

DOCUMENT OF INTERNATIONAL MONETARY FUND
AND NOT FOR PUBLIC USE

**FOR
AGENDA**

SM/82/246

CONTAINS CONFIDENTIAL
INFORMATION

December 30, 1982

To: Members of the Executive Board
From: The Acting Secretary
Subject: Mauritania - 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 Mauritania. A draft decision appears on page 23.

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

Att: (1)

Other Distribution:
Department Heads

INTERNATIONAL MONETARY FUND

MAURITANIA

Staff Report for the 1982 Article IV Consultation

Prepared by the Staff Representatives for the 1982
Article IV Consultation with Mauritania

Reviewed by the Committee on Article IV Consultations

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

December 28, 1982

I. Introduction

The 1982 Article IV consultation discussions with Mauritania were held in Nouakchott during the period September 30-October 19, 1982. The discussions also included a comprehensive review of the program for 1981 under a stand-by arrangement which ended on March 31, 1982. The Mauritanian representatives included Mr. Ahmed Ould Zein, Governor of the Central Bank, Mr. Sidi Ould Ahmed Deya, Minister of Finance; Lt.Col. Ann Amadore Babaly, Minister of Planning and Regional Development; and other ministers and senior officials of ministries and agencies concerned with economic and financial matters. The staff team consisted of Messrs. Ch. A. François (head-AFR), Buu Hoan (AFR), Mrs. M. Tyler (ETR), Mr. J. Tavares (FAD), Mr. Y. Fassassi (EP-AFR), and Miss C. Elwell (secretary-AFR).

An 18-month stand-by arrangement in an amount of SDR 29.7 million (174.7 per cent of former quota), in support of a program covering calendar years 1980 and 1981, was approved by the Executive Board on July 23, 1980 (EBS/80/154). Following a review of the program for 1980 and the adoption of the program for 1981, on June 5, 1981 the existing stand-by arrangement was canceled and replaced by an augmented arrangement for SDR 25.8 million for the duration of the arrangement ending March 31, 1982 (EBS/81/118), which took into account the increase in quota resulting from the Seventh Review of Quotas. The amount of Fund resources purchased by Mauritania under the two stand-by arrangements totaled SDR 34.7 million, or 136.1 per cent of present quota, of which SDR 17.5 million represented ordinary resources.

Mauritania continues to avail itself of the transitional arrangements of Article XIV. A summary of Mauritania's relations with the Fund and the World Bank group is provided in the Appendices.

II. Background and Recent Economic Developments

1. Background

The Mauritanian economy experienced substantial structural changes in the 1970s as a result of a severe and prolonged drought in 1970-72, the Government's decision in 1973 to take full control of the country's main economic and financial activities, and a sharp scaling up in public investment and defense expenditure between 1975 and 1978. Because of the drought, agriculture declined sharply, livestock herds were decimated, and part of the rural and nomadic population drifted to the edges of urban centers in search of food and employment. Following Mauritania's withdrawal from the West African Monetary Union (WAMU) and the French franc area in June 1973, the Government established an independent central bank and national currency, nationalized all commercial banks and the mining sector, and created a number of state enterprises to promote production and exports. At the same time, with substantial foreign financial assistance, Mauritania launched a large-scale investment program aimed at expanding the country's infrastructure and creating an industrial base.

Reflecting the expansionary investment policy, weak economic management, and a sharp deterioration in the terms of trade, the Mauritanian economy incurred increasing internal and external imbalances during the period 1973-78. In addition, between 1975 and 1978 Mauritania was involved in the armed conflict over the Western Sahara, which led to a sharp increase in government current expenditures and to disruptions to the mining and shipping of iron ore. As a result of these factors, the current account deficit of the balance of payments (before official grants) rose from the equivalent of 2 per cent of GDP in 1973 to 40 per cent in 1978. The sharp increase in government expenditures for investment and national defense, together with a slow growth in government revenue, caused a substantial widening in the overall fiscal deficit. The implication of this growing financial gap for pressures on domestic resources and on the balance of payments were masked to a considerable extent by a large inflow of external grants and concessional loans. However, the increased foreign borrowing caused the level of the external indebtedness to increase from 27 per cent of GDP in 1973 to 126 per cent in 1978, while the debt service ratio rose sharply to 35 per cent, despite the concessional nature of most of the loans contracted. Despite the large investment effort, especially for infrastructure and industry, the growth in real GDP was negligible, with most of the increase registered in the livestock and the service sectors.

Following a military coup d'état in July 1978, Mauritania gradually withdrew from the conflict over the Western Sahara and reached a formal peace agreement in August 1979. Simultaneously, the new Government undertook to implement various adjustment measures to redress the difficult economic and financial situation.

2. An overall view of adjustment efforts during 1978-81

Since mid-1978, the Mauritanian Government has sought to redress the large domestic and external imbalances by pursuing corrective policies in the framework of both a medium-term rehabilitation plan prepared with assistance from the World Bank and consecutive short-term programs supported in 1978/79 by a loan from the Trust Fund and in 1980-81 by a stand-by arrangement which ended in March 1982. The principal strategy of these adjustment programs was to restrain the growth of consumption severely while stimulating and restructuring domestic supply. This was to be achieved by: (1) adherence to restrained wage, fiscal, and monetary policies; (2) structural reform of the public enterprises sector, the banking system, and tax administration; (3) bilateral renegotiation of part of the external debt and strict debt management, (4) restructuring the fishing sector and the investment policy, (5) and maintenance of an exchange and trade system virtually free of restrictions together with the adoption of a realistic exchange rate policy. These programs also provided for an increase in public investment to expand production and export capacity and enlarge the transportation infrastructure since a large amount of external project aid remained available at concessional terms, mainly from Arab oil-producing countries and the People's Republic of China. As nonproject budgetary aid was expected to decline, the programs aimed at substantially reducing the budget and external current deficits. It also provided that, in the event external budgetary assistance exceeded a minimum forecast level, bank credit to the Government would be reduced by a corresponding amount so that the sum of such credit and foreign aid would conform to the program objective for the budget deficit.

Following implementation of most of the adjustment policies between 1978 and 1981 and a sharp recovery in production and exports, most of the program's objectives were achieved, and the performance criteria under the stand-by arrangements were met except for two interim test dates (June 30 and September 30, 1981). However, despite initial steps taken by the authorities during 1980-81, the implementation of a number of important structural measures in the areas of tax administration, public enterprises, and the banks fell short of expectations. In addition, with the exception of a 2 per cent correction in February 1982, the understanding in respect of exchange rate policy was not carried out. For the period 1978-81 as a whole, the reduction in domestic and external imbalances resulted from a sharp recovery in production and exports and a stabilization in real consumption which led to an increase in national savings (Table 1). In contrast to a decline of 4 per cent in 1978, real GDP is officially reported to have expanded at an annual rate of 6 per cent during 1979-81. On average,

