the 1982 Article IV Consultation

Prepared by the Staff Representatives for the 1982 Consultation with the People's Republic of the Congo

Approved by J.B. Zulu and S. Kanesa-Thasan

August 27, 1982

I. Introduction

The 1982 Article IV consultation discussions with the People's Republic of the Congo were held in Brazzaville during the period June 18-July 1, 1982. The Congo continues to avail itself of the transitional arrangements of Article XIV. The representatives of the Congo included Mr. I.O. Lekoundzou, Minister of Finance; Mr. C. Oye Mba, Governor of the Bank of Central African States (BEAC), Mr. G. Bokilo, National Director of the BEAC; Mr. A. ıkantsi, Secretary General of the Ministry of Planning; and other senior officials of ministries and agencies concerned with economic and fin[illegible]l matters. The staff team consisted of Messrs. M. Sidibé (head-AFR), [illegible]ronquist (AFR), J. Harnack (AFR), A. Abisourour (ETR), Ms. A. Mullor-[illegible]n (INST), and Miss Y. Georges (secretary-AFR).

II. The Economic Background

The Congo has a population of about 1.6 million, some 40 per cent of whom live in the two main urban areas. Educational enrollment and adult literacy in the Congo are among the highest in sub-Saharan Africa. Over the last decade the public sector's role in the economy has expanded rapidly, with its share currently estimated at about three quarters of non-oil and one half of total gross domestic product (GDP). Foreign private participation remains important in key sectors such as petroleum, forestry, construction, and commerce. Meanwhile, the economy has become increasingly dependent on the petroleum sector, whose share in GDP grew from less than 2 per cent in 1970 to 33 per cent in 1980 and an estimated 36 per cent in 1981 (Table 1 and Chart 1). Consequently, developments in the economy parallel movements in oil production and prices.

In the early 1970s crude oil production, which expanded rapidly following the coming on stream of the first offshore field, fostered economic growth. The economic boom, however, was short-lived, as oil output declined due to geological and technical factors; in 1975-77 oil producti[illegible] averaged only 82 per cent of its 1973-74 level. With the recession in industrial

Table 1 People's Republic of the Congo Selected Economic and Financial Indicators, 1979-82

	1979	1980	1981	1982 Est.
	(Annual percentage changes)			
Production and prices				
Real GDP	9.8	15.8	14.5	11.0
Of which: mining sector	(13.0)	(21.0)	(24.8)	(11.9)
GDP deflator	13.7	22 8	22.4	18.2
Consumer prices	7.4	7.6	16.7	
Government finance				
Revenue	-8.3	127 5	78.5	15 2
Oil	(73.3)	(159.0)	(114 5)	(7 0)
Non-oil	(-33 1)	(102.8)	(42 5)	(27 5)
Grants	-76 4	-100.0	--	..
Expenditure and net lending	-16.9	106.0	46 7	23 2
Current	(-29.2)	(106.7)	(16.9)	(28.1)
Capital	(121 6)	(143.4)	(157.8)	(15 0)
Net lending	(214.3)	(-100 0)	(--)	(--)
Money and credit				
Domestic credit	10.1	17 2	25 8	...
Central Government (net)	(-0.2)	(5 3)	(-80 2)	(.)
Other	(15 6)	(22.8)	(68 2)	(.)
Broad money (M_2)	21 8	36 7	50 3	
Velocity (GDP relative to M_2)	6.4	6.5	6.2	.
Interest rate (one-year savings deposits, end of period)	6.5	6 5	6.5	6 5
External sector				
Exports, f o.b 1/	55 8	82.3	31 7	6.7
Of which petroleum	(56 6)	(109 7)	(44 4)	(6 8)
Imports, f o b 1/	31.4	49 1	64 0	6 3
Export volume	18.7	9 5	19 8	6 4
Of which petroleum	(7 6)	(24 5)	(23 5)	(8 6)
Import volume	20.8	31 5	73.7	2.5
Terms of trade (deterioration -)	15.0	44 9	14.0	-4 4
Nominal effective exchange rate (depreciation)	1.9	3 8	-0 5	-0 6 2/
Real effective exchange rate (depreciation -)	-1 1	-4 1	0 4	-4 7 2/
	(In per cent of GDP)			
Central government savings 3/	0 8	4 1	17 7	13 2
Central government balance (deficit -) 4/	-4 2	-3 5	3 7	1 6
External financing (net)	-0 4	2 5	-0 4	
Domestic bank financing (net)	--	0 3	-3 5	
Gross domestic investment	30 3	32 8	40 9	39 6
Gross domestic savings	19 2	32 2	24 0	26 5
External current account deficit 5/	8 3	10 1	23 3	18 2
External debt, inclusive of use of Fund credit	64 8	56 0	52 0	45 4
Debt service ratio 6/	14 6	6 8	9 2	12 0
Interest payments 6/	5 8	3.4	3 0	3 6
	(In millions of SDRs)			
Overall balance of payments	8 4	64 3	54 1	57 2
Gross official reserves (weeks of imports, c i f)	5 5	7 3	6 8	9 4
External payments arrears	26 7	4.1	1.7	--

