

DOCUMENT OF INTERNATIONAL MONETARY FUND  
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**FOR  
AGENDA**

EBS/76/530

CONFIDENTIAL

December 22, 1976

To: Members of the Executive Board

From: The Secretary

Subject: The People's Republic of the Congo - Request for Stand-By Arrangement

Attached for consideration by the Executive Directors is a request from the People's Republic of the Congo for a stand-by arrangement in the first credit tranche equivalent to SDR 4.7 million, together with the staff's analysis and recommendation.

This subject, a request for a Trust Fund loan (TR/76/24, 12/22/76), and Congo's request for a purchase under paragraphs 2, 3, and 4 of the Decision on Compensatory Financing of Export Fluctuations (paper to be issued as EBS/76/531), have been tentatively scheduled for discussion on Wednesday, December 29, 1976.

Att: (1)



INTERNATIONAL MONETARY FUND

The People's Republic of the Congo - Request for Stand-by Arrangement

Prepared by the African Department<sup>1/</sup>

(In consultation with the Exchange and Trade Relations, Fiscal,  
Treasurer's, and Legal Departments)

Approved by J.B. Zulu

December 21, 1976

In the attached letter, dated November 19, 1976, the Government of the People's Republic of the Congo requests a stand-by arrangement in the enlarged first credit tranche in an amount equivalent to SDR 4.7 million for a period of one year. This amount, which represents 36.25 per cent of the Congo's quota, will be augmented by any repurchases in respect of purchases under the requested stand-by arrangement unless the Congo informs the Fund to the contrary when a repurchase is made. A waiver under Article V, Section 4 of the Fund Agreement is required. The Congo will consult with the Managing Director concerning the currencies to be purchased from the Fund prior to making any request to purchase under the stand-by arrangement.

The People's Republic of the Congo became a member of the Fund in July 1963 and has at present a quota of SDR 13 million, of which the equivalent of SDR 1.6 million has been paid in gold. No par value for the Congo's currency, the CFA franc, has been established with the Fund, and the original currency subscription has not yet been paid. The relationship between the CFA franc and the French franc, which is the intervention currency, is fixed at CFAF 1 = F 0.02, and the rates for other currencies in terms of CFA francs parallel the movements of the French franc against these currencies. The representative rate for the CFA franc under Rule 0-3 is obtained on the basis of the fixed relationship between the CFA franc and the French franc and the representative rate of the French franc (EBD No. 4884/75-1815, November 25, 1975).

So far the Congo has made no use of Fund resources, but it incurred a repurchase commitment equivalent to SDR 0.46 million in respect of excess currency paid in connection with the 1970 quota increase. The last installment in respect of this repurchase was discharged in December 1975.

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<sup>1/</sup> A staff mission consisting of Messrs. Bhatia (AFR), Cronquist (AFR), Stahl (ETR), Griffith (FAD), and Mrs. Klotz (secretary, AFR) visited Brazzaville during the period November 10-19, 1976 to discuss the requested use of Fund resources.

As of November 30, 1976 the Fund's holdings of CFA francs on behalf of the Congo totaled the equivalent of SDR 4.1 million, arising from currency subscriptions in connection with quota increases. The Congo has expressed its intention to request a purchase in an amount equivalent to SDR 6.5 million under paragraphs 2, 3, and 4 of the 1975 Decision on compensatory financing of export fluctuations (EBS/76/531). It has also requested a loan from the Trust Fund (TR/76/24).

The Congo has received SDR allocations totaling SDR 4.4 million. It has used SDRs to obtain currency and to effect repurchases. As of November 30, 1976 its SDR holdings amounted to SDR 2.1 million, or 46 per cent of its net cumulative allocation.

The latest Article XIV consultation discussions with the Congo were held in Brazzaville during the period November 24-December 6, 1975. The staff report (SM/76/52, and Supplement 1) was discussed by the Executive Board on August 4, 1976.

## I. Recent Developments and Policies

### 1. Background

During the decade up to 1975 the Congolese economy registered a modest growth in real GDP, averaging about 4 per cent per annum. In the first half of that period, growth occurred mainly in forestry, manufacturing, and commerce, while in the period after 1970 growth was concentrated in the mining sector, where potash production reached its maximum level in 1971-72 and crude oil output rose substantially with the entry into production of offshore oil fields in 1972. Throughout this period little progress was made in agriculture, and after 1970 the activity in the forestry sector also stagnated and manufacturing output showed only marginal increases.