Table 1 Mauritania Selected Economic and Financial Indicators, 1978-82

| | 1978 | 1979 | 1980 | | 1981 | | 1982 |
|--|--------|--------|---------|--------|---------|--------|--------|
| | Actual | Actual | Program | Actual | Program | Actual | Est |
| (Annual per cent changes unless otherwise specified) | | | | | | | |
| National income and prices | | | | | | | |
| GDP at constant prices | -4.4 | 5.5 | | 3.7 | | 8.5 | 4.0 |
| GDP deflator | 8.6 | 5.9 | | 8.0 | | 3.3 | 5.0 |
| Consumer prices (Upper income group) | 7.1 | 9.1 | | 11.1 | | 18.7 | 12.1 |
| External sector (on the basis of SDRs) | | | | | | | |
| Exports, f.o.b. | -22.3 | 20.3 | 19.7 | 32.4 | -- | 51.9 | -5.5 |
| Imports, f.o.b. | -14.7 | 3.7 | 16.3 | 11.5 | 31.5 | 12.8 | 22.9 |
| Non-oil imports, f.o.b. | -18.9 | -3.3 | 13.4 | 18.3 | 13.4 | 23.1 | 25.0 |
| Export volume | -20.0 | 20.0 | . | 20.5 | | 34.1 | -7.5 |
| Import volume | -17.7 | -8.3 | | -2.7 | | 26.5 | 14.3 |
| Terms of trade | -14.9 | -12.2 | | -2.9 | | 7.9 | -1.7 |
| Nominal effective exchange rate 1/ (depreciation -) | -8.2 | -6.7 | | 0.7 | | 19.6 | 8.6 2/ |
| Government budget | | | | | | | |
| Revenue, excluding grants | 14.7 | 16.1 | 6.9 | -17.0 | 22.8 | 36.7 | -0.3 |
| Total expenditures | 26.2 | -1.5 | -7.3 | -13.6 | -1.0 | 14.1 | 6.0 |
| Money and credit | | | | | | | |
| Domestic credit | 3.2 | 5.3 | 37.3 | 18.0 | 22.2 | 15.8 | 28.3 |
| Government | -68.8 | 71.0 | 248.4 | 86.3 | 98.7 | 43.2 | 97.3 |
| Private sector | 9.8 | 4.5 | 9.0 | 11.4 | 9.9 | 11.4 | 12.1 |
| Money and quasi-money | 2.0 | 13.4 | 19.8 | 20.5 | 21.8 | 33.7 | 21.9 |
| Velocity (GDP relative to M2) | 4.7 | 4.1 | 4.3 | 4.4 | 4.2 | 3.9 | 3.2 |
| Interest rate (annual maximum deposit rate) | 6.0 | 6.0 | 9.0 | 9.0 | 9.0 | 9.0 | 9.0 |
| (In per cent of GDP) | | | | | | | |
| Central Government | | | | | | | |
| Budget deficit 3/ | | | | | | | |
| Excluding grants | 24.2 | 18.7 | 12.6 | 13.8 | 8.3 | 9.1 | 12.7 |
| Including grants | 5.2 | 4.7 | 11.7 | 8.7 | 5.6 | 5.2 | 11.7 |
| Domestic bank financing | -2.1 | 1.3 | 8.2 | 2.5 | 4.4 | 2.1 | 6.7 |
| Foreign financing (including grants) | 23.9 | 17.0 | 4.4 | 11.3 | 3.8 | 8.0 | 4.3 |
| Gross domestic investment | 26.7 | 24.8 | | 36.0 | | 38.2 | 37.7 |
| Gross national savings | -13.0 | -11.9 | | 0.2 | | 5.5 | -6.4 |
| External current account deficit 4/ | | | | | | | |
| Excluding grants | 39.6 | 36.6 | 36.3 | 36.2 | 44.6 | 32.7 | 45.8 |
| Including grants | 13.5 | 16.6 | 28.7 | 20.4 | 40.8 | 18.4 | 37.8 |
| External debt outstanding 5/ | 125.5 | 116.1 | | 125.5 | | 131.9 | |
| Debt service ratio (in per cent of exports of goods and services) 6/ | 21.6 | 32.7 | | 16.5 | . | 20.3 | 16.6 |
| Interest payments (in per cent of exports of goods and nonfactor services) | 6.8 | 8.9 | | 7.4 | | 6.5 | 8.0 |
| (In millions of SDRs unless otherwise specified) | | | | | | | |
| Overall balance of payments | -5.7 | 18.9 | -30.0 | -29.7 | -18.0 | 28.7 | -38.2 |
| Gross official reserves (months of imports) | 3.9 | 5.3 | | 5.8 | | 5.6 | 3.5 |
| Outstanding external arrears on external debt | 22.8 | 14.5 | -- | 38.6 | -- | 20.4 | |

Source: Data provided by the Mauritanian authorities, and staff estimates

1/ Trade weighted, period average

2/ First ten months

3/ On budget year basis, and including amortization of external debt

4/ Excludes rescheduled interest payments

5/ Including use of Fund credit

6/ Actual debt service payments

the highest growth rates were recorded in the fishing sector (24 per cent per annum); the rural sector (9 per cent per annum), with livestock expanding steadily over the period and cereal production increasing somewhat more moderately; and the tertiary sector (4 per cent per annum). After the cessation of hostilities, iron ore output increased by 24 per cent in 1979 to more normal prewar levels and then was maintained at a level of about 8.5 million tons despite weak world demand for minerals. As nominal consumption increased very little during the period because of very strict budgetary and income policies, gross national savings, as a proportion of GDP, moved from a negative ratio of 13 per cent in 1978 to a positive level equivalent to 5.5 per cent in 1981. At the same time, the share of gross capital formation in total GDP increased from 27 per cent in 1978 to 38 per cent in 1981 following the implementation of government projects in the areas of mining, agriculture, and transportation. In spite of this acceleration in investment, the current account deficit of the balance of payments (before official grants and net of debt relief), declined from 40 per cent of GDP in 1980 to 33 per cent in 1981. However, because of the shift in the composition of foreign assistance toward loans, the current account deficit, including official grants, rose from 14 per cent of GDP to 18 per cent.

a. Fiscal performance

Under the financial programs, the overall budget deficit (before grants) 1/ was targeted to be reduced from UM 5.1 billion (19 per cent of GDP) in 1979 to UM 4 billion in 1980 and to UM 3 billion in 1981 (Tables 2 and 3). The medium-term objective was to eliminate this deficit by 1984. On a budgetary year basis, which includes a three-month complementary period, the actual budget deficit declined to UM 4.2 billion (14 per cent of GDP) in 1980 and to UM 3.1 billion (9 per cent of GDP) in 1981 2/. The deviations from the program targets resulted basically from shortfalls and lags in government revenue, reflecting partly a loss of royalties from the fishing sector associated with the new fishing policy and a reduction of the tax burden on mineral production, and more importantly, widespread tax exemptions, tax evasions, and administrative weaknesses in enforcing tax collections. To compensate for these shortcomings, the authorities kept total nominal budgetary expenditure in 1979-81 at a level below that of 1978, with reduction in security outlays, general expenditure, and net lending, a freeze on expenditure for materials and supplies, and a slight increase in expenditure for civilian personnel. The larger-than-programed budget deficits were financed mainly by external budgetary assistance and by a small increase in payments arrears. Although lower than in 1978-79, the external assistance was about twice the minimum level (UM 1.4 billion) forecast in the program. Therefore, the authorities limited net recourse to the banking system to levels which were consistent with the adjusted program ceilings (Table 2).

1/ The budget includes amortization of external debt but excludes public investment financed by external resources.

2/ On the basis of more comprehensive data on Treasury operations, which were not available during previous missions, it is now estimated that the actual cash deficit on a calendar-year basis only declined from UM 5 billion in 1979 (19 per cent of GDP) to UM 4.6 billion (15 per cent of GDP) in 1980 and to UM 4.1 billion (12 per cent of GDP) in 1981.

Table 2. Mauritania: Execution of Financial Programs, 1978-81

| | 1978 <u>1/</u> | 1979 <u>1/</u> | 1980 <u>2/</u> | 1981 <u>3/</u> |
|--|----------------------------------|----------------|----------------|----------------|
| <hr/> | | | | |
| <u>Overall budget deficit before grants <u>4/</u></u> | <u>(In billions of UM)</u> | | | |
| Target | 3.8 | 3.6 | 4.0 | 3.0 |
| Outcome | 5.9 | 5.1 | 4.2 | 3.1 |
| As a percentage of GDP | 24.2 | 18.7 | 13.8 | 9.1 |
| <u>Net increase in domestic credit</u> | <u>(Annual rate of increase)</u> | | | |
| Initial target | 23.1 | 16.1 | 32.1 | 22.2 |
| Adjusted target <u>5/</u> | 23.1 | 16.1 | 18.6 | 15.9 |
| Outcome | 3.2 | 8.2 | 18.0 | 15.8 |
| <u>Net increase in credit to the Government</u> | <u>(Annual rate of increase)</u> | | | |
| Initial target | 99.0 | 25.0 | 303.0 | 98.3 |
| Adjusted target <u>5/</u> | 99.0 | 25.0 | 151.1 | 52.6 |
| Outcome | -68.8 | 71.0 | 86.3 | 43.2 |
| <u>Current account deficit before grants</u> | <u>(In millions of SDRs)</u> | | | |
| Target <u>6/</u> | 176 | 255 | 192 | 271 |
| Outcome <u>6/</u> | 166 | 167 | 183 | 195 |
| As a percentage of GDP | 39.6 | 36.6 | 36.2 | 32.7 |
| <u>Current account deficit net of imports related to aid</u> | <u>(In millions of SDRs)</u> | | | |
| Target <u>6/</u> | -- | -- | 56 | 61 |
| Outcome <u>6/</u> | 81 | 99 | 94 | 80 |
| As a percentage of GDP | 19.4 | 21.7 | 18.5 | 13.4 |
| <u>Overall balance of payments</u> | <u>(In millions of SDRs)</u> | | | |
| Target | -22.0 | -10.0 | -30.0 | -18.0 |
| Outcome <u>7/</u> | -5.7 | 18.9 | -29.7 | 28.7 |
| As a percentage of GDP | -1.4 | 4.1 | -5.9 | 4.8 |

Source: Data provided by the Mauritanian authorities; and staff estimates.