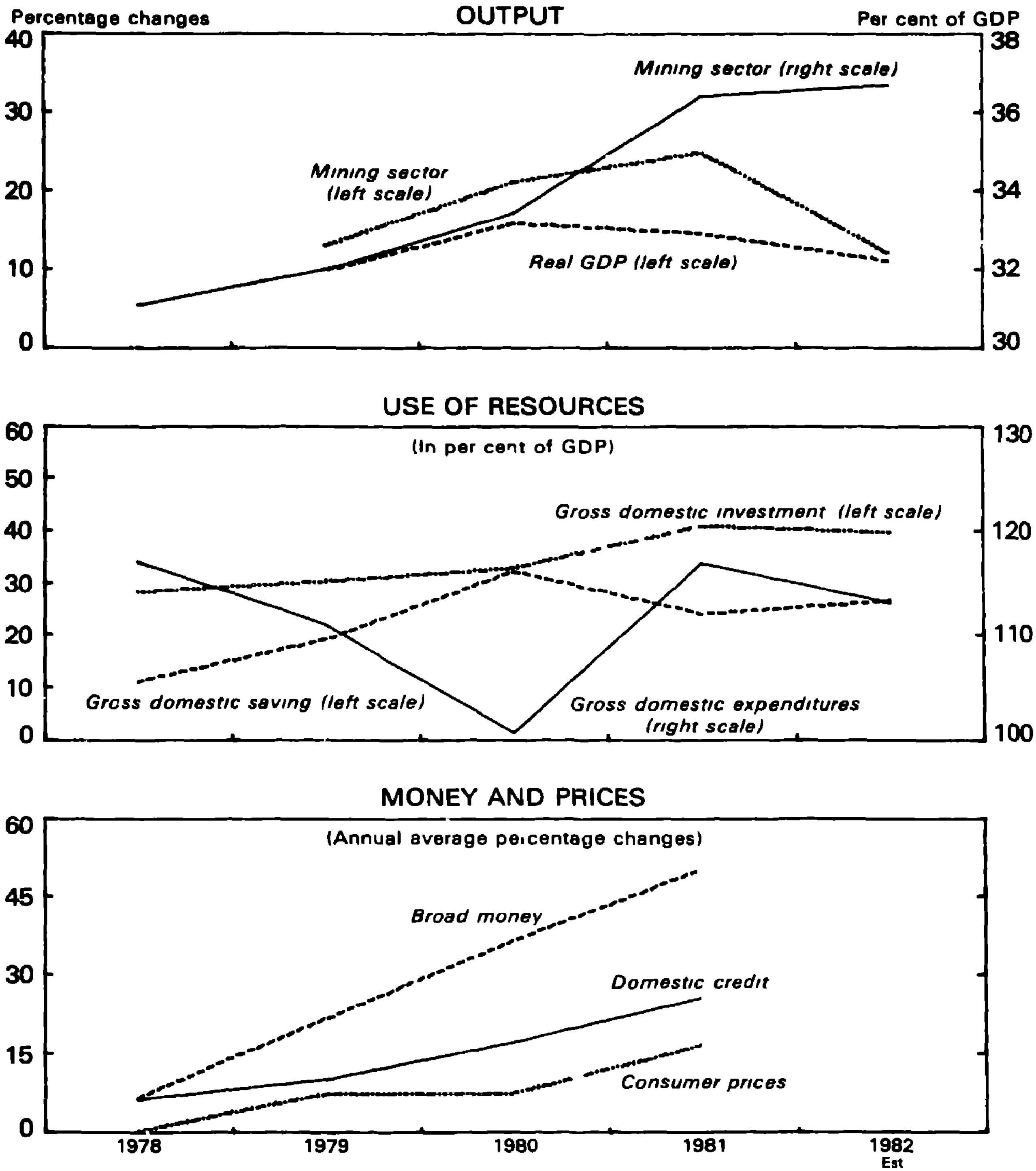
Sources Data provided by the Congolese authorities, and staff estimates.

1/ Based on SDRs.
2/ First half.
3/ Excluding grants.
4/ Commitment basis
5/ Including public transfers.
6/ Scheduled, as per cent of exports of goods and nonfactor services, including the Fund

CHART 1

PEOPLE'S REPUBLIC OF THE CONGO

OUTPUT, USE OF RESOURCES, AND MONEY AND PRICES, 1978-82



Sources Data provided by the Congolese authorities, and staff estimates countries also adversely affecting the forestry sector, the Congo's economic situation deteriorated markedly during that period. Real GDP declined at an average annual rate of 3 per cent in the three years 1975-77. Since 1978 petroleum output has recovered dramatically. Following a 35 per cent increase in that year to 2.42 million tons, it rose steadily to 4.10 million tons in 1981. Despite the continued stagnation of agriculture and forestry, real GDP growth averaged an estimated 13 per cent during 1979-81.

The recovery in oil production, together with favorable world prices, resulted in increasingly large external and budgetary receipts. Crude oil exports, which rose by 57 per cent in 1979 and more than doubled in 1980, rose further by 44 per cent in 1981 to SDR 807 million. Thus, although import payments increased rapidly, the trade balance has been in surplus since 1978. However, owing to large and increasing net services and transfer payments related to the oil sector and to the growing interest payments on external debt, the current account deficit deteriorated markedly over the period and particularly in 1981, when it reached SDR 369 million, or the equivalent of 23 per cent of GDP (Chart 2). With the improved oil prospects, the country was able to mobilize large foreign resources in the form of long-term private and public borrowings, which, after falling in 1979, more than doubled over the two subsequent years to reach SDR 403 million in 1981. In that year private sector short-term borrowing also rose substantially. Consequently, notwithstanding the rapid increase in debt amortization, the overall balance of payments, which turned around from a deficit equivalent to SDR 24 million in 1978 to a surplus of SDR 8 million in 1979, improved further in 1980-81, when the surpluses averaged SDR 59 million. By early 1982 the Congo was able to liquidate all external payments arrears, while improving its external reserve position. Nonetheless, at the end of 1981 gross official reserves represented only about two months of 1981 imports (c.i.f.).

Notwithstanding the substantial growth of resources accruing from the oil sector, in 1979-80 the budgetary situation remained weak. This reflected inadequate expenditure restraint measures and poor non-oil revenue performance. During these two years, non-oil revenue, on average, remained at the 1978 level owing in part to deficiencies in tax collection as well as to the continued difficult financial position of the state enterprises. In relation to nominal GDP, budgetary expenditure and net lending, 1/ which had declined to 25 per cent in 1979, rose again to 36 per cent in 1980. As a result, the budgetary deficit remained relatively large, representing about 4 per cent of GDP in each of the two years (Table 1 and Chart 3). Although in this period the budgetary deficit fell below its 1978 level, available means of financing were inadequate, and payments arrears, largely domestic, continued to accumulate.

As a result of these developments, a major objective of the stabilization program adopted by the authorities in 1979 was not achieved. The

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1/ Excluding part of central government investment financed by foreign grants and loans.

program, which was supported by a one-year stand-by arrangement (EBS/79/197) in the second credit tranche in an amount of SDR 4 million, or 15.7 per cent of the Congo's current quota, aimed essentially at improving public sector finances and strengthening the balance of payments. In particular, the fiscal deficit was to be reduced to a level that could be financed without any further accumulation of arrears. Since this performance criterion was not observed, the Congo's drawings under the stand-by arrangement were limited to the first two scheduled purchases totaling SDR 2 million.