In contrast to the moderate real growth, financial performance has been unsatisfactory through most of this period. Government budgets have recorded large annual deficits (averaging some 10 per cent of total expenditure in the decade ended 1974) resulting in substantial accumulation of government arrears, domestic bank credit has expanded at an average annual rate of 15 per cent, the balance of payments (measured by changes in net foreign assets of the banking system) has registered overall deficits in five of the ten years, and the Congo's external debt has risen rapidly, with debt service currently accounting for 24 per cent of exports of goods and services. Despite the large increase in oil production in 1973 and the increase in world oil prices in 1974, the financial situation worsened. Operating under optimistic assumptions regarding future oil production and government revenues, the authorities allowed a substantial increase in wages and salaries and in other current expenditures, and embarked upon an ambitious development program. Thus, in 1974

current expenditures rose by nearly 75 per cent, and capital expenditures rose by 60 per cent, which more than offset the 75 per cent increase in total revenues and resulted in an overall Treasury deficit equivalent to 12 per cent of total expenditures. Although the balance of payments improved from an overall deficit of CFAF 0.1 billion in 1973 to a surplus of CFAF 4.2 billion in 1974, the improvement was small in comparison with the increase of CFAF 35.5 billion in export receipts.

The full extent of the deterioration in the financial situation surfaced in 1975, when, contrary to earlier expectations, oil production not only failed to increase but actually declined because of technical difficulties with existing oil wells and delays in the opening of a second offshore oil deposit. As the expansion in government expenditures continued and the anticipated increase in revenues did not materialize, the Treasury, as well as the overall budgetary (accrual basis), deficit nearly tripled to 24 per cent of total outlay in 1975 (Tables 1 and 2). The deficit was mainly financed by borrowing from the Central Bank and by the use of deposits, but there was also a net increase in payments arrears (mostly to domestic suppliers) to CFAF 9.8 billion at the end of 1975.<sup>1/</sup> Simultaneously, private sector demand also expanded, as the guaranteed minimum wage in the private sector was adjusted upward by 70 per cent and bank credit to the private sector rose by 28 per cent. As a result, consumer prices rose by 17 per cent in 1975 (while import prices in terms of CFA francs are estimated to have increased at a much lower rate). The volume of imports rose by over 15 per cent. With the decline in oil output, the volume of exports fell, and, since the terms of trade also worsened, the trade account reverted to a deficit which, together with an increased deficit on services account but an improvement in net transfers, resulted in a doubling of the deficit on current account. Despite a larger inflow of capital (mainly for oil exploration), the overall balance of payments reverted from a surplus in 1974 to a deficit of CFAF 4.0 billion, or SDR 15.4 million, in 1975 (Table 3).

The Congo's external debt increased rapidly, with outstanding total disbursed debt rising from the equivalent of CFAF 44 billion at the end of 1973 to CFAF 77 billion at the end of 1975. Service payments totaled CFAF 3.5 billion in 1974 and CFAF 5.6 billion in 1975. As a result of the budgetary difficulties, the Congo fell behind in servicing (amortization and interest) its public external debt, and at the end of 1975 such arrears totaled CFAF 3.3 billion. The external debt profile has also become increasingly unfavorable because of a larger use of suppliers' credits by the Government in the recent past, with the average interest rate increasing from 1.1 per cent in 1973 (when much of the debt was noninterest-bearing) to 6.5 per cent in 1975 and the maturity period shortening from an average of 27 years to 9.5 years. Although suppliers'

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<sup>1/</sup> This refers to the arrears at the Treasury level. In addition, the Ministry of Finance also owed a substantial amount in unprocessed bills.

Table 1. The People's Republic of the Congo: Operations of the Treasury, 1974-76  
(In millions of CFA francs)

|                                      | 1974          | 1975           | 1976                     |                          |
|--------------------------------------|---------------|----------------|--------------------------|--------------------------|
|                                      |               |                | Actual<br>Jan.-<br>Sept. | Estimate<br>Full<br>year |
| <u>Total revenue</u>                 | <u>38,350</u> | <u>50,267</u>  | <u>33,014</u>            | <u>44,000</u>            |
| Nonpetroleum revenue                 | 23,321        | 38,050         | 25,014                   | 32,400                   |
| Petroleum revenue                    | 15,029        | 12,217         | 8,000                    | 11,600                   |
| <u>Current expenditure</u>           | <u>38,903</u> | <u>49,334</u>  | <u>37,900</u>            | <u>48,750</u>            |
| Current deficit                      | -553          | -1,711         | -4,886                   | -4,750                   |
| <u>Capital expenditure</u>           | <u>5,401</u>  | <u>16,762</u>  | <u>3,876</u>             | <u>4,000</u>             |
| <u>Total budgetary expenditure</u>   | <u>44,304</u> | <u>66,096</u>  | <u>41,776</u>            | <u>52,750</u>            |
| <u>Budgetary deficit</u>             | <u>-5,954</u> | <u>-15,829</u> | <u>-8,762</u>            | <u>-8,750</u>            |
| Special accounts (net)               | 733           | 807            | 1,020                    | 900                      |
| Autonomous budgets (net)             | -211          | -681           | -518                     | -700                     |
| <u>Treasury deficit</u>              | <u>-5,432</u> | <u>-15,703</u> | <u>-8,260</u>            | <u>-8,550</u>            |
| <u>Domestic financing (net)</u>      | <u>2,845</u>  | <u>13,549</u>  | <u>8,260</u>             | <u>...</u>               |
| Equipment bonds                      | 1,157         | 399            | 508                      | 650                      |
| Customs duty bills                   | -19           | -18            | 11                       | ...                      |
| Deposits with Treasury               | 3,637         | 5,407          | 4,019                    | ...                      |
| Payments arrears                     | -465          | 3,459          | 1,078                    | ...                      |
| Central Bank                         | 183           | 3,953          | 1,057                    | ...                      |
| Change in cash balances (increase -) | -1,676        | 349            | 1,587                    | ...                      |
| Other                                | 28            | --             | --                       | --                       |
| <u>Foreign financing (net)</u>       | <u>2,587</u>  | <u>2,028</u>   | <u>--</u>                | <u>....</u>              |
| Drawings                             | 2,644         | 4,970          | --                       | ...                      |
| Amortization                         | -57           | -2,942         | --                       | ...                      |