1/ Financial program supported by a loan from the Trust Fund and adopted in July 1978 (TR/78/40). Although the program ended on May 31, 1979, the authorities continued their adjustment policies during the whole of 1979.

2/ Stand-by arrangement approved in July 1980 (EBS/80/154).

3/ Stand-by arrangement approved in June 1981 (EBS/81/118).

4/ On budget year basis, and including amortization of external debt.

5/ Adjusted for the amount of external aid in excess of UM 1.4 billion.

6/ Excluding debt service payments rescheduled.

7/ Including change in external payments arrears.

Table 3. Mauritania. Policy Measures Under the 1980-81 Stand-By Program Status of Implementation

| 1980-81 Program | Status of Implementation |
|---|--|
| 1. <u>Fiscal measures</u> | |
| a. No general increase in wages | Implemented |
| b. No new recruitment except for certain essential services and students returning from abroad | Implemented |
| c. Revision of tax code | A new tax code promulgated in 1982 |
| d. Reduction of tax exemptions | Not Implemented |
| e. Improvement of tax administration | Limited progress |
| f. Taxpayers' census to enlarge tax base | Census completed but not implemented |
| 2. <u>Monetary measures</u> | |
| a. Increase in interest rates by 1-3 percentage points | Effectuated on August 4, 1980 |
| b. Limits on credit expansion to both the private sector and Government | Credit expansion was within program limits |
| c. Gradual reduction of the banks' outstanding short-term foreign liabilities | Not Implemented |
| d. Restructuring of the commercial banking system | Limited progress |
| 3. <u>Public enterprises</u> | |
| a. Restructuring of SNIM | Implemented |
| b. Price and tariff adjustments | Tariff adjustments for water and electricity and wharf services Sharp price increases for basic commodities sold by SONIMEX |
| c. Reduction in operating expenses | Implemented in the case of SONIMEX Limited progress from other public enterprises |
| 4. <u>External sector measures</u> | |
| a. Limitation to US\$30 million in 1980 and US\$40 million in 1981 on new borrowing of nonconcessional nature | Implemented |
| b. Correction of the sharp effective appreciation of the ouguiya in 1981 | Only limited correction (2 per cent) thus far |
| c. A revision of the system of determining the exchange rate | A review was undertaken in April 1982, but no steps have been taken for implementation of necessary changes |
| d. Complete elimination of certain import restrictions by the end of the program period | Implemented |

b. Monetary policy

Reflecting the lower-than-programmed bank financing of the Government and the strict control on the growth of credit to the economy, total domestic credit was kept within the quarterly ceilings for 1980. During part of 1981, credit to the Government temporarily exceeded the ceilings because of considerable delays in the disbursement of external aid. With the large inflow of foreign aid in the last quarter, credit to the Government was reduced to below the ceiling for December 1981, and payments arrears, which had been accumulated during the first nine months of the year, were settled. Credit to the economy, which also increased more than envisaged during the first nine months of 1981, was sharply reduced during the last quarter of the year as a result of a rapid collection of outstanding claims and the settlement of payments arrears by the Government. For the year as a whole, total domestic credit expanded by 16 per cent and was marginally less than the ceiling for December 1981. As foreign assets of the banking system increased, instead of declining as envisaged, broad money grew by almost 33 per cent in 1981 (21 per cent in 1980).

c. Structural reforms

The tighter fiscal policy and the moderate credit stance were accompanied by measures to improve the financial performance of the public enterprise sector and to strengthen the banking system. To facilitate the expansion in mining capacity and the financing of a new project, the national mining company (SNIM) was restructured, with World Bank assistance, and its financial position has been strengthened through an increase in the equity capital (mostly foreign shareholders), additional tax exemptions, liquidation of debt due by the Government, and the divestiture of unprofitable activities. Efforts were also made to reduce the operating deficits of other public enterprises and to improve their financial structure. To that end, official retail prices for basic foodstuffs and public utilities were raised substantially during 1980-81. Nevertheless, most state enterprises continued to incur substantial losses, due primarily to inefficient management, wornout equipment, overstaffing, and an accumulation of unpaid bills due from customers. With regard to the commercial banking system some of the recommendations offered by a Fund technical assistance mission in early 1980 were implemented. However, major difficulties continued to be encountered in obtaining repayment and service of loans extended because of the weak financial situation of most of the enterprises, poor prospects for recovering delinquent loans, and the accumulation of arrears by the Government. In addition, a few banks have accumulated large amounts of overdue external trade credits which cannot be repaid because of lack of liquidity by the banks or the importers.

d. Balance of payments

Even after a number of corrections to official published data, Mauritania's balance of payments performance was significantly more favorable than foreseen under the programs. The current account deficit before official grants, which was projected to increase substantially in connection with the abovementioned investment projects, remained lower than targeted and, as a proportion of GDP, declined from 37 per cent in 1979 to 33 per cent in 1981. Excluding imports of goods and services financed by grants and those related to investment directly financed from abroad, rescheduled interest payments, and foreign technical assistance, the current account deficit was reduced from 22 per cent of GDP in 1979 to 18 per cent in 1980 and 13 per cent in 1981. Over the period 1979-81 export earnings (in terms of SDRs) more than doubled as a result of a fivefold increase in the volume of fish exports and higher prices for iron ore. During the same period import payments other than those directly financed from abroad rose at an annual average rate of 14 per cent, owing primarily to an increase in petroleum products, foodstuffs and chartering of fishing boats. Although official transfers declined by about one fourth, the current account deficit was fully financed by an increase in official capital inflows, including debt relief obtained and equity capital subscriptions to SNIM. In addition, there was a net increase of SDR 15.5 million in net foreign assets of the banking system and a SDR 2.4 million reduction in external payments arrears. With an increase in short-term official deposits with the Central Bank, Mauritania's gross international reserves rose to SDR 152 million at the end of December 1981, when they were equivalent to 5.6 months of 1981 imports.

Reflecting a continuing rapid rate of borrowing between 1978 and 1981, Mauritania's outstanding external public debt (including short-term credits and repurchase obligations to the Fund) rose by more than one third to US\$914 million by end-1981 and was equivalent to 132 per cent of GDP. As most of the increase in external indebtedness represented loans at very concessionary terms from Arab oil-producing countries and international organizations, the profile and the structure of the debt are relatively favorable, the average maturity period is 21 years, the average interest rate is 3 per cent, and the grant element is 48 per cent. Nevertheless, as a consequence of the sheer size of the external debt, scheduled debt service payments were not feasible in 1980-81, and Mauritania obtained substantial debt relief through bilateral renegotiations. As a result, the actual debt service as a ratio of exports of goods and services was limited to 16.5 per cent in 1980 and to 20.3 per cent in 1981. At the end of 1981 external arrears in respect of debt service payments amounted to SDR 20 million. In 1981 Mauritania made the final compensation payment to the former shareholders of the nationalized iron mine (which totaled US\$90 million during 1975-81).