In 1981 budgetary resources from the oil sector more than doubled to CFAF 126 billion. Non-oil receipts grew by 42 per cent, owing to the high level of economic activity and the improvement of tax administration, notably through the introduction of a prepayment system (perception par anticipation). As a result, total budgetary revenue rose to CFAF 210 billion, 1/ compared with CFAF 117 billion in 1980 and CFAF 52 billion in 1979. Thus, notwithstanding the continued rapid expansion of government spending, there was a major turnaround in the overall balance, from a deficit of CFAF 12.6 billion in 1980 to a surplus of CFAF 18.9 billion in 1981. This enabled the Treasury to meet public external debt obligations, virtually eliminate external payments arrears, and improve its position with the banking system. At the end of 1981 the banking system's net claims on the Government had been reduced to CFAF 4 billion from CFAF 22 billion as of end-1980. At the same time, the Treasury was able to discharge its other current payments obligations on a timely basis, thereby contributing to improving the liquidity of the economy and stimulating economic activity. However, domestic arrears, which were tentatively estimated at CFAF 75 billion at the end of 1980, were reduced by only 10 per cent to some CFAF 68 billion, or the equivalent of 32 per cent of 1981 budgetary revenue. Although no breakdown is available, indications are that these arrears are largely owed to state enterprises.

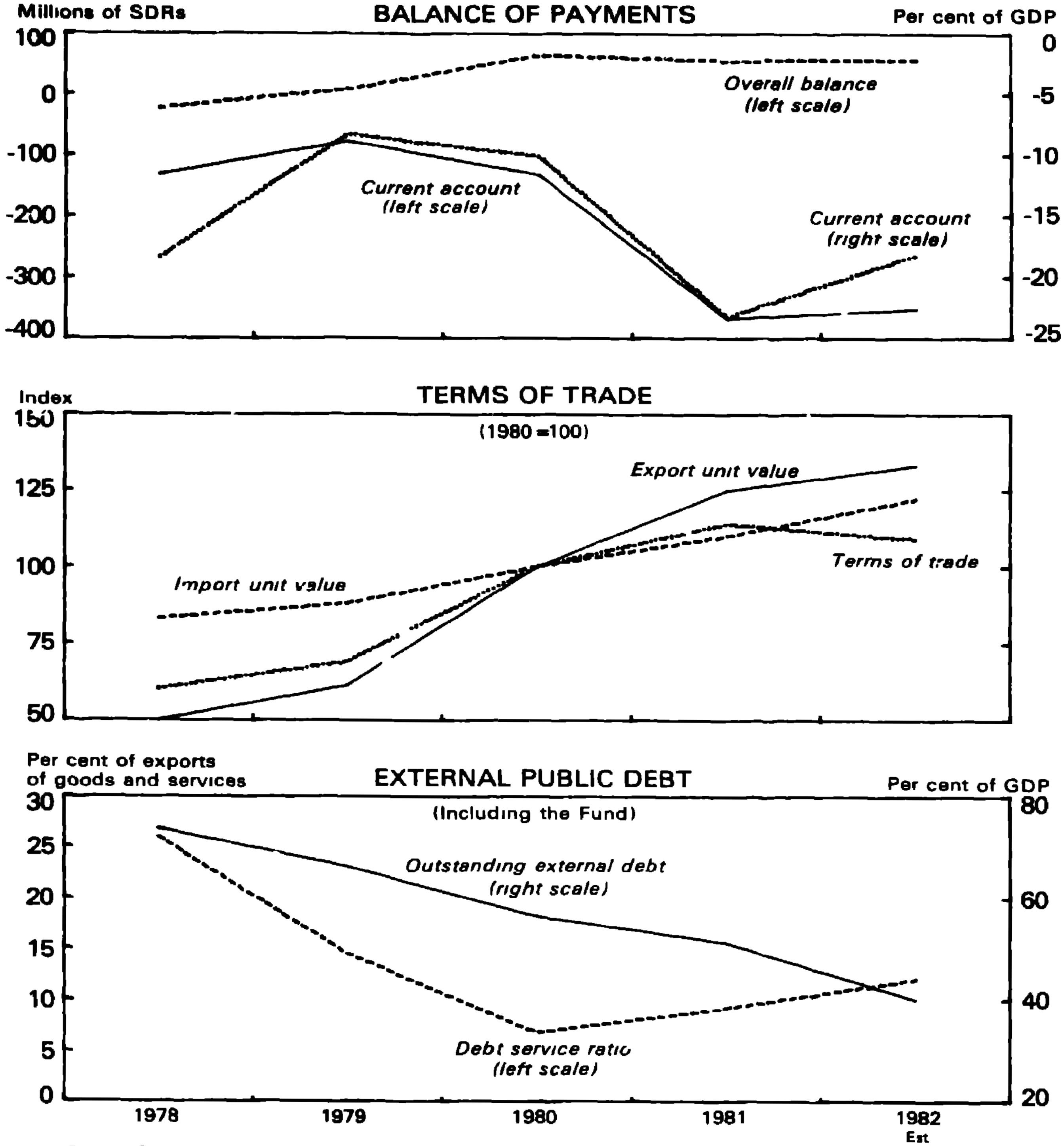
Reflecting a renewed confidence in the economy, demand for credit rose sharply. In contrast to 1979-80, when it averaged 19 per cent, the growth rate of credit to the economy accelerated to 68 per cent in 1981. This was largely attributable to credit to the private sector, whose share, after declining in 1979-80, increased rapidly to represent two thirds of the total in 1981, partly on account of medium-term borrowing by oil companies matched by an increase in commercial banks' foreign liabilities. With the turnaround in the budgetary situation, net government borrowing was significantly reduced and domestic credit expanded by 26 per cent in 1981, compared with an average of 14 per cent in the two preceding years. As the external position improved considerably, the expansion of broad money, which was below that of nominal GDP in 1979-80, reached 50 per cent, compared with a nominal GDP growth of 40 per cent. Indications are that these developments, coupled with the depreciation of the CFA franc pari passu with the French franc, intensified pressures on domestic prices. As measured by movements in the European consumer price index, inflation accelerated to 17 per cent in 1981 from an average of 7.5 per cent in 1979-80 (Chart 1).

1/ As of August 25, 1982, SDR 1 = CFAF 374.624.