Table 2. The People's Republic of the Congo: Central Government  
Budgetary Operations, 1974-77

(In millions of CFA francs)

|                                       | 1974<br>Actual | 1975<br>Actual | 1976<br>Original<br>budget | 1976<br>Estimate | 1977 <sup>1/</sup><br>Projections |
|---------------------------------------|----------------|----------------|----------------------------|------------------|-----------------------------------|
| <u>Revenue</u>                        | <u>38,143</u>  | <u>43,467</u>  | <u>46,036</u>              | <u>42,350</u>    | <u>45,000</u>                     |
| Nonpetroleum revenue                  | 20,432         | 30,662         | 33,576                     | 32,650           | 35,000                            |
| Tax revenue                           | (19,515)       | (27,045)       | (32,498)                   | (30,550)         | (32,800)                          |
| Nontax revenue                        | (917)          | (3,617)        | (1,078)                    | (2,100)          | (2,200)                           |
| Petroleum revenue                     | 17,711         | 12,805         | 12,460                     | 9,700            | 10,000                            |
| Income tax                            | (11,175)       | (6,546)        | (6,000)                    | (6,100)          | (6,500)                           |
| Royalties                             | (6,536)        | (6,259)        | (6,460)                    | (3,600)          | (3,500)                           |
| <u>Current expenditure</u>            | <u>35,961</u>  | <u>41,775</u>  | <u>49,440</u>              | <u>47,050</u>    | <u>47,000</u>                     |
| Debt service <sup>2/</sup>            | 4,182          | 3,809          | 4,569                      | 4,550            | 4,000                             |
| Wages and salaries                    | 14,110         | 20,106         | 23,300                     | 22,900           |                                   |
| Materials                             | 4,379          | 5,032          | 6,125                      | 4,600            | 43,000                            |
| Unallocated                           | 4,005          | 4,528          | 4,020                      | 4,000            |                                   |
| Transfers                             | 9,295          | 8,300          | 11,426                     | 11,000           |                                   |
| <u>Current surplus or deficit (-)</u> | <u>2,172</u>   | <u>1,692</u>   | <u>-3,404</u>              | <u>-4,700</u>    | <u>-2,000</u>                     |
| <u>Transfers to investment budget</u> | <u>7,119</u>   | <u>15,500</u>  | <u>3,000</u>               | <u>3,000</u>     | <u>1,000</u>                      |
| <u>Total expenditure</u>              | <u>43,090</u>  | <u>57,275</u>  | <u>52,440</u>              | <u>50,050</u>    | <u>48,000</u>                     |
| <u>Overall deficit</u>                | <u>-4,947</u>  | <u>-13,808</u> | <u>-6,404</u>              | <u>-7,700</u>    | <u>-3,000</u>                     |

Sources: Ministry of Finance; and staff estimates.

1/ Projections based on measures outlined in the attached letter of intent.

2/ Includes amortization.

Table 3. The People's Republic of the Congo:  
Balance of Payments, 1974-77

(In millions of CFA francs)

|   | 1974    | 1975    | 1976 <u>1/</u> | 1977 <u>2/</u>  |
|---|---------|---------|----------------|-----------------|
| Exports, f.o.b.   | 63,511  | 49,470  | 50,469         | 53,400          |
| Petroleum   | 38,500  | 28,300  | 31,000         | 30,520          |
| Other   | 25,011  | 21,170  | 19,469         | 22,880          |
| Imports, c.i.f.   | 59,189  | 69,050  | 78,560         | 81,360          |
| Trade balance   | 4,322   | -19,580 | -28,091        | -27,960         |
| Services (net)  | -19,629 | -32,303 | -39,644        | -40,000         |
| Balance on goods and services                             | -15,307 | -51,883 | -67,735        | -67,960         |
| Unrequited transfers (net)                                | -7,768  | 2,086   | 4,180          | 5,400           |
| Government  | 4,512   | 7,367   | 8,800          | 10,000          |
| Private   | -12,280 | -5,281  | -4,620         | -4,600          |
| Nonmonetary capital, including errors and omissions (net) | 27,324  | 45,809  | 60,045         | 60,560          |
| Government  | 8,992   | 9,198   | ...            | ...             |
| Private   | 13,740  | 32,217  | ...            | ...             |
| Errors and omissions                                      | 4,592   | 4,394   | ...            | ...             |
| Subtotal  | 4,249   | -3,988  | -3,510         | -2,000          |
| Change in net foreign assets (increase -)                 | -4,249  | 3,988   | 3,510          | 2,000           |
| Central Bank  | -3,071  | 2,175   | 3,440          | -1,248          |
| Commercial banks  | -1,178  | 1,813   | 70             | --              |
| IMF position  | --      | --      | --             | 3,248 <u>3/</u> |