Since January 1974, when the peg with the French franc was severed, the exchange rate of the ouguiya has been determined on the basis of a fixed relationship with a basket of currencies. After May 1977 the main objective has been to stabilize the exchange rate of the ouguiya vis-à-vis the U.S. dollar, the currency in which most of the country's exports and capital transactions are denominated. To that end, the share of the dollar in the currency basket was gradually increased from 20 per cent during 1974-77 to 72 per cent, while the share of the French franc was reduced from 33 per cent to 20 per cent. As a result of these changes and movements in foreign exchange markets abroad, during 1978-80 the ouguiya rate remained virtually unchanged relative to the U.S. dollar while depreciating relative to the currencies of Mauritania's principal trading partners, especially France, Senegal, and Spain. The import-weighted nominal index of the ouguiya showed a cumulative depreciation of 14 per cent between 1977 and 1980. With the strengthening of the U.S. dollar beginning in October 1980 and the subsequent weakening of the French franc beginning in April 1981, the trade-weighted nominal index appreciated by 20 per cent in 1981 and by an additional 9 per cent during the first ten months of 1982. In terms of the French franc and the CFA franc, which are the currencies relevant for about half of official trade, the ouguiya appreciated by 30 per cent over the last two years. When the financial program for 1981 was prepared in early 1981, the authorities indicated that they would take steps to correct the appreciation that had already taken place during the first quarter of 1981 and to revise the weights and composition of the currency basket in order to ensure a greater stability in the effective exchange rate. However, as indicated above, these intentions were not effected.

III. Report on the Discussions

The consultation discussions were conducted in conjunction with exploratory discussions on a comprehensive new adjustment program, which the Mauritanian authorities hoped could be supported by use of Fund resources in the near future. The discussions focused on the general developments and policies in 1982 and on the short- and medium-term adjustment policies required to stimulate domestic supply and further reduce Mauritania's large economic and financial imbalances. They took place at a time when a serious deterioration was being experienced in 1982, and when the main policies for 1983 had not yet been formulated.

1. Overall economic activity in 1982

Overall economic growth is estimated to have slowed down from 9 per cent in 1981 to about 4 per cent in 1982. The growth in the traditional rural sector was expected to remain relatively high because of a good agricultural harvest in 1981/82 and continued rapid expansion in livestock

production induced by favorable weather conditions. Activity in the already large trade and distribution sector was also expected to remain buoyant. These sectors, however, are largely outside government control and do not contribute to official export and tax revenues. By contrast, a decline was expected in the modern sector of the economy, which accounts for about one third of GDP. The export of iron ore, which had thus far performed relatively well despite sharply reduced world demand, was projected to decline by 10 per cent as a result of a further weakening in steel production in industrial countries. After impressive growth in 1981, fish production would stagnate at best because of the difficulties encountered in enforcing the new national fishing policy, in particular controlling illicit fishing by foreign vessels in territorial waters and preventing Mauritanian vessels from selling part of their catch illegally to the nearby Canary Islands. Lengthy electricity stoppages during part of the year, together with increased competition from imports, caused a falling-off of production in Mauritania's manufacturing sector. On the other hand, gross capital formation was projected to expand further in connection with the acceleration in the implementation of a large project to increase the production of iron ore (the Guelbs project) and continued large outlays for the fishing sector and a deep sea port.

After four years of modest wage increases and low rates of inflation, in January 1982 the minimum wage for unskilled labor (SMIG) was increased by 25 per cent and the wage bill for civil servants by 7 per cent. There is no fully adequate indicator to measure domestic inflation in Mauritania. However, reflecting an adequate supply of basic foodstuffs and continued price controls, the increase in recorded consumer prices for low-income groups has remained moderate in 1982. By contrast, the increase in the price index for European-type goods, mostly imported, has continued to be rapid (12 per cent) in 1982 despite a further appreciation of the ouguiya.

2. Economic and development policies

a. Planning

The economic and development policies, together with the investment program for the period 1981-85, are embodied in a recently adopted development plan. To restore a viable medium-term balance of payments equilibrium, the Mauritanian Government is giving the highest priority to developing further mineral, fishing, and agricultural resources, and to expanding the country's narrow transportation infrastructure. The authorities also intend to intensify their efforts to rehabilitate the public enterprise sector and with assistance from some friendly Arab countries, to reactivate some industrial plants, including an oil refinery and a sugar refinery, which were completed in recent years but could not enter into production because of technical and financial difficulties. For the period 1981-85 the plan envisages an investment target of UM 89.2 billion at 1980 prices (US\$1.8 billion), an amount substantially higher than that realized during

the period 1976-80. Most of the investment will be effected by public enterprises and the Government and will be allocated to productive sectors, with emphasis given to mining (33 per cent), agriculture (22 per cent), and industry (9 per cent). The remainder will be distributed among social infrastructure, public utilities, and housing. The Mauritanian representatives stated that about half of foreign financing required had already been committed in the form of grants or concessional loans.

While acknowledging the need to expand investment to increase Mauritania's production and reduce economic dependency on foreign aid, the staff expressed some reservations about the overall size of the investment target for the period 1981-85, especially in view of the required levels of external and domestic financing. With the exception of the large mining project now under way, the implementation of other projects was likely to be hampered by administrative and financial constraints, construction bottlenecks, and shortage of skilled labor. The mission also commented on the fact that the impressive investment effort in the 1970s had not, as acknowledged previously by the authorities, been accompanied by commensurate growth in agricultural and industrial production. In that context, the staff stressed the need to improve procedures to evaluate projects so as to ensure an adequate rate of economic return and an orderly pace of implementation. The staff added that prime consideration should also be given to efficient management of existing and future investments, adequate provision for recurrent costs, and appropriate price policies. The need to encourage smaller-scale projects which would attract private Mauritanian capital was also mentioned in the discussions. In concluding the discussions on the investment policy, the staff suggested a more realistic programming of investments and their financing so as to allow an overall assessment of their medium-term impact on the budget, the balance of payments and the external debt servicing. The Mauritanian authorities are presently undertaking this review with technical assistance from the World Bank.

b. Mining

The government project (the Guelbs) to raise production capacity of iron ore from about 10 million tons to about 14 million tons by mid-1984 is proceeding as scheduled. This project will gradually exploit new large deposits of low-grade iron ore as the reserves of an old mine are depleted. As the transportation and processing facilities of the present mine will be used, the cost of the project has been limited to US\$433 million, of which US\$60 million would be financed by the National Mining Company (SNIM). In 1983-84 the Government plans, with Arab investment, to reopen the facilities of the copper mine to extract and process sulfurous copper, as the oxide copper deposit became depleted in 1978. The Government hopes that, with the exploitation of new layers and the use of energy-saving technology, copper mining would be profitable and production could return to the 1974 level of 20,000 tons.

c. Fisheries

Given exceptionally rich fishing grounds along the Atlantic Coast, the fishing sector is the most important near-term potential source of foreign exchange and government revenue. In 1978 the value of the fish catch by some 200 vessels from 15 different countries (mainly Japan, Korea, Spain, and the U.S.S.R) was officially estimated at about US\$1 billion, of which Mauritania received only US\$23 million in the form of fishing royalties. With a view to taking full control of the exploitation of its waters, in July 1979 the Government decided to reduce the number of fishing permits granted to foreign fleets, to raise royalties, and to expand the Mauritanian fleet considerably. To that end, it encouraged the acquisition of vessels by Mauritanian individuals and companies as well as the creation of joint ventures with foreign companies. Since 1979 more than 30 new companies have been created. Notwithstanding a number of difficulties encountered in enforcing effective control of fishing activity, the new policy led to a sharp increase in foreign exchange earnings from US\$44 million in 1978 to US\$115 million in 1981. Considering that these results are still well below the potential of the sector, the Government recently decided to reinforce its control by requiring that all fish catches be disembarked in the port of Nouadhibou or be transhipped in a cargo under the supervision of the customs office. As a result of these measures, the authorities expected that total foreign exchange earnings would double in 1983 to US\$245 million, of which US\$229 million would be in the form of export receipts and US\$16 million in the form of royalties. While recognizing the large potential of the fishing sector in the medium term, the staff remarked that the achievement of the export target for 1983 will require improved port facilities, adequate marketing organization, experienced personnel, and military surveillance of the territorial waters, which would take considerable time and expenditure.

d. Agriculture

Priority is also being given in the new plan to rural development projects designed to raise agricultural output and income and to reduce Mauritania's heavy reliance on imported cereals, now equivalent to two thirds of domestic consumption. Improved incentives and extension services will be developed to encourage cultivation in the rain- and flood-fed land, which now produces most of the domestic supply of foodstuffs. At the same time, as the production on rain-fed land is subject to the vagaries of weather, emphasis will continue to be given to large irrigation projects, which are expected to raise the total irrigated area of the country from 4,000 ha in 1980 to 11,000 ha by 1985. To ensure the full utilization of the country's limited agricultural potential, the authorities intend to review agricultural producer prices, establish adequate extension services and marketing facilities, and revamp the operations of the Government's main agency (SONADER). To maintain official retail prices for rice at socially acceptable levels, the authorities intend to continue with their policy of price subsidies. They emphasized that these subsidies implied no budgetary charges, as they were financed by profits made by the government trading company (SONIMEX) on sales of other commodities.