CHART 2

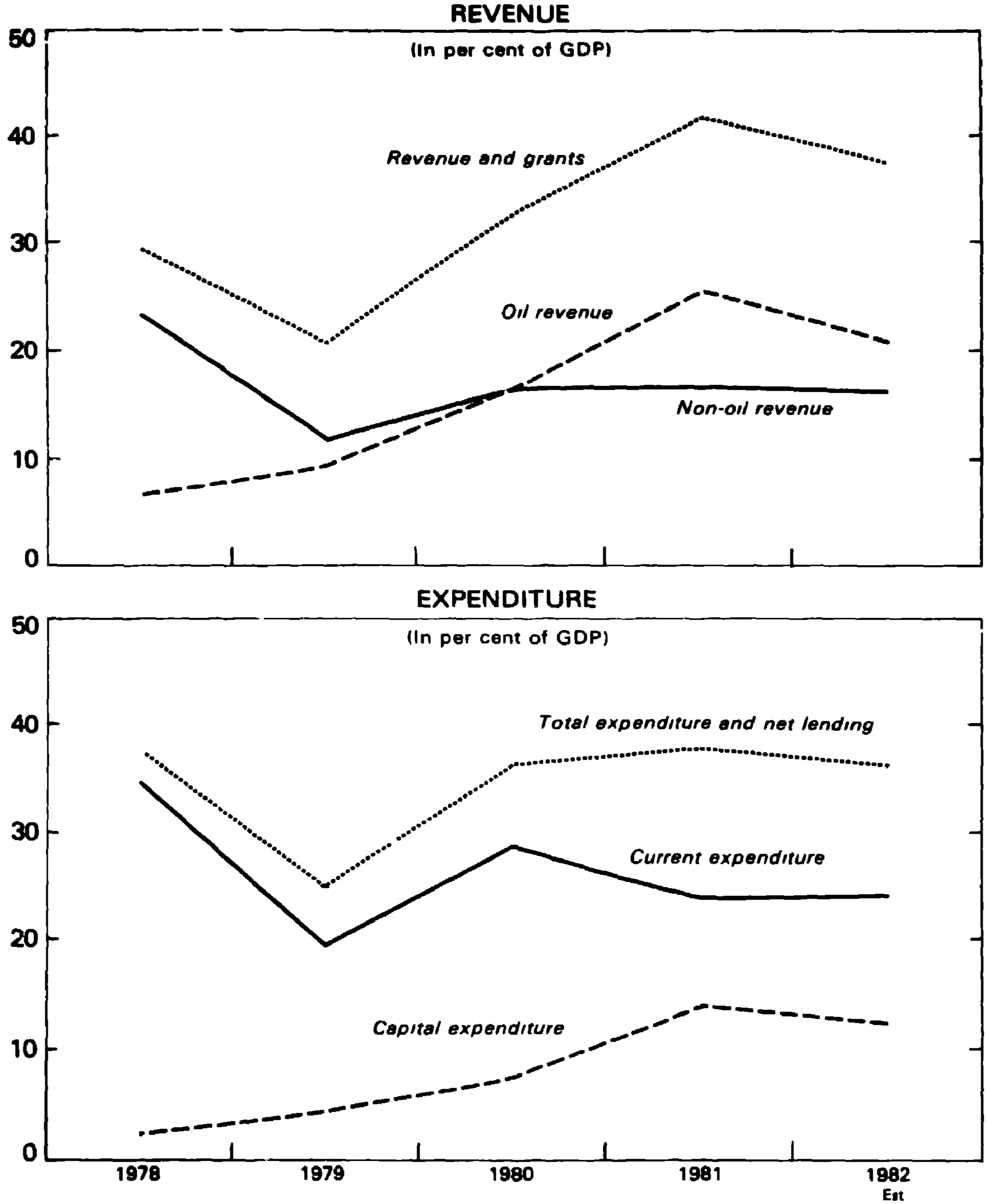
PEOPLE'S REPUBLIC OF THE CONGO

EXTERNAL INDICATORS, 1978-82



Sources Data provided by the Congolese authorities, and staff estimates

CHART 3
PEOPLE'S REPUBLIC OF THE CONGO
CENTRAL GOVERNMENT FINANCE, 1978-82



Sources: Data provided by the Congolese authorities and staff estimates.

The expansion of the public sector's role in the economy stemmed from the nationalization of existing private companies and the creation of new state enterprises in line with the Government's desire to control and direct economic development. In early 1980 there were 68 state-owned enterprises and 6 mixed enterprises, including the 2 commercial banks. Many of these state enterprises are small government agencies and those engaging in large-scale production are few, with the 6 largest accounting for close to two thirds of their total output and over one half of their employment. The state enterprises dominate the manufacturing, modern agricultural, transportation, and utilities sectors. Owing to inappropriate investment, employment, and pricing policies, as well as weaknesses in management, the economic performance of these enterprises remained unsatisfactory throughout the 1970s. Their financial difficulties also mounted, requiring increasing government subsidies. Such subsidies were estimated at CFAF 6 billion in 1980, but no information is available on subsidies channeled through the investment budget. Their financial difficulties became acute toward the end of the decade, prompting the Government in 1980 to adopt a number of measures aimed at rehabilitating them. These included the settlement of their debt to the Government through a compensation scheme and the establishment of rehabilitation programs for the major enterprises. The National Management Center (CENAGES), which was created in 1978 to provide state enterprises with technical and management assistance, was entrusted with the follow-up of the execution of these measures.

For 1982, crude oil production is estimated to increase by 12 per cent, or about half the 1981 rate, to 4.6 million tons. Consequently, although most other sectors are expected to expand faster than in 1981, GDP growth is projected to slow down to 11 per cent in 1982. Assuming an average export price of US$31 per barrel, oil export receipts could expand by 7 per cent to SDR 861 million in 1982. Together with larger net transfers, this would more than offset the increase in payments for imports and net services, and the current account deficit is expected to decline from 23 per cent of GDP to 18 per cent in 1982. As net capital inflows are expected to remain at a relatively high level owing to large private and public foreign borrowings, the overall balance of payments surplus is forecast to reach the equivalent of SDR 57 million. Because of the continued growth of oil and non-oil revenue, the latter due to continued rapid GDP growth and the general application of the prepayment system, total budgetary revenue is projected to increase by 17 per cent. Thus, the 1982 budgetary outcome is likely to remain favorable, despite an estimated 23 per cent increase in government spending. The rapid expansion of current budget expenditure is largely attributable to the more than doubling of interest payments on the public debt as well as to the 32 per cent growth of the wage bill, owing mainly to the Government's decision to raise civil servants' monthly wages and salaries by CFAF 7,000-CFAF 10,000 and to the impact of the Government's long-standing policy of offering employment to all school and university graduates. Public debt service payments are budgeted to rise sharply in 1982 reflecting the debt reschedulings in 1978-80, the increased borrowings since 1980, the takeover by the Government of debt obligations of a number of state enterprises, and the depreciation of the CFA franc.