Source: Data provided by the Central Bank.

1/ Staff estimates.

2/ Staff projections based on measures outlined in the attached letter of intent.

3/ Includes the drawing under the compensatory financing decision.

credits constituted only about one third of the total disbursed debt outstanding at the end of 1975, the scheduled service payments for these credits in the three years 1976-78 exceed the service payments on other loans.

## 2. Developments in 1976 and prospects

In 1976, as technical difficulties were gradually resolved, the decline in oil production was halted and output is estimated to rise by about 6 per cent. Production of potash, on the other hand, declined. In the agricultural sector there was a substantial increase (65 per cent) in coffee production but a decline in the output of sugar, cocoa, and rice. Growth in the forestry sector was also stymied by transportation difficulties and other problems attendant upon the nationalization of forestry export trade in 1975. In nominal terms, according to staff estimates, GDP may increase by about 13 per cent.

The financial situation has continued to be serious. Although in the 1976 budget some taxes were increased and expenditure restraints were announced (for details, see SM/76/52, Supplement 1), it is now estimated that the year will end with an increased current, as well as an overall, budget deficit (Table 2). Compared to the budgetary outcome for 1975, however, the overall budget deficit is expected to be halved to CFAF 7.7 billion as a result of an 80 per cent reduction in capital expenditure. Total revenue is estimated at CFAF 42.3 billion, CFAF 4.0 billion less than the budget estimate, while expenditure is projected at CFAF 50.0 billion, or CFAF 2.0 billion below the budget estimate. Most of the revenue shortfall is due to lower petroleum royalties (CFAF 3.6 billion instead of the budgeted receipts of CFAF 6.9 billion), although import duty receipts will also be short by about CFAF 1.0 billion. On the expenditure side, most of the saving is to be in purchases of materials, outlays on which have increased substantially since 1972. Transfers to the capital budget are estimated at CFAF 3.0 billion. Much of this amount is required to finance operating deficits of state enterprises and will not be available for investment. The Treasury deficit for 1976 is estimated at CFAF 8.5 billion (Table 1), almost half of which is to be financed by use of deposits with the Treasury, and the balance by the use of cash balances, borrowing from the banking system, and an increase in payments arrears. At the end of September 1976 payments arrears amounted to almost CFAF 11.0 billion. In addition, there were unprocessed bills totaling CFAF 6.8 billion.

The strong expansion in credit to the private sector was maintained during the first eight months of 1976, as the monetary authorities continued to accommodate requests for rediscounts (Tables 4 and 5). Credit to the private sector rose by 18 per cent, and the use of central bank rediscount facilities by the banks, which had accounted for about 19 per cent of short-term credit at end-1975, rose to 22 per cent at the end of August 1976. However, the authorities expect that a part of the credit

Table 4. The People's Republic of the Congo: Monetary Survey, 1974-77<sup>1/</sup>

(In billions of CFA francs; end of period)

|  | 1974         |              |              | 1975         |              |              | 1976         |              |                    | 1977 <sup>2/</sup> |
|--|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------------|--------------------|
|  | Dec.         | March        | June         | Sept.        | Dec.         | March        | June         | Aug.         | Dec. <sup>3/</sup> | Dec.               |
| Foreign assets (net)                         | 6.15         | 4.83         | 1.81         | 2.77         | 2.16         | 3.04         | -0.40        | 0.16         | -1.35              | -0.10              |
| Domestic credit                              | <u>23.36</u> | <u>27.16</u> | <u>29.90</u> | <u>31.32</u> | <u>34.05</u> | <u>33.79</u> | <u>37.94</u> | <u>39.13</u> | <u>39.20</u>       | <u>41.00</u>       |
| Government (net)                             | 2.21         | 4.78         | 5.04         | 6.40         | 6.94         | 6.22         | 7.66         | 7.19         | 7.20               | 7.20               |
| Private sector                               | 21.15        | 22.38        | 24.86        | 24.92        | 27.11        | 27.57        | 30.28        | 31.94        | 32.00              | 33.80              |
| Money  | 23.52        | 23.96        | 24.03        | 25.70        | 26.07        | 26.39        | 27.56        | 28.06        | 27.00              | 26.00              |
| Quasi-money                                  | 1.74         | 1.88         | 1.91         | 2.00         | 2.08         | 2.38         | 2.45         | 2.45         | 2.35               | 2.00               |
| Medium- and long-term<br>foreign liabilities | 1.48         | 1.86         | 1.94         | 2.07         | 2.71         | 2.99         | 3.42         | 3.51         | 3.75               | 4.90               |
| IMF  | --           | --           | --           | --           | --           | --           | --           | --           | --                 | 3.25               |
| Other items (net)                            | 2.77         | 4.29         | 3.83         | 4.32         | 5.35         | 5.07         | 4.11         | 5.27         | 4.75               | 4.75               |