Following heavy losses during the drought year, the livestock sector has been largely reconstituted with minimum government intervention, and contributed about one fifth of GDP in 1981. The activities of this sector are effected mostly by nomadic population outside official control, through traditional channels and border trade. Excluding exceptional movements across the borders due to climatic conditions, the illicit export of live-stock, mostly to Senegal, constitutes an important source of foreign exchange earnings (estimated at US\$40 million in 1980), which financed a significant part of unrecorded private sector imports and capital transactions. To improve supply conditions, the authorities are giving more emphasis to modern stockraising techniques. They have also reactivated a public corporation (SOMECOB), which has a monopoly on animal exports in all forms. The Mauritanian representatives are fully aware that their efforts to integrate the illicit export of livestock into official channels are made difficult by the price differential vis-à-vis Senegal, the attractive imported supplies on the Senegal market, and the convertibility of the CFA franc.

With technical assistance from the World Bank, the Government is presently carrying out a comprehensive review of the operations of the major public enterprises. The conclusions of this review will be used in early 1983 to formulate rehabilitation plans and specific measures toward improving the economic and financial performance of individual enterprises. To that end, in early November 1982 the Government created an interministerial permanent committee for the rehabilitation of public enterprises.

3. Domestic financial policies

a. Fiscal policies

Following continued improvement during 1978-81, there has been a significant deterioration of fiscal performance during 1982. While the overall budget deficit (before external aid) was targeted to decline by half to UM 2 billion (about 6 per cent of GDP), it is now estimated that the actual deficit on a calendar year basis could exceed UM 4.7 billion (or 13 per cent of GDP), reflecting primarily a stagnation of government revenue and a modest increase in total expenditure. Instead of the 37 per cent increase budgeted for 1982, government revenue was likely to stagnate, even assuming a major effort to collect taxes during the last quarter of the year. Based on actual developments through August 1982, the shortfall was due mainly to import duties and taxes on fishing exports. On the other hand, total expenditures (including amortization) are projected to rise by 6 per cent, reflecting mainly an increase in the wage bill and in interest payments on external debt. Despite this increase, the actual level of expenditure during calendar year 1982 would be kept below budgetary appropriations, as part of the appropriations has been frozen because of lack of resources. Since the level of external budgetary assistance in

the form of grants and concessional loans combined was projected to decline by nearly one half to only UM 1.6 billion, the Government was confronted with a difficult financial situation. Unless additional foreign aid could be mobilized during the last quarter, it was expected that the large financing requirements would be covered by a sharp increase in central bank advances and/or an accumulation of payments arrears with respect to supplies and external debt obligations. The increase in bank credit to the Government, including special advances against earlier purchases from the Fund, was tentatively estimated at UM 2.5 billion, an amount equivalent to 26 per cent of broad money at end-1981.

While commending the authorities for the success of their efforts in restraining expenditure, the staff sought to understand the main factors responsible for the disappointing tax performance over the last four years, especially in the context of rapid economic growth. The Mauritanian representatives acknowledged that the poor revenue performance was due to widespread tax evasion and administrative difficulties in enforcing tax collections. This reflected the lack of a well-established administrative machinery and social unresponsiveness to the tax system from a population which twenty years ago consisted mainly of nomads and farmers. The size of the country, together with the length of the borders with four countries, made it practically impossible to control all imports and exports effectively. Evasion of nonwage income taxes has been widespread, in particular by the trade, fishing, and livestock sectors. Because of weak financial performance, public enterprises have been unable to contribute as much revenue as had been anticipated. In addition, Mauritania's tax system is characterized by a large number of overlapping indirect and direct taxes, often with quite high rates. The pervasive use of specific rather than ad valorem taxes in the current inflationary environment has further diminished the built-in elasticity of the tax system. The rapid growth expected in revenue from the fishing sector has not materialized because of the remaining difficulties in implementing the new fishing policy. Finally, despite the recovery in export receipts from iron ore, government revenue from the mining sector has increased only moderately because of substantial tax concessions for SNIM, which were granted so that the mining company could finance part of its planned investment and gradually write off certain past expenditure assumed on behalf of the Government.

Notwithstanding the structural weaknesses of Mauritania's tax administration, which will take some years to correct, there are a number of areas where tax collection could be substantially improved and tax exemptions be reduced. The census of taxpayers completed in 1981 also constitutes an important instrument to enlarge the tax base and raise revenue. The recently adopted new tax code, if properly implemented, could simplify assessment and collection procedures and increase yields in spite of lower tax rates. Finally, since about half of the tax receipts are based on international trade, a more realistic exchange rate policy would have contributed to better tax performances in 1981 and 1982.

As long as the prospects for a significant revenue expansion are limited, the authorities intend to continue to enforce a strict budgetary discipline. To that end, they will continue to restrain severely the growth in employment, wages, and salaries and in expenditures for material and supplies. They also envisaged some saving measures in subsidies and transfers. Finally, they expected to reduce debt service payments through a new round of debt relief renegotiations. The implementation of a restrictive budgetary policy has been facilitated since 1979 by a significant improvement in budgetary procedures, including the closure of a large number of special accounts.

At the time of the mission, the Mauritanian authorities were not sufficiently advanced with their preparations to discuss meaningful fiscal targets for 1983. However, given the increasing uncertainties regarding foreign aid, they recognized the need for a substantial reduction in the overall deficit and the urgency for comprehensive action in 1983. It was agreed that discussions with Fund staff on the 1983 budget would take place in mid-January 1983. The staff took the position that external assistance could not be a substitute for the much needed further adjustment in the fiscal area, and that the authorities should aim at reducing the overall budget deficit to at least UM 2 billion (about 6 per cent of GDP). In the forthcoming discussions, the staff would further consider the consistency of this target with a realistic evaluation of domestic revenue and external assistance. Given the difficulties experienced in the past, a strengthening of the administrative capacity of the Treasury will be necessary to ensure an effective implementation of fiscal policies and a close monitoring of fiscal operations.

b. Monetary policies

Credit to the private sector (including public enterprises) increased at a relatively rapid pace (12 per cent) during the first half of 1982, mainly in response to short-term financing requirements of the trade and fishing sectors. The authorities indicated, however, that no further increase in private credit would be allowed during the second half of the year. Nevertheless, taking into account the large bank financing requirement of the Government during the same period, total domestic bank credit is likely to cause a sharp increase in net foreign liabilities of the banking system. Already, during the first part of 1982, net foreign liabilities increased sixfold reflecting both a sharp drop in gross domestic assets of the Central Bank and a further increase in external liabilities, including trade credits. Taking these developments into account, the growth in broad money is forecast at 22 per cent in 1982.

Although the monetary authorities have pursued a relatively restrictive credit policy toward the private sector since 1979, there have been major difficulties in controlling the growth of credit, recovering delinquent loans, and allocating adequate credit resources for development needs. This reflected the fact that a large part of the increase in credit in the

past was absorbed by public enterprises to finance operating losses and to alleviate cash problems resulting from an increase in public sector payments arrears and other accounts receivable. It also reflected inadequate evaluation of credit requests, and structural financial difficulties of private enterprises and individuals. As the Central Bank maintained a restrictive rediscount policy, the deposit money banks supplemented their resources by obtaining short-term credits on commercial terms from their affiliates abroad, with the result that net foreign liabilities of the banks more than doubled between end-1978 and June 1982 to US\$78 million, an amount equivalent to more than one fourth of private domestic credit outstanding at end-June 1982. Part of these short-term external credits is overdue.

As part of a general effort to strengthen the financial structure of the banking system and reduce the existing liquidity overhang, the Central Bank, with technical assistance from the Fund, recently took steps to upgrade the management capability of the banks and has considerably intensified its controls over banks' operations by regular auditing of banks' accounts and by increasing penalties for violation of banking legislation. Overall monthly credit ceilings have been established for each bank, including one on recourse to short-term foreign trade credits, and all credits in excess of UM 1 million (US\$20,000) are subject to prior authorization of the Central Bank. The civil code was modified to enhance the banks' ability to recover delinquent loans, and the banks have begun to write off part of their bad debts. In addition to these specific measures, a more comprehensive reorganization of the banking system is contemplated, with a view to improving the efficiency of the financial system and facilitating overall credit management and control. Although interest rates were raised by 1-3 percentage points in August 1980, in accordance with the program, there has been little reliance on interest rates as a tool for encouraging financial savings and discouraging borrowing. In view of the structural problems of the public enterprises and present banking practices, complicated by certain religious attitudes, the authorities consider that banks' clients are largely unresponsive to interest rate changes.

4. External prospects and policies

The improving trend in the balance of payments during 1978-81 has been reversed in 1982. Preliminary estimates for 1982 pointed to a very pronounced turnabout in the current account and in the overall balance resulting from a combination of factors. Overall export earnings are projected to decline by 5 per cent in SDR terms, due mainly to a fall in iron ore shipments. Following an impressive increase in 1980-81, fish exports are expected to stagnate, while fishing royalties will decline. On the other hand, import of goods and services are estimated to increase by 20 per cent, with more than half of this increase on account of the planned acceleration in investment. The remainder of the increase (SDR 50 million) reflects a 15 per cent increase in imports of petroleum products, intermediate goods for the mining company, and unspecified goods and services

financed by trade credits. As a result of these developments, the current account deficit before grants is expected to widen by 13 percentage points to 46 per cent of GDP. ^{1/} Since official grants are likely to decline by one third, the current deficit after grants as a proportion of GDP is projected to more than double to 38 per cent. A large part of this deficit will be financed by planned net concessional borrowing by the Government and the mining company. Nevertheless, an overall balance of payments deficit of about SDR 40 million is projected (compared with a surplus of SDR 30 million in 1981) unless additional untied assistance is received during the later part of the year. However, the loss of reserves is likely to be contained by a buildup of arrears in the form of delays in debt service payments by the Government.

Detailed balance of payments projections for 1983 and the medium term could not be prepared at the time of the mission, because of lack of reliable data on future investment and related financing, and because the relevant policies for 1983 were not yet formulated. However, rough estimates show that, unless substantial adjustment and rescheduling measures are taken quickly, the balance of payments will show further deterioration in 1983. As for Mauritania's medium-term external prospects, a prospective bright spot is the potential for a significant increase in iron ore production and a substantial rise in fishing exports. However, while domestic production capacities are being considerably expanded, the prospects for a rapid increase in export receipts in the short term will depend largely upon a recovery in world demand for iron ore and an efficient organization and control of the fishing sector.

The extraordinarily heavy burden of external debt service represents a worrisome weakness in the medium-term prospects. Mauritania's external indebtedness, including use of Fund resources and short-term trade credits, would reach US\$1.1 billion by end-1982, an amount equivalent to 163 per cent of GDP. Despite the concessional character of most of the loans and the bilateral reschedulings already obtained, debt service payments, even on existing debt are projected to increase rapidly during 1983-86, with peaks of 35 per cent and 41 per cent respectively in 1983 and in 1986 due to balloon amortization payments of short-term deposits with the Central Bank. The staff team pointed out that debt rescheduling would provide only temporary relief and that new borrowing even on concessionary terms would add to the debt service burden. Therefore, unless export and budgetary prospects improve significantly in the coming years, higher debt servicing would reach unsustainable levels. The Mauritanian representatives expressed a large degree of confidence that Mauritania will be able to obtain adequate debt relief through bilateral negotiations with friendly countries as well as a continued large inflow of official grants and long-term loans to finance the planned investment projects. They were, however, less optimistic about the prospects for new nonproject assistance. The Mauritanian representatives agreed with the staff that, in the future,

^{1/} When investment-related imports are netted out, the adjusted current account widened by 7 percentage points to 20 per cent.

deficits on the external current account could not be maintained at the current high level. Accordingly, it was agreed to prepare a realistic evaluation of the prospects for such capital inflows in the context of the preparation of the mediumterm balance of payments outlook mentioned above. This assessment will be crucial for the design and formulation of appropriate adjustment policies for 1983 and the medium term.

Regarding the exchange rate policy, the Mauritanian representatives explained that their policy which they have followed with some consistency since 1977, has been to stabilize the exchange rate of the ouguiya in terms of a basket of currencies used in the foreign operations, whether it caused a depreciation of the effective rate as in 1977-80 or an appreciation as in 1981-82. In their view, the large share of the U.S. dollar in the currency basket is amply justified by its dominant role in the receipts from exports and capital as well as in effecting payments for foodstuffs, petroleum products, and external debt. From a more fundamental point of view, they discounted the positive effects that a more flexible exchange rate policy would have on export volumes of iron ore and fish and on the substitution of domestically produced goods for imports, while expressing serious concern about the immediate impact on the domestic price of essential goods, such as rice, sugar, and energy. The staff replied that there has been a very substantial and continued appreciation of the ouguiya vis-à-vis the main trading partners, in particular the neighboring countries, in a context of weakening fiscal and external performances. Such an appreciation will have a number of negative consequences, both in the short and the medium term, which will hamper the adjustment efforts undertaken. The staff noted in particular the already noticeable decline in the competitive position of the agricultural and industrial sectors, the large expansion in certain imports which are likely to be re-exported illegally to neighboring countries, and the stagnation of taxes on international trade. While the effective appreciation helped the authorities to contain the increase in the domestic price of essential imported goods, it did not prevent a rapid increase in other prices. The resulting price distortions have created higher profit margins which are not taxed. Regarding the export sector, the staff agreed that a more flexible exchange policy would not necessarily stimulate export volume in the short term because of market constraints; however, it would improve the sector's net financial position, thereby providing more resources to compete on the world market, to finance new investments, and to pay income taxes or royalties. In addition, in the present context of unfavorable external prices, a more realistic exchange policy would be required. Although the staff stressed the need for early action, the Mauritanian authorities stated that given the numerous policy implications of the exchange rate issue, they would rather view it in the broader context of the formulation of a program for 1983.

Regarding the trade and payments system, the Mauritanian representatives stated that the temporary application, in January 1980, of quotas on some imports and the temporary suspension of certain other imports considered to be luxury goods and those which could be produced locally, was

first relaxed in 1981 by raising quotas, and subsequently entirely discontinued. The Mauritanian representatives expressed the view that any protection of infant industries should be provided by way of import tariffs rather than quantitative restrictions, and they added that they were in the process of reviewing import tariffs with a view to providing adequate protection to newly created industries. In June 1981, the basic limits on the sale of foreign exchange for business travel were raised. The Mauritanian representatives explained that requests for amounts in addition to the basic limits were approved in bona fide cases. No other changes were made since the previous consultation in the regulations governing payments and transfer for current international transactions, and the same limits continue to be applied on the sale of foreign exchange for tourist travel abroad and for salary remittances by foreigners working in Mauritania. These limits involve restrictions subject to Fund approval under Article VIII, Section 2(a).

As regards the reported external payments arrears in respect of debt service payments, the Mauritanian authorities explained that in part the arrears had been accumulated in anticipation of a debt rescheduling or refinancing agreement. While external payments arrears have been reduced by half in 1981, they are likely to increase again in 1982. With respect to the short-term trade credits overdue, the Central Bank stated that an appropriate arrangement was being negotiated with the interested foreign banks.

IV. Staff Appraisal

Following Mauritania's withdrawal from the conflict over the Western Sahara after July 1978, the Government undertook to redress the extraordinarily large imbalances of the country in the context of both a medium-term rehabilitation plan and consecutive short-term programs supported by Fund resources. To this end, the authorities have implemented a number of important adjustment measures aimed at reducing the budgetary and external deficits and have begun to initiate reforms and investments essential to the restoration of financial viability in the medium term. The principal measures included restrained wage, fiscal, and monetary policies, bilateral reschedulings of external debts, structural reforms of tax administration, public enterprises and banks, a restructuring of the fishing sector, and a reorienting of investments.