III. Report on the Discussions

1. Economic development policies

Following the rapid and large rise in resources accruing from the oil sector, in 1981 the Congolese authorities adopted the first Five-Year Economic and Social Development Plan, covering the period 1982-86. According to the Congolese representatives, the plan is designed to set the stage for self-sustained economic growth in the post-petroleum era and aims at achieving three primary objectives: (i) the development and unification of the national territory through the improvement of the basic physical infrastructure; (ii) the revival of the productive base and the creation of conditions propitious to its future expansion, notably through the rehabilitation of state enterprises; and (iii) the improvement of the living standards of the population. The plan envisages total investments of CFAF 1,970 billion (at 1981 prices), of which CFAF 1,110 billion represents investments by the public sector; of the remainder, oil sector investments would account for up to 70 per cent. It is estimated that these investments would help achieve an annual GDP growth of 10 per cent. The plan does not provide annual investment tranches; on average, the volume of investment could reach CFAF 394 billion, compared with CFAF 208 billion in 1981.

The public sector investment program, the core of the plan, devotes about 44 per cent of total investment to physical infrastructure, particularly transportation (roads, rail, and waterways), energy and water, and urban and rural infrastructure; 37 per cent to agriculture, forestry and industry, including resources to rehabilitate the state enterprises; and the balance to social and administrative infrastructure. During the plan period 70 per cent (CFAF 780 billion) of public sector investment would be undertaken by the Central Government. On an annual basis, such investment expenditure under the budget would be CFAF 156 billion, compared with CFAF 71 billion in 1981.

The availability of resources, both domestic and foreign, for the financing of the plan is critically dependent on prospects for the oil sector. These prospects are clouded, not only by uncertainties concerning world market conditions and exchange rate movements but also by the peculiar characteristics of the Congolese oil fields which make the Congo a high-cost producer. The oil fields are relatively small and difficult to exploit, additional large investments in exploration, research, and development are therefore essential determinants of the time profile of oil production. Most scenarios indicate that oil output will decline after the mid-1980s. The Congolese authorities assume that, with the coming on stream of additional oil fields, oil output will increase steadily to 7.5-8.0 million tons in 1985 and decline thereafter. Assuming further an average price of US$32 per barrel and an exchange rate of CFAF 250, the plan forecasts that oil resources accruing to the public sector will be CFAF 900 billion, about the mid-point of a projected range of CFAF 650 billion to CFAF 1,200 billion. Taking into account the likely evolution of non-oil revenue, current expenditure, and debt service, the plan envisages that some CFAF 400 billion would be available for the investment budget. The remainder (CFAF 380 billion) of central government investment would be financed with foreign loans. With borrowing by state enterprises projected at CFAF 280 billion, total public external borrowing would amount to CFAF 660 billion (SDR 1.9 billion).

Since the plan was adopted, the volume of oil output for 1982 and 1983 has been revised downward by 13 per cent and 20 per cent, respectively, to 4.6 and 5.5 million tons. The staff team noted that this provided clear indications of uncertainties regarding the volume of resources likely to become available during the plan period. Also, the planned level of investment does not seem consonant with the absorptive capacity of the economy. Moreover, during the early years of the plan investment spending is likely to be concentrated on infrastructure, notably road and building construction, and will not have an immediate impact on the productive base of the economy. Therefore, in all likelihood, strong pressures will be exerted on the labor and goods and services markets, and thereby on the general level of prices as well as on the external position.

The Congolese representatives responded that their authorities were mindful of the short-lived oil boom experience of 1973-74 as well as of the likely inflationary impact of their current development efforts. For this reason, they have adopted a flexible approach to development planning. Investment targets under the plan would be adjusted annually in light of experience and changing circumstances, particularly with respect to the oil sector prospects. They added that, in the choice of investments, priority would be accorded to those projects which have a larger impact on production as well as the living standards of the population. Moreover, in the area of transportation, priority would be given to those infrastructure projects which would foster economic integration, thereby ensuring a greater flow of goods and services from the producing to the consuming areas. In their view, the inadequate transportation and distribution networks have hampered the development of agriculture, forestry, and to some extent domestic industry. The successful easing of these bottlenecks would also exert downward pressures on domestic prices. As regards potential shortages in the labor market, they noted that relief could only be achieved in the medium- to long-term, as it would require the structural reform of the educational system to achieve a better balance of supply and demand in this market. In the meantime, however, pressures were not expected to be unduly high because additional efforts would be made to expand vocational training, especially in the construction trade, and also immigration from neighboring countries was likely to increase.

The rehabilitation of state enterprises is essential for the future growth of manufacturing and agriculture. For state enterprises in these sectors, the rehabilitation programs included in the development plan call essentially for the modernization and expansion of capacity to be financed mostly with government transfers and foreign borrowing. In the circumstances, the staff stressed that, to ensure efficient use of resources, the planned infusion of capital should be made contingent upon the adoption and effective implementation of measures designed to improve these enterprises' economic efficiency and financial performance. These include careful investment choices, flexible employment and pricing policies, and better management. While they shared these views, the Congolese representatives observed that in practice the strict application of this principle may prove to be difficult, as undercapitalization and government-imposed policies had also contributed to the poor performance of these enterprises. As regards future policy, they stated that during the plan period efforts would be concentrated on the rehabilitation of existing enterprises, while expansion of the public sector through the creation of new enterprises would be limited. In this respect, the Government would preferably seek association with private domestic and foreign capital, especially in the forestry sector, which needs to be revitalized.

Since 1975 minimum wage rates have remained unchanged. The Congolese representatives stated that, in an attempt to limit pressures on domestic prices, the Government would maintain prudent income policies and avoid general increases in wage rates. In line with this policy stance, and following the substantial increase in budgetary resources, in 1982 the Government decided to raise civil servants' monthly wages and salaries by lump sums. With respect to public enterprises, wage awards would be tied to productivity gains. In any event, all requests for wage increases would be carefully examined in light of the enterprises' financial situation.

2. Financial policies

The recent improvement in the budgetary situation reflects the upsurge in oil revenue rather than a fundamental readjustment of budgetary policy. For a number of years the Government maintained an expansionary fiscal policy stance in the face of poor revenue performance. The resulting large budgetary deficits were financed, as mentioned earlier, in part by a substantial accumulation of payments arrears. A major factor in the expansion of government spending has been the growing financial burden of the Government's educational and recruitment policies. Scholarships are liberally granted, and all graduates of schools and universities unable to find a job elsewhere are offered employment by the Government. According to tentative estimates made in the plan, on the basis of present policies new recruitment in the civil service is likely to increase from 3,860 in 19[illegible] to 8,800 in 1986. Therefore, during the plan period the annual rate of growth of civil service employment will be 10 per cent, as against 8.8 per cent in 1976-81.

The Congolese representatives were keenly aware of the policy implications of these prospects, and recognized that the availability of domestic resources for development financing will be critically dependent not only on oil resource prospects but also on the fiscal policy stance. Accordingly, a medium-term objective of budgetary policy is to raise the ratio of non-oil receipts to current expenditure (excluding debt service) to 75 per cent from 57 per cent in the 1982 budget. This would require determined efforts to contain the growth of current expenditure and to mobilize additional domestic budgetary resources. Given its structure, containing current spending necessarily involves a readjustment of both recruitment and educational policies. This is all the more important because the recurrent costs of investment projects are likely to impose a rapidly increasing burden on the budget. However, noting that employment-creation opportunities associated with the planned investments would fall substantially short of demand, the Congolese representatives observed that a rapid and drastic change in the government recruitment policy would be difficult to effect in view of its social consequences. Moreover, the beneficial impact of a structural reform of the educational system could only be felt in the medium- to long-term. They nonetheless shared the view that this underscored the necessity to adopt timely adjustment measures in these areas. Meanwhile, the authorities will endeavor to strengthen all mechanisms for more effective control of both current and investment outlays. This includes the rationalization of budget preparation to take account of actual needs of government ministries and departments, established on the basis of the preceding year's results, the improvement of procedures for procurements, which should entail significant reductions in costs, and more realistic project evaluation and costing.

On the revenue side the objective is to make the tax system more elastic. To that end the Government intends to revise the tax system, especially the customs tariff and the investment code, with a view to adapting them to the new economic conditions and objectives. In the immediate future tax collection will be improved further, notably through a more systematic tax audit and the substantial reduction of exemptions, so as to increase tax yield within the framework of the existing legislation. It is also hoped that the successful rehabilitation of the state enterprises would enable them to discharge their tax liabilities.

As explained by the Congolese representatives, current spending under the 1982 budget does not fully reflect the medium-term objective because of a number of special factors. Almost 60 per cent of the anticipated rapid growth of personnel outlays is attributable to the impact of the Government's decision to raise civil servants' wages and salaries and the emoluments of the diplomatic personnel. The upgrading of salary scales, which had been suspended during 1978-81, as well as the provision of appropriations for the partial settlement of wage and salary arrears, have also been contributing factors. Total wage and salary arrears are estimated at CFAF 2 billion, of which about 28 per cent is to be liquidated in 1982. However, the cost of new recruitment still represents 28 per cent of the total increase in personnel outlays. The Congolese representatives attributed the relatively rapid growth of other current outlays for 1982 to the sharp increase in interest payments on the public debt, the significant upward adjustment in scholarship rates, and the implementation of the plan to settle government arrears vis-à-vis state enterprises and other domestic creditors. Appropriations for such settlements amount to some CFAF 3.4 billion.

Regarding monetary policy, the Congolese representatives stated that its primary objective remained the promotion of economic growth, while endeavoring to maintain price stability. Accordingly, the monetary authorities' credit policy stance continued to be accommodative. In their opinion, the recent rapid expansion of credit to the economy was not a cause for immediate concern and should be viewed in the light of the revival of economic activity in the non-oil sector after an extended period of sluggish growth. Nonetheless, they were concerned about the sharp expansion (159 per cent) of nonrediscountable credit by commercial banks during the two years ended March 1982; over this period deposit liabilities of banks more than doubled, reflecting in part the improved liquidity of the economy. Moreover, following the recent upsurge in budgetary revenue, the ceiling on government borrowing from the Central Bank will be substantially adjusted upward at a time when government recourse to central bank financing of development projects is likely to become important. Consequently, it will be essential to ensure a better coordination between budgetary and monetary policies; this may require greater effectiveness of credit control. The Congolese representatives added that the monetary authorities will keep developments in these areas under review and would not rule out the activation of the reserve ratio, which is a more effective credit control instrument, especially at a time of increasing commercial bank liquidity. While recognizing that a more active interest rate policy could also be useful, they indicated that this may prove more difficult to achieve because the monetary authorities consider that easy money helps promote investment. With respect to providing incentives for greater retention of private funds in the country, they pointed out that interest rates on large deposits were freely negotiable.

3. External policies and exchange system

Following the 1973-74 oil boom the Congo resorted to significant foreign borrowing to sustain a large investment program. However, as the boom was short-lived, the budgetary situation deteriorated rapidly, and this, together with the poor performance of state enterprises, led to an accumulation of substantial external payments arrears and to debt rescheduling. After the significant recovery of oil production and the gradual reduction of external arrears, the Congo's credit standing has improved quickly over the last three years, and foreign borrowing accelerated anew. On the basis of data compiled by the Caisse Congolaise d'Amortissement, with World Bank technical assistance, external public debt outstanding rose by 60 per cent in the two years ended December 31, 1981, when it amounted to CFAF 263.8 billion (SDR 861.0 million), equivalent to 52 per cent of 1981 GDP. The Central Government accounts for two thirds of this total, the remainder representing debt of the state enterprises, notably the transportation company. Reflecting the debt rescheduling efforts as well as the sharp increase in export receipts, the debt service ratio declined from 14.6 per cent in 1979 to 6.8 per cent in 1980. However, it rose to 9.2 per cent in 1981 and is expected to reach 12 per cent in 1982 and 13.2 per cent in 1983. This, combined with the large external borrowing foreseen in the plan, may rapidly exert pressure on the country's external debt servicing capacity. The Congolese representatives observed that they will endeavor to preserve the country's renewed creditworthiness. For this reason, as a matter of policy, infrastructure projects will be financed through domestic public savings and official development assistance, while external borrowing on conventional terms will be reserved for directly productive projects where the rate of return at least equals the cost of borrowing. Moreover, steps have been taken to improve centralization and coordination in the area of debt contracting.

The Congo's currency, the CFA franc, is pegged to the French franc at the rate of CFAF 1 = F 0.02. During the period 1977-80 the import-weighted nominal effective exchange rate appreciated steadily at an average annual rate of 2.5 per cent. Since then the trend has been reversed, reflecting the depreciation of the French franc vis-à-vis the U.S. dollar and other major currencies. In real terms, the import-weighted effective exchange rate remained stable in 1977-79 but depreciated by 4 per cent in 1980, stabilized in 1981 and depreciated again by 5 per cent in the first half of 1982. The Congolese representatives stressed that the exchange rate of the CFA franc should be seen in the light of the Congo's membership in a monetary union as well as of the marked improvement of the country's external position. The common exchange rate may not always be appropriate for each individual member country, but the solidarity aspect of the arrangement is an element to which they attach great importance. The authorities were of the view that the current exchange rate was appropriate to their circumstances. The Congo maintains an exchange system that is free of restrictions on payments and transfers for current international transactions.

IV. Staff Appraisal

The economy of the Congo has expanded rapidly since 1978, following the recovery in oil output, and the country's external position has also improved markedly. However, reflecting the continued expansionary fiscal policy stance, the budgetary situation remained precarious until 1981, when an upsurge in oil resources brought about a substantial turnaround in government finances. Despite this recent improvement, the country suffers from weaknesses in economic management. The economy has become increasingly dependent on the oil sector, while performance in the traditional export sectors, agriculture and forestry, has remained sluggish. Moreover, the state enterprises' output has been well below capacity and their financial situation remains weak. Furthermore, although external arrears have been liquidated, the Government is still saddled with large outstanding domestic arrears.

In 1982 the economy is forecast to grow at a relatively rapid pace. With resources accruing from the oil sector expected to remain substantial, the budget and balance of payments are both likely to be in surplus. The medium-term resource prospects also seem promising. Oil production is expected to decline only during the second half of the 1980s. With a view to channeling these resources to sectors that would promote self-sustained growth in the post-petroleum era, the first Five-Year Development Plan gives priority to physical infrastructure, agriculture, forestry, and industry through the rehabilitation of state enterprises, as well as to improving the living conditions of the population. The basic priorities of the plan may be justifiable and could help promote growth in the non-oil sector of the economy. However, the planned level of investment does not seem consonant with the absorptive capacity of the economy. Moreover, the sectoral distribution of public investment is such that, during the first years of the plan, public spending will be concentrated on infrastructure, notably road and building construction. As a result, the planned increases in investment expenditures are likely to exert pressure on domestic prices and the external position. In view of the constraints in the area of exchange rate policy arising from the Congo's membership in a monetary union, the maintenance of relative price stability is essential for the growth of the non-oil sector of the economy. Thus, it will be important to contain public spending at levels consistent with the economy's absorptive capacity. In this respect, the authorities' decision to adopt a flexible approach and adjust investment targets annually in light of experience and changing circumstances is appropriate. The decision to restore conditions for growth in the manufacturing and agricultural sectors through the rehabilitation of state enterprises is also justified and should be implemented quickly and with determination. To ensure efficient use of resources, transfers to and borrowings by these enterprises should be accompanied by, if not made contingent upon, the effective implementation of corrective measures designed to improve their economic efficiency and financial performance. These measures should include careful investment decisions, flexible employment and pricing policies, and better management.

To contain inflationary pressures, prudent demand management and income policies will be crucial. In this respect, fiscal policy will have to play a key role. In the light of past experience and of the considerable uncertainties surrounding oil prospects, a more prudent fiscal policy stance is called for. To that end, determined efforts should be made to contain the growth of spending, particularly current expenditure, and mobilize additional domestic resources. Given the structure of the current budget, this will involve a timely readjustment of recruitment and educational policies. The authorities' stated policy of raising the ratio of non-oil budgetary receipts to current expenditure (excluding debt service) is a step toward limiting the expansion of current expenditure. The budgetary control system should also be strengthened and great care exercised in the selection, evaluation, and costing of investment projects. A better coordination of budgetary and monetary policies would also be warranted. Credit policy should be less accommodative and designed to supplement fiscal policy, while avoiding any overheating of the economy. In this regard, it would be helpful to ensure greater effectiveness of credit control through the activation of the reserve ratio and a more active interest rate policy.

Although the overall balance of payments position improved recently, owing to the sharp increase in oil receipts accompanied by substantial foreign borrowing, the external current account imbalance has widened significantly and debt service obligations are rising. More prudent demand management policies, including a flexible investment policy and restraint in the area of external borrowing, is thus necessary to avoid creating excessive pressures on the external position of the country. At the same time, the authorities' declared policy of borrowing on conventional terms only for the financing of projects with high rates of return should be effectively implemented; this would help preserve the country's borrowing capacity. With the improvement in the country's absorptive capacity, access to international capital markets will become important in the medium term, especially if oil prospects were to be less favorable than currently projected.

V. Proposed Decision

The following draft decision is proposed for adoption by the Executive Board:

1. The Fund takes this decision in concluding the 1982 Article XIV cousultation with the Congo, in light of the 1982 Article IV consultation with the Congo conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

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

People's Republic of the Congo - Relations with the Fund

(As of July 31, 1982)

Date of membership	July 10, 1963
Status	Article XIV
Quota	SDR 25.5 million
Intervention currency	The CFA franc, issued by the Bank of Central African States (BEAC), is pegged to the French franc at the rate of CFAF 1 = F 0.02.
Local currency/SDR equivalent	CFAF 373.05 = SDR 1
Fund holdings of currency	SDR 22.22 million (87.1 per cent of quota)
Net cumulative allocation of SDRs	SDR 9.72 million
Holdings of SDRs	SDR 0.96 million, or 9.8 per cent of the net cumulative allocation
Trust Fund loans disbursed	
First period	SDR 5.39 million
Second period	SDR 7.32 million
Gold distribution	11,126 fine ounces
Direct distribution of profits from gold sales	US$2.09 million

Staff contacts and technical assistance

The last Article IV consultation discussions were held in December 1978; the staff report (SM/79/90), together with a request for a one-year stand-by arrangement (EBS/79/197) and for a Trust Fund loan (TR/79/11), was discussed by the Executive Board on April 25, 1979. The Board decision on the consultation was:

1. This decision is taken by the Executive Board in concluding the 1978 consultation with the Congo, pursuant to Article XIV, Section 3, of the Articles of Agreement.

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

People's Republic of the Congo - Relations with the Fund (concluded)

A staff team visited Brazzaville in May 1979 to help implement the program, and in December 1979 to review the performance under the program.

Discussions on another program were begun in February 1980 in Brazzaville and continued in April 1980 in Washington. No agreement was reached.

A staff member of the Bureau of Statistics visited Brazzaville in November 1981 to collect data for the Government Finance Statistics Yearbook.

People's Republic of the Congo - Financial Relations with the World Bank Group

(As of July 31, 1982)

(In millions of U.S. dollars)

A. IBRD/IDA program of lending operations	Disbursed		Undisbursed	
	IBRD	IDA	IBRD	IDA
Agriculture (livestock)	--	5.3	--	0.3
Education	5.6	4.0	2.4	--
Mining (potash)	30.0	--	--	--
Petroleum	--	2.2	--	2.8
Transportation				
Highways	--	5.5	--	--
Railways	38.0	22.3	--	14.4
Total	73.6	39.3	2.4	17.5
Less: Amortization	-31.4	-0.1		
Outstanding, excluding undisbursed	42.2	39.2		

B. IFC investments	Disbursed	Undisbursed
Equity	--	0.2
Loans	--	3.5
Total	--	3.7

Memorandum item:

IBRD/IDA gross disbursements 1/	
FY 1977	9.2
FY 1978	9.2
FY 1979	17.8
FY 1980	7.0
FY 1981	12.3

Source: World Bank Group.

1/ Fiscal year July 1-June 30.

People's Republic of the Congo - Basic Data

Area, population, and GDP per capita

Area	342,000 square kilometers
Population: Total (1981 estimate)	1.6 million
Growth rate	2.7 per cent
GDP per capita (1981)	SDR 896

	1978	1979	1980	1981	1982 Est.
GDP (at market prices)					
Total (in billions of CFA francs)	203.9	254.5	361.9	507.5	666.0
Agriculture (per cent of real GDP)	(11.3)	(10.6)	(9.5)	(8.9)	(8.3)
Mining (per cent of real GDP)	(31.1)	(32.0)	(33.4)	(36.4)	(36.7)
Manufacturing (per cent of real GDP)	(9.2)	(8.8)	(8.3)	(8.3)	(9.0)
Government (per cent of real GDP)	(14.9)	(13.9)	(12.7)	(11.6)	(11.0)
Percentage change in real GDP	...	9.8	15.8	14.5	11.0
Gross investment as per cent of nominal GDP	28.2	30.3	32.8	40.9	39.6
Prices (per cent change)					
GDP deflator	...	13.7	22.8	22.4	18.2
Consumer prices	10.1	8.1	7.2	17.0	18.0
Central government finance		(In billions of CFA francs)			
Revenue	56.3	51.6	117.4	209.6	241.4
Of which: oil revenue	(13.1)	(22.7)	(58.8)	(126.1)	(134.9)
Grants	3.7	0.8	--	--	4.0
Expenditure and net lending	75.9	63.1	130.0	190.7	235.0
Current	(70.1)	(49.6)	(102.5)	(119.8)	(153.5)
Capital	(5.1)	(11.3)	(27.5)	(70.9)	(81.5)
Net lending	(0.7)	(2.2)	(--)	(--)	(--)
Overall surplus or deficit (-), commitment basis	-15.9	-10.7	-12.6	18.9	10.4
Arrears	13.7	6.4	4.6	-7.1	-4.0
Overall surplus or deficit (-), cash basis	-2.2	-4.3	-8.0	11.8	6.4
Foreign financing (net)	0.8	-0.8	9.1	-2.2	...
Domestic financing (net)	-1.8	1.1	-2.5	-9.6	...
Debt rescheduling	3.2	4.0	1.4	--	--

People's Republic of the Congo - Basic Data (concluded)

	1978	1979	1980	1981	1982 Est.
Money and credit			(Per cent change)		
Domestic credit	6.4	10.1	17.2	25.8	...
Central Government	17.3	-0.2	5.3	-80.2	...
Other	1.3	15.6	22.8	68.2	...
Money and quasi-money	7.0	21.8	36.7	50.3	...

	1978	1979	1980	1981 Prov.	1982 Est.
Balance of payments			(In millions of SDRs)		
Exports, f.o.b.	246.2	383.7	699.3	920.8	981.2
Imports, f.o.b.	-213.7	-280.9	-418.7	-686.7	-730.0
Trade balance	32.5	102.8	280.6	234.1	251.2
Services and private transfers (net)	-202.8	-212.1	-462.1	-649.9	-662.9
Current account balance	-170.3	-109.3	-181.5	-415.8	-411.7
Official transfers	37.2	32.7	48.6	46.8	58.4
Capital account (net)	118.6	63.8	149.6	425.0	410.6
Official	(95.3)	(43.6)	(148.6)	(100.1)	(92.1)
Private	(23.3)	(20.2)	(1.0)	(324.9)	(318.5)
Errors and omissions (net)	-13.1	12.9	40.9	--	--
Allocation of SDRs, Trust Fund, and valuation changes	3.7	8.4	6.6	-1.9	--
Overall surplus or deficit (-)	-23.8	8.4	64.3	54.1	57.2
Current account deficit as per cent of GDP	18.4	8.3	10.1	23.3	18.2
Gross official foreign reserves (end of period)	8.8	36.6	72.5	109.6	162.0
In weeks of imports, c.i.f.	1.7	5.5	7.3	6.8	9.4
External public debt					
Disbursed and outstanding (end of period)	590.2	623.2	703.8	861.0	972.9
Debt service as per cent of exports of goods and non-factor services					
Excluding the Fund	26.1	14.6	6.7	9.1	11.9
Including the Fund	26.1	14.6	6.8	9.2	12.0