

EBS/62/49

CONFIDENTIAL

April 27, 1962

To: Members of the Executive Board

From: The Secretary

Subject: United Arab Republic - Request for Stand-By Arrangement

Attached for consideration by the Executive Directors is a request from the United Arab Republic for a stand-by arrangement. A paper by the staff will be circulated early next week. This matter is expected to be scheduled for consideration by the Executive Board not later than May 7.

Att: (1)

United Arab Republic
Ministry of Economy

Office of the Minister

April 26, 1962

Confidential

Dear Mr. Jacobsson:

The United Arab Republic has been faced for some time with a difficult balance of payments problem which has been due to a combination of circumstances. The Government is pursuing policies designed to increase production and employment and raise the standard of living of the people, and these efforts have resulted in pressure on our resources. The U.A.R. has also faced in the last several years heavy contractual payments of an exceptional character. In addition, the situation has been aggravated recently as a consequence of exceptionally poor agricultural crops, particularly cotton. As a result of our difficult balance of payments situation, foreign exchange reserves have fallen to a low level. The balance of payments will also be affected by the plans of the U.A.R. to settle with foreigners remaining claims.

In these circumstances, the Government is undertaking a comprehensive financial program designed to assure conditions of internal and external balance in the economy. To assist in meeting the balance of payments deficit while the program is being implemented, the U.A.R. requests a stand-by arrangement in the amount of \$42.5 million. The U.A.R. authorities will consult the Managing Director as to the currencies to be purchased from the Fund before making any purchase under the requested stand-by arrangement. Negotiations have also been initiated with a number of countries with the view of obtaining additional financial support for this financial program. The program, which has the approval of the Cabinet, includes the measures described in the following paragraphs:

1. For some months now the Government has been engaged in a major effort to reduce its dependence on financing by the banking system. These efforts are meeting with considerable success and will be continued. The 1962/63 budget beginning July 1 is now in preparation and in its final form will be fully consistent with the limitations placed on the Government's dependence on the banking system described in the following paragraph.
2. The net claims of the banking system on the Government (government obligations held by the banking system minus government deposits with the banking system minus counterpart deposits related to imports under U.S. Public Law 480) will not rise above the level of March 31, 1961 by more than LE 10 million at any time prior to September 30, 1962; nor by more than LE 20 million at any time prior to March 31, 1963; nor by more than LE 25 million at any time prior to June 30, 1963.
3. Cotton financing follows a seasonal pattern, rising from September until November-December and declining thereafter. The current requirements for cotton financing are less than a year ago in view of the lower level of production, and, moreover, the level of such financing should decline by

next June below the level existing on June 30, 1961, as a decline in cotton stocks is expected to take place. A ceiling has been imposed on cotton financing as follows: The level of cotton financing will decline at least to LE 27 million by June 30, 1962 and to LE 20 million by August 31, 1962. For the remainder of 1962, the ceiling on such credit will be LE 85 million. During the first half of 1963 cotton financing will decline, falling at least to LE 55 million by March 31, 1963, and to LE 27 million by June 30, 1963. The ceilings for cotton financing after September 1, 1962 relate to the 1962/63 cotton season and are made on the assumption of a normal cotton crop. These ceilings may be adjusted after prior agreement with the Managing Director of the Fund, in the light of the actual size of the cotton crop.

4. A moderate increase in other bank accommodation for the private sector and public organizations not covered by the budget (referred to hereafter as the "nongovernment sector") is to be permitted. The total claims of the banking system on the nongovernment sector (excluding cotton financing) will not rise above the level of March 31, 1961 by more than LE 5 million at any time prior to September 30, 1962, nor by more than LE 10 million at any time prior to March 31, 1963, nor by more than LE 12.5 million at any time prior to June 30, 1963.

5. The following measures relating to credit control are being taken: (a) The Central Bank will impose forthwith two separate ceilings on each commercial or specialized bank, one for cotton financing and one for other financing of the nongovernment sector. Whenever any bank is in excess of either of its ceilings, such bank will not be granted any accommodation (including renewal of outstanding credits) by the Central Bank and such other penalties will be imposed as necessary to assure remedial action by the Bank concerned. (b) The Central Bank not later than May 15, 1962 will raise its discount rate from 3 to 5 per cent and adjust its interest rate schedule accordingly. (c) The Central Bank not later than May 15, 1962, will increase the reserve requirements for commercial banks from $12\frac{1}{2}$ per cent to $17\frac{1}{2}$ per cent. The banks, however, will be permitted a reasonable time, not to exceed sixty days, to comply fully with the new requirements. (d) The Central Bank will take steps to assure that the banks as a group maintain at least the same ratio of holdings of government obligations to their total assets as existing on December 31, 1961, and that banks henceforth purchase government obligations only from the Central Bank or from another bank.

6. Price controls will be dismantled as rapidly as possible with the view to their eventual elimination.

7. The objectives of policies in the external sector will be to establish a new par value at a realistic level, to eliminate multiple currency practices and to abolish restrictions on current payments and transfers. With regard to the exchange system, the practice of premiums will be abandoned and a new realistic rate of US\$2.30 per Egyptian pound will be announced for all exchange transactions not later than May 15, 1962, and in any event prior to any request for a drawing under the stand-by arrangement with the Fund. Since in the short run, the application of this rate to all exports will in some cases (cotton, onions, rice, petroleum,

and groundnuts) give rise to windfall profits, there would in these cases be temporary use of export taxes. From the outset, however, each export commodity will receive greater incentive than in the recent past. Moreover, such taxes will be gradually reduced in order to provide continuing stimulus for increased production of export commodities. On the import side, there will be limited use of subsidies to be provided for in the budget in order to ease the price adjustment. Such subsidies will be applied only to the following: wheat, flour, kerosene, edible oil, sugar, and other similar essential foodstuffs. The policy of the Government will be to reduce the amount of these subsidies gradually.

8. With regard to import policies, the following measures will be taken: (a) An open general license will be established not later than July 1, 1962 for a substantial proportion of permitted imports. Such goods which are not on the open general license will be subject to nondiscriminatory global quotas. The level of restrictions will be reduced forthwith to the extent feasible and further reduced as rapidly as circumstances permit. (b) With regard to nonessential goods, there will be increased use of import duties and decreased use of quotas and outright prohibitions. (c) State owned or controlled importing agencies will be instructed forthwith to operate, in making import decisions, on a commercial basis and will be given freedom to choose sources of supply.

9. The U.A.R. will not, without prior Fund approval, introduce any multiple currency practice, introduce any restrictions on current payments and transfers, or intensify any existing ones.

10. The U.A.R. will terminate its bilateral payments agreements with Fund members at the earliest possible date and not later than present termination dates. This policy will apply not only to agreements having clearing accounts in inconvertible currencies but also to those in convertible currencies providing for swing limits. With regard to bilateral payments agreements which it may not be possible to terminate, the U.A.R. will not accord any preferential treatment to its bilateral partners.

11. If at any time during the period of the stand-by arrangement (i) the net claims of the banking system on the Government have risen by more than the limits specified in paragraph 2 above; or (ii) the level of cotton financing by the banking system has not been within the limits specified in paragraph 3 above; or (iii) the total claims of the banking system on the nongovernment sector (excluding cotton financing) have risen by more than the limits specified in paragraph 4 above; or (iv) the U.A.R. introduces any restrictions on current payments and transfers, intensifies any existing ones, or introduces any multiple currency practice, the U.A.R. will consult with the Fund prior to any further drawing under the stand-by arrangement and agree with it the terms on which such further drawings will be made.

/s/
Dr. A.M. Kaissouni
Minister of Economy