During 1980-81 the implementation of these measures was carried out in a manner consistent with the financial objectives and performance criteria of the 18-month stand-by arrangement ended on March 30, 1982. This achievement, coupled with a rapid recovery in domestic production (averaging 6 per cent during 1979-81), led to a reduction in real consumption and to a sharp expansion in export volumes of iron ore and fish. Though somewhat above the program's targets in absolute terms, the budget deficit

(before grants) as a ratio to GDP was reduced from 24 per cent in 1978 to 9 per cent in 1981. Domestic credit expansion to the Government and the rest of the economy as a whole was restrained within the margins provided under the program, even after taking into account an automatic downward adjustment for higher-than-expected external budgetary assistance. During the period, important adjustments were made to official prices despite a general freeze on wages, and the major restructuring of the large mining company was carried out very successfully. Major progress was also made under the new fishing policy to exploit directly the rich fishing grounds of the Mauritanian Atlantic coast. As a consequence, the ratios of the external current account gap to GDP for 1980 and 1981 were reduced in accordance with the targets of the programs, and the overall balance of payments position in these years was more favorable than envisaged, even after taking into account delays in debt service payments.

Notwithstanding the progress made during 1978-81, Mauritania's budgetary and external imbalances remain large, and their financing, even though concessional, has become more costly because of a declining trend in official grants. Moreover, the implementation of policies in certain aspects of the program, particularly the pace of reform of tax administration, public enterprises, and banks, has been disappointing. The large increase in fish exports was not accompanied as expected by a commensurate contribution to government revenue. Finally, the exchange rate vis-à-vis the U.S. dollar has been rigidly maintained, contrary to the understanding under the program and this has added cost/price distortions, discouraged production in the agricultural, and manufacturing sectors, intensified illicit trade, and aggravated external imbalances.

During 1982 Mauritania has incurred substantially higher internal and external deficits, reflecting increasing difficulties in mobilizing non-project external assistance and weaknesses in implementing effectively certain policies, in particular with respect to the fiscal area, the exchange rate, and the fishing sector. These factors were exacerbated by exogenous elements, notably the decline in iron ore shipments due to weak external demand. The major aid-financed investment projects to expand production capacities advanced as scheduled. Even after the exclusion of expenditures related to these investments, both the budget and the current account deficits showed a sharp deterioration as compared with 1981. Unless additional external budgetary assistance have been mobilized or drastic measures taken during the last quarter, the budget and balance of payments deficits for 1982 will be substantially larger than in 1981, and would lead to a serious loss in reserves or further accumulation of domestic and external payments arrears.

In the context of the deterioration experienced during 1982 and the lagging pace in the implementation of basic reforms, prospects for 1983 and the following years appear worrisome. Without adequate adjustment measures, both budgetary and balance of payments deficits will be extraordinarily large, and the external debt service ratio for the next few years is expected to rise rapidly from the current level of 17 per cent.

Even though the Mauritanian authorities are confident that they could attract longterm external assistance and obtain further debt relief from friendly oil-producing countries, they agreed that external assistance would not be a substitute for the desirable adjustments needed in certain sectors of the economy. Thus, a combination of external financing and strong internal measures should be implemented to bring about the necessary reductions in the imbalances in an orderly and efficient way. The pace of the adjustment will depend greatly on the amount of the assistance which will be available in the coming years to finance both planned investments and the current operations of the budget. Given the declining trend of grants, and the importance of containing the growth of debt service commitments, the staff believes that it is imperative for Mauritania to take early and comprehensive steps to reduce the deficit in external current account. It needs to be emphasized that debt rescheduling provides only temporary relief and that borrowing even at concessionary terms also adds to debt service.

The internal adjustment measures could, in the view of the staff, be implemented in the framework of the economic strategy defined in the new development plan. The cornerstone for an improved financial situation would have to be a determined effort to strengthen fiscal performance, in particular on the revenue side. In this regard, a strengthening of tax administration and Treasury management is indispensable. It would also be essential to take more decisive action to strengthen the structure of public enterprises (other than SNIM) and the banks and to promote agricultural development. At the same time, it will be necessary, possibly with World Bank assistance, to improve project evaluation procedures as well as the overall programming of investment in order to ensure an efficient use of resources and to prevent a further aggravation of the external debt servicing burden. In the staff's opinion, these policies should be accompanied by a correction of the appreciation of the ouguiya between 1980 and 1982 and by the adoption of a flexible exchange policy for the future.

Despite the prevailing pressures on the balance of payments, Mauritania's exchange and trade system has remained relatively liberal. The basic foreign exchange limits for business travel abroad were raised in 1981, and additional amounts were sold in bona fide cases. Limits continue to apply on the sale of foreign exchange for travel and salary remittances and their maintenance constitutes restrictions subject to Fund approval under Article VIII, Section 2(a). Given the difficult balance of payments situation and the weak net reserve position, the staff recommends the continued approval of these restrictions. The staff would urge the authorities to give the highest priority to the elimination of delays in debt service payments by the Government as part of their comprehensive adjustment program.

V. Proposed Decision

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

1. The Fund takes this decision relating to Mauritania's exchange measures subject to Article VIII, Sections 2 and 3, and in concluding the 1982 Article XIV consultation with Mauritania, in light of the Article IV consultation with Mauritania conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. The Fund notes that, despite pressures on the balance of payments, Mauritania's exchange system has remained relatively free of restrictions. In view of the circumstances of Mauritania, the Fund approves the restrictions on the sale of foreign exchange for travel and salary remittances, until March 31, 1984 or the next Article IV consultation, whichever comes first. The Fund would urge Mauritania to eliminate its external arrears as soon as possible.

MAURITANIA - Basic Data

Area, population, and GDP per capita

| | |
|--------------------------|-------------------------------|
| Area | 1.1 million square kilometers |
| Population: Total (1981) | 1.5 million |
| Growth rate | 2.5 per cent |
| GDP per capita (1981) | SDR 397 |

| | <u>1978</u> | <u>1979</u> | <u>1980</u> | <u>1981</u> | <u>1982</u> Proj. |
|--|-------------|-------------|-------------|-------------|----------------------|
| <u>(In millions of ouguiyas)</u> | | | | | |
| <u>Gross domestic product at 1973 prices</u> | 13,362 | 14,092 | 14,612 | 15,849 | 16,483 |
| Rural sector | 2,861 | 3,462 | 3,452 | 3,614 | ... |
| Of which: livestock | (2,571) | (3,085) | (3,085) | (3,233) | (...) |
| Fishing | 590 | 674 | 708 | 1,073 | ... |
| Industrial sector | 2,338 | 2,474 | 2,347 | 2,643 | ... |
| Of which: mining | (1,498) | (1,574) | (1,330) | (1,436) | (...) |
| fish processing | (166) | (141) | (222) | (337) | (...) |
| Construction, public works, and services | 6,281 | 6,229 | 6,733 | 6,973 | ... |
| Indirect tax less subsidies | 1,242 | 1,253 | 1,372 | 1,546 | ... |
| <u>Gross domestic product at current market prices</u> | 24,200 | 27,018 | 30,260 | 33,914 | 37,305 |
| <u>Resource gap</u> | 7,795 | 7,727 | 9,247 | 9,893 | 15,581 |
| <u>Gross domestic expenditure</u> | 31,995 | 34,745 | 39,507 | 43,807 | 52,886 |
| Consumption | 25,358 | 28,055 | 28,618 | 30,850 | 38,810 |
| Gross capital formation | 6,457 | 6,690 | 10,889 | 12,957 | 14,076 |
| <u>Savings</u> | | | | | |
| Gross domestic savings | -1,338 | -1,037 | 1,642 | 3,064 | -719 |
| Gross national savings | -3,138 | -3,205 | 62 | 1,852 | -2,388 |
| <u>Government finance 1/</u> | | | | | |
| Current revenue | 5,300 | 6,154 | 5,105 | 6,981 | 6,960 |
| Of which: iron ore royalties | -- | 221 | 313 | 388 | 420 |
| fishing royalties 2/ | 1,566 | 922 | 722 | 1,393 | 1,467 |
| Total expenditure 3/ | 11,375 | 11,199 | 9,677 | 11,046 | 11,709 |
| Budget deficit | 6,075 | 5,045 | 4,572 | 4,065 | 4,749 |

1/ On a calendar-year basis.

2/ Including export taxes on fish.

3/ Including amortization of external debt.

MAURITANIA - Basic Data (concluded)

| | <u>1978</u> | <u>1979</u> | <u>1980</u> | <u>1981</u> | <u>1982</u> Proj. |
|--|-------------|-------------|-------------|-------------|----------------------|
| <u>Government finance (corr'd)</u> | | | | | |
| Financing | 6,075 | 5,043 | 4,572 | 4,065 | 4,749 |
| Official grants | 4,588 | 3,902 | 1,547 | 1,331 | 390 |
| Foreign borrowing (gross) | 1,199 | 688 | 1,882 | 1,389 | 1,210 |
| Domestic borrowing | 288 | 455 | 1,143 | 1,345 | 3,149 |
| Of which: banking system | (-500) | (363) | (754) | (703) | (2,483) |
| Extrabudgetary expenditure | 5,264 | 4,849 | 7,023 | 6,116 | 6,989 |
| <u>Monetary survey (end of period)</u> | | | | | |
| Foreign assets (net) | -1,712 | -1,069 | -1,556 | -737 | -2,897 |
| Domestic credit | 9,372 | 9,922 | 11,709 | 13,557 | 17,393 |
| Claims on Government (net) | 511 | 874 | 1,628 | 2,331 | 4,814 |
| Claims on the economy | 8,861 | 9,048 | 10,081 | 11,226 | 12,579 |
| Broad money | 5,161 | 5,874 | 7,080 | 9,431 | 11,496 |
| Long-term borrowing by banks | 882 | 604 | 414 | 201 | 77 |
| Other items (net) | 1,617 | 2,375 | 2,659 | 3,188 | 2,923 |

(In millions of SDRs)

Balance of payments

| | | | | | |
|-------------------------------------|------|------|------|------|------|
| Exports, f.o.b. | 95 | 114 | 141 | 229 | 217 |
| Imports, f.o.b. | -213 | -221 | -247 | -328 | -403 |
| Of which: petroleum products | (19) | (33) | (25) | (54) | (61) |
| capital goods | (32) | (2) | (33) | (45) | (90) |
| Services (net) <u>1/</u> | -29 | -37 | -78 | -91 | -99 |
| Private unrequited transfers | -23 | -24 | -25 | -18 | -21 |
| Current account balance | -171 | -172 | -199 | -207 | -306 |
| Official unrequited transfers | 109 | 91 | 80 | 85 | 53 |
| Nonmonetary capital (net) <u>2/</u> | 56 | 100 | 89 | 150 | 215 |
| Overall balance | -6 | 19 | -30 | 29 | -38 |
| Arrears (decrease -) | 9 | -8 | 24 | -18 | ... |
| Net foreign assets (increase -) | -3 | -11 | 6 | -10 | ... |

Outstanding external debt
(end of period)

| | | | | |
|-----|-----|-----|-----|-------|
| 505 | 520 | 637 | 785 | 1,072 |
|-----|-----|-----|-----|-------|

Gross official foreign reserves
(end of period)

| | | | | |
|----|----|-----|-----|-----|
| 67 | 96 | 118 | 152 | ... |
|----|----|-----|-----|-----|

(Annual per cent change)

| | | | | | |
|-----------------------|-------|-------|------|------|------|
| <u>Terms of trade</u> | -14.9 | -12.2 | -2.9 | 7.9 | -1.7 |
| Export price | -11.8 | 0.1 | 9.9 | 13.3 | 2.1 |
| Import price | 3.7 | 13.2 | 14.0 | 5.0 | 3.9 |

1/ Includes fishing royalties.

2/ Including allocation of SDRs.

Mauritania - Relations with the Fund 1/

| | |
|---|--|
| Date of membership: | September 10, 1963 |
| Quota: | SDR 25.5 million |
| Exchange system: | Since January 22, 1974 the exchange rate of the ouguiya has been determined on the basis of a basket of currencies. |
| Intervention currency and the rate: | US\$; US\$1 = UM 53.720 |
| SDR/Local currency equivalent: | SDR 1 = UM 57.071 |
| Fund holdings of currency: | 271.98 per cent of quota (of which 41.18 per cent under the compensatory financing facility, 2.25 under the oil facility and 62.59 per cent under the supplementary financing facility). |
| SDR position: | Current holdings are SDR 57,879 or 0.6 per cent of net cumulative allocation of SDR 9.72 million. |
| Gold distributions: | 11,124.698 ounces |
| Direct distribution of profits from gold sales: | US\$2.09 million |
| Trust Fund loan disbursements: | SDR 12.70 million |
| Subsidies on costs of SFF resources | SDR 1,334,785 |

Last Article IV consultation discussions

The last Article IV consultation discussions with Mauritania were held in Nouakchott during the period November 13-28, 1979, followed by additional discussions at Fund headquarters during the period February 12-15, 1980. The staff report (SM/80/73) was discussed by the Executive Board on April 18, 1980, and the following decision was taken:

1/ As of October 31, 1982.

Mauritania - Relations with the Fund (concluded)

1. The Fund takes this decision relating to Mauritania's exchange measures subject to Article VIII, Sections 2 and 3, and in concluding the 1979 Article XIV consultation with Mauritania, in the light of the 1979 Article IV consultation with Mauritania conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. The Fund notes that, despite pressures on the balance of payments, Mauritania's exchange system has remained relatively free of restrictions. In view of the circumstances of Mauritania, the Fund approves the restrictions on the sale of foreign exchange for travel and salary remittances as described in SM/80/91 until June 30, 1981 or the next Article IV consultation, whichever comes first. The Fund would encourage Mauritania to eliminate its external arrears as soon as possible.

[The approval of Mauritania's exchange restrictions under the above decision was extended until March 31, 1982, then until August 31, 1982, finally until January 31, 1983 or the completion of the next Article IV consultation, whichever is the earlier (Decision No. 7187/82/114 adopted on August 20, 1982).]

Mauritania - Relations with the World Bank Group 1/

A. Bank loans and IDA credits

| | | | <u>Amount less cancellation 2/</u> | | |
|---|-----------------|--------------------------------|------------------------------------|------------|--------------------|
| | | | <u>(US\$ million)</u> | | |
| <u>Fiscal</u> <u>year</u> | <u>Borrower</u> | <u>Purpose</u> | <u>Bank</u> | <u>IDA</u> | <u>Undisbursed</u> |
| One loan and nine credits fully disbursed | | | 66.0 | 35.5 | -- |
| 1976 | Mauritania | Technical Assistance | | 2.7 | |
| 1979 | Mauritania | Urban and Rural Development | | 8.0 | 2.8 |
| 1980 | SNIM | Guelbs Iron Ore | 60.0 | | 32.7 |
| 1981 | Mauritania | Gorgol Irrigation | | 15.0 | 11.2 |
| 1982 | Mauritania | Petroleum Exploration | | 3.0 | 2.2 |
| 1982 3/ | Mauritania | Second Education | | 5.7 | 5.7 |
| 1982 3/ | Mauritania | Fourth Highway | | 4.0 | 4.0 |
| 1983 3/ | Mauritania | Technical Assistance | | 4.6 | 4.6 |
| TOTAL | | | 126.0 | 78.5 | 63.2 |
| of which has been repaid | | | 66.0 | 1.6 | |
| Total now outstanding | | | 60.0 | 76.9 | |
| Total undisbursed | | | 32.7 | 30.5 | 63.2 |

B. Loans expected to be approved in 1983, 3rd-4th quarters

| | | | |
|------------|--------------------------------|------------|------------|
| Mauritania | SONADER - Technical Assistance | 8.0 | 8.0 |
| Mauritania | Small-scale Irrigation | <u>8.0</u> | <u>8.0</u> |
| Total | | 16.0 | 16.0 |

C. Technical assistance

Since 1977 the Bank has been providing technical assistance to the Ministry of Planning in the areas of macroeconomic analysis, project evaluation, and sectoral policies and in the preparation of the Five-Year Development Plan (1981-85). The Bank has also been providing technical assistance to Mauritania's Rural Development Agency (SONADER). Currently, the Bank is assisting the Mauritanian authorities with an in-depth review of the operations of major public enterprises and in the formulation of a rehabilitation plan for the public enterprise sector.

1/ As of October 31, 1982.

2/ Prior to exchange adjustments.

3/ Not yet effective.