Source: Data provided by the Banque des Etats de l'Afrique Centrale.

<sup>1/</sup> Encompassing the Central Bank, deposit money banks, deposits with the Postal Checking System, and short-term credit (customs duty bills) extended by the Treasury.

<sup>2/</sup> Projections based on measures outlined in the attached letter of intent.

<sup>3/</sup> Staff estimates.

Table 5. The People's Republic of the Congo: Summary Accounts of the Central Bank, 1974-77

(In billions of CFA francs; end of period)

|  | 1974        |             |              | 1975         |              |              | 1976         |              |              | 1977 <sup>1/</sup>  |
|--|-------------|-------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|---------------------|
|  | Dec.        | March       | June         | Sept.        | Dec.         | March        | June         | Aug.         | Dec.         | Dec. <sup>2/</sup>  |
| Foreign assets (net)                   | 5.47        | 4.42        | 3.32         | 3.39         | 3.29         | 4.56         | 0.56         | 1.36         | -0.15        | 1.10                |
| Domestic credit                        | <u>7.95</u> | <u>9.21</u> | <u>11.08</u> | <u>11.59</u> | <u>13.02</u> | <u>11.71</u> | <u>15.09</u> | <u>15.51</u> | <u>15.70</u> | <u>17.95</u>        |
| Government (net)                       | 2.37        | 4.39        | 4.60         | 6.24         | 6.42         | 6.14         | 7.46         | 7.13         | 7.20         | 7.20                |
| Banks and other financial institutions | 5.58        | 4.82        | 6.48         | 5.35         | 6.60         | 5.57         | 7.63         | 8.38         | 8.50         | 10.75 <sup>2/</sup> |
| Liabilities to banks                   | 0.48        | 0.60        | 0.63         | 0.69         | 0.96         | 0.80         | 0.59         | 1.45         | 0.85         | 0.90                |
| Liabilities to private sector          | 11.61       | 11.62       | 12.50        | 12.86        | 14.04        | 14.04        | 13.84        | 14.14        | 13.80        | 14.00               |
| IMF                                    | --          | --          | --           | --           | --           | --           | --           | --           | --           | 3.25                |
| Other items (net)                      | 1.33        | 1.41        | 1.27         | 1.43         | 1.31         | 1.43         | 1.22         | 1.28         | 0.90         | 0.90                |

Source: Data provided by the Banque des Etats de l'Afrique Centrale.

<sup>1/</sup> Projections based on measures outlined in the attached letter of intent.

<sup>2/</sup> Staff estimates.

<sup>2/</sup> To provide some flexibility during the year, the limit on rediscounts is fixed at CFAF 12.0 billion in the program.

extended to the Agence Transcongolaise des Communications during the first half of 1976 will be repaid before the end of the year and that, consequently, credit to the private sector will rise by about 18 per cent for the full year.

The balance of payments is estimated to show a deficit of CFAF 3.5 billion in 1976. Although the overall deficit is somewhat lower than in 1975, this improvement was brought about by substantial increases in the net inflow of unrequited transfers and capital; the trade deficit widened, and there was a larger deficit on the services account. The larger trade deficit reflects a 14 per cent increase in imports in the face of a virtual stagnation of total export receipts, which in 1975 were already 22 per cent lower than in 1974 as a result of the decline in petroleum exports. While export receipts from oil increased, other export receipts continued to decline. Exports of forestry products, which had suffered from the recession in export markets in 1975, declined further. Exports of potash also declined, on account of less favorable prices and the continued depletion of the existing deposits. The increase in the deficit on the services account by 23 per cent to CFAF 40 billion reflects mainly the upsurge in the category of "other services," especially exploration expenditures of the petroleum and mining industries (rising by 28 per cent to CFAF 32 billion). In addition debt service payments were also higher; scheduled payments for the year are CFAF 14.4 billion or 24 per cent of exports of goods and services. Gross official reserves fell by SDR 8.4 million during the first 9 months of 1976 and amounted to SDR 4.2 million at the end of September 1976.

Thus at the end of 1976 the Congo finds itself with continued domestic and external financial imbalances. In view of the likely increase, beginning in mid-1977, in oil production from another oil field, these imbalances could be contained for some time in the future. However, proven oil reserves are estimated to last for only about six years, and, unless corrective measures are adopted, the financial disequilibrium will re-emerge. It is in recognition of this eventuality that the Congolese authorities have decided to introduce measures with a view to preventing a further deterioration of the situation and to utilizing additional resources coming from the oil sector for diversifying the economy to withstand the foreseen depletion of the oil fields in the medium term.

## II. The Program for 1977

In the attached letter of intent the Congolese authorities set out the program and policies to be followed during 1977. The program aims at limiting the balance of payments deficit in 1977 to CFAF 2 billion (SDR 6.7 million). The program is based on an estimate of export receipts of CFAF 53.4 billion. Oil production, as well as exports, is projected at 1.8 million tons, while exports of forestry products are not expected to begin to recover from the low levels of 1975-76 until around the end of

the year. The program is conceived as a first corrective step and as providing an opportunity to formulate a program in the medium term to correct the financial imbalances and to develop the nonoil sector to ensure a satisfactory rate of growth despite the likely exhaustion of the present oil fields by 1982. In the meantime, the authorities hope to prevent a further deterioration in the financial situation in 1977 mainly through measures in the areas of the budget and credit.

The main emphasis is on a reduction of government current budget expenditures, which, as mentioned earlier, have expanded substantially in the past few years. Although the budget for 1977 has not yet been presented, the letter of intent states that current expenditures, excluding debt service, will be contained at CFAF 43.0 billion, corresponding to the level expected to be realized in 1976, while total expenditures (i.e., including debt service and transfers to the investment budget) in 1977 will be limited to CFAF 48.0 billion. Given the projected budgetary receipts of about CFAF 45.0 billion, this policy will result in a more than 50 per cent reduction in the current deficit (including debt service of CFAF 4 billion) to CFAF 2.0 billion, and a 60 per cent reduction in the overall deficit to about CFAF 3.0 billion, or the equivalent of 6 per cent of total expenditures (Table 2). The authorities indicated that the limit on current expenditures will be enforced by holding expenditures on wages and salaries at the 1976 level, except that an increase of CFAF 1.0-1.5 billion is assumed for the hiring of new personnel completing their training. Transfers to state enterprises will be frozen at their 1976 level pending the outcome of envisaged studies to improve their profitability. Appropriations for other current expenditures, particularly those for materials, will be examined critically with a view to reducing them, if need be, in order to keep total current outlays at the above level. Investment spending will be limited to those projects for which domestic nonbank or foreign financing becomes available.

The limit on budgetary outlays is based on the assumption that the Government's total take from oil production will be about CFAF 10 billion. However, this figure could be exceeded if the Government succeeds in enforcing a new decree of October 1976, raising royalty and income tax payments, which the petroleum companies are contesting as being incompatible with their original agreements with the Government. The projected budgetary deficit will be covered by the counterpart of the requested drawing under the compensatory financing decision (EBS/76/531) and by foreign assistance. A part of the former is also expected to be used to reduce existing arrears in government payments.

Credit policy will also be considerably more restrictive in 1977 than hitherto. The monetary authorities intend to limit total net domestic credit during 1977 so as not to exceed CFAF 41.0 billion at the end of the year, i.e., about 5 per cent over the August 1976 level. Present statutory limitations will leave net credit to the Treasury almost unchanged (though the use by the Government of the counterpart of the contemplated

compensatory drawing from the Fund would be tantamount to a corresponding increase in credit). Hence the overall limit on total credit expansion implies a deceleration in credit to the private sector from an estimated rate of 18 per cent in 1976 to about 6 per cent in 1977. To ensure that credit expansion will remain within the ceiling, the monetary authorities intend to limit total rediscounts, including rediscounts of the Treasury's customs duty bills and advances to banks, to CFAF 12.0 billion at the end of 1977,<sup>1/</sup> compared with CFAF 8.4 billion at the end of August 1976 and with an estimated CFAF 8.5 billion at the end of December 1976. Since the liquidity of commercial banks is already sufficiently strained, and is likely to continue to be so, they will depend increasingly on central bank rediscounts to finance their credit operations during the year. Accordingly, the Central Bank will be in a better position to control the expansion of credit. Given the projected balance of payments deficit, the ceiling on total domestic credit should result in a small decline in money of some 4 per cent in 1977 compared with a forecast increase of 3 per cent in GDP at current prices. The overall liquidity in the economy (defined as the sum of domestic and net foreign assets) will increase by about 8 per cent. On the basis of past relationship between imports and liquidity, the resulting level of liquidity would appear to be consistent with the level of imports (CFAF 81.4 billion, or about 4 per cent higher than in 1976) implied by the aforementioned balance of payments target.

The authorities also recognize the seriousness of their external debt problem. Following the recent rapid increase in external borrowing, the debt profile has been considerably shortened, and the scheduled service charges on outstanding disbursed debt will impose a heavy burden on the balance of payments and on the government budget in the next few years. Although the Congolese authorities have taken steps to renegotiate part of the existing debt, a more comprehensive review of the external debt policy is contemplated by them. To facilitate such a review, the Government will avoid as far as possible any further increase in the country's short- and medium-term external debt during 1977.

The Congo maintains a relatively liberal system of trade and payments. In the attached letter, the Congolese authorities state their intention not to introduce new restrictions on imports for balance of payments reasons or on payments and transfers for current international transactions.

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<sup>1/</sup> The projected use of rediscounts at the end of 1977 is CFAF 10.75 billion, but the higher figure of CFAF 12.0 billion is retained as a limit to provide some flexibility during the year.

### III. Staff Appraisal and Recommendations

Despite the seriousness of the Congo's economic and financial problems, the authorities, until now, had refrained from introducing adequate measures to correct the imbalances. However, with foreign exchange reserves virtually exhausted by the middle of 1976, a high level of external indebtedness, and increased government payments arrears, they have now decided to adopt corrective measures within the framework of a financial program for 1977 as a preliminary step toward the introduction of a more comprehensive medium-term program. By maintaining current budgetary expenditures in 1977 at the 1976 level and reducing total expenditures, and by a deceleration in credit expansion, the authorities intend to arrest the rapid financial deterioration and to contain the 1977 balance of payments deficit within reasonable limits. Arresting the growth in current expenditures is admittedly a difficult task, but, given the rapid increase in such expenditures during the past three years, such a measure should not have adverse effects on the efficiency of government operations. The modest aim of this program, however, does not encompass providing the basis for the resumption of sustained real growth in the economy and for an eventual equilibrium in the balance of payments. These will require new investments to diversify the economy. Fortunately, the Congo can expect significant additional resources from the petroleum sector during the next few years, which could be used for that purpose. The authorities are aware of the need to formulate medium-term economic and financial policies to supplement the 1977 program and have expressed interest in seeking Fund assistance under the extended facility. Furthermore, in view of the present high level of external indebtedness and the heavy debt service charges falling due in the next few years, the Congo will need additional external assistance in order to avoid a net outflow of capital during that period. In the meantime, the financial program for 1977 appears to be a reasonable effort and, by preventing further deterioration in the financial situation, should improve the balance of payments in the medium term.

In view of the foregoing, the following decision is submitted for consideration by the Executive Board:

The Government of the People's Republic of the Congo has requested a stand-by arrangement for a period of one year in an amount equivalent to SDR 4.7 million. The Fund approves the stand-by arrangement attached to EBS/76/530 and grants any necessary waiver of the conditions of Article V, Section 3(a)(iii) of the Articles of Agreement.

Stand-By Arrangement - The People's Republic of the Congo

1. Annexed hereto is a letter dated November 19, 1976 from the Minister of Finance of the People's Republic of the Congo setting forth the objectives and policies which the authorities of the People's Republic of the Congo will pursue.

2. The International Monetary Fund grants this stand-by arrangement to support these objectives and policies.

3. The People's Republic of the Congo will remain in close consultation with the Fund during the period of the stand-by arrangement and, in particular, will consult with the Fund in accordance with paragraph 7 of the annexed letter. These consultations may include correspondence and visits of officials of the Fund to the People's Republic of the Congo or of representatives of the People's Republic of the Congo to Washington, D.C. For the purpose of these consultations, the People's Republic of the Congo will keep the Fund informed of developments in the exchange, trade, credit, and fiscal situation through reports at intervals or dates requested by the Fund.

4. For a period of twelve months from \_\_\_\_\_ the People's Republic of the Congo will have the right, after making full use of any gold tranche that it may have, to make purchases from the Fund in the currencies of other members in exchange for its own currency in an amount equivalent to SDR 4.7 million. The amounts available in accordance with this paragraph 4 shall be augmented by amounts equivalent to repurchases in respect of purchases under the stand-by arrangement, unless when any such repurchase is made, the People's Republic of the Congo informs the Fund that it does not wish the stand-by arrangement to be augmented by the amount of that repurchase.

5. The People's Republic of the Congo will pay charges for this stand-by arrangement in accordance with Executive Board Decision No. 270-(53/95), adopted December 23, 1953; 876-(59/15), adopted April 27, 1959; and 1345-(62/23), adopted May 23, 1962.

6. Subject to paragraph 4 above, the People's Republic of the Congo will have the right to engage in the transactions covered by this stand-by arrangement without further review by the Fund. This right can be suspended only with respect to requests received by the Fund after (a) a formal ineligibility, or (b) a decision of the Executive Board to suspend transactions, either generally (under Article XVI, Section 1(a)(ii)) or in order to consider a proposal, made by an Executive Director or the Managing Director, formally to suppress or to limit the eligibility of the People's Republic of the Congo. When notice of a decision of formal ineligibility or of a decision to consider a proposal is given pursuant to this paragraph 6, purchases under this stand-by arrangement will be

resumed only after consultation has taken place between the Fund and the People's Republic of the Congo and understandings have been reached regarding the circumstances in which such purchases can be resumed.

7. Not later than three years after each purchase of exchange by the People's Republic of the Congo under this arrangement, the People's Republic of the Congo shall repurchase an equivalent amount of the People's Republic of the Congo's currency from the Fund, provided that, if the People's Republic of the Congo's currency held by the Fund as a result of transactions under this arrangement is reduced by repurchases under Article V, Section 7, or otherwise, such reductions shall be credited against the earliest amounts that become payable under this paragraph 7. Repurchases shall be made with the assets specified by the Fund at the time of the repurchase, in accordance with the Fund's policies and practices at the time of repurchase.

8. The rate of exchange at which the People's Republic of the Congo will purchase currencies from the Fund in exchange for the People's Republic of the Congo's currency and at which the Fund will return the People's Republic of the Congo's currency in repurchase operations and make all other computations involving the People's Republic of the Congo's currency will be such rate as the Fund may from time to time determine under Article IV, Section 8, of the Fund Agreement.

Annex to Stand-By Arrangement

PEOPLE'S REPUBLIC OF THE CONGO

Ministry of Finance

The Minister

Brazzaville, November 19, 1976

Dear Mr. Witteveen:

1. The Congo's oil production, after having increased substantially in 1973 and 1974, has since declined. In addition, exports of forest products have fallen. As a result, the improvement in the balance of payments recorded in 1974 has not continued, and in 1975 the Congo again incurred a balance of payments deficit. The Central Bank's external assets have declined by CFAF 2.2 billion in 1975 and by CFAF 2.7 billion in the first six months of 1976. The Government budget has also registered increasing deficits. Prospects are that, in the absence of a corrective program, these deficits will continue. In these conditions, the Government of the Congo is adopting a financial program to improve the budgetary and balance of payments situations. In view of the low level of external reserves, the Government of the People's Republic of the Congo requests a stand-by arrangement from the International Monetary Fund in the amount of SDR 4.7 million for a period of one year; this amount will be augmented by the amount of any repurchases in respect of purchases under the requested stand-by arrangement. Prior to any purchase under the requested stand-by arrangement, the Government will consult with the Managing Director of the International Monetary Fund concerning the currencies to be purchased. The Government intends to block in a special account with the Central Bank the counterpart in CFA francs of purchases made under the stand-by arrangement.

2. The program for 1977 is being reviewed by the Government as part of a longer-term program to assure a satisfactory rate of growth and eventual equilibrium in the balance of payments. Such a program is expected to include, among others, measures relating to producer prices for agricultural products, the granting of seasonal and medium-term credit and extension services to the agricultural sector, reshaping of current expenditures with a reduction in their growth rate, and improvement of the financial situation of state enterprises. The Government hopes to elaborate such a program and to begin to implement it before the end of next year. Meanwhile, the financial program for 1977, as described below, aims at limiting the overall balance of payments deficit to CFAF 2.0 billion.

### Fiscal Policies

3. In the 1976 budget, the Government adopted several measures including increases in certain tax rates, to improve public finances. Nevertheless, as a result of a further decline in oil production, the overall deficit is still large. Hence, the Government intends to limit current expenditures with a view to bringing them in better balance with the long-term revenue prospects. The 1977 budget, now being drawn up, will limit total expenditures to CFAF 48.0 billion. Current expenditures, excluding debt service, will be limited to CFAF 43.0 billion, or at the level of expenditures expected to be realized for 1976. Expenditures on wages and salaries will be held at the 1976 level, except for those in respect of hiring personnel completing their training. Transfers to state enterprises will also be held at their actual 1976 levels, pending the results of envisaged studies on improving their operations. Other expenditures, especially those for material and supplies, which have increased considerably since 1974, will be examined with a view to effecting the savings needed to keep current expenditures at the above-mentioned level. Capital expenditures will be for only those projects for which non-bank or foreign financing becomes available. In view of the high level of foreign debt service until 1980, the Government will as far as possible avoid any further increase in its short-term and medium-term external debt.

4. Because of the budgetary problems, the Government has been forced to incur arrears in payments which already total about CFAF 16 billion. It is the Government's intention to reduce these arrears in 1977. To this end, a part of the counterpart funds of the requested drawing from the Fund under the compensatory financing decision will be utilized to reduce arrears. In regard to arrears vis-a-vis state enterprises, the reduction will be linked with efforts to make those enterprises more viable and to regularize their financial transactions with the Treasury.

### Credit Policies

5. The rate of expansion in total domestic credit will be limited to 5 per cent in 1977; the level of domestic credit will not exceed CFAF 41 billion at the end of 1977. As credit to the Government is limited by the statutes of the Central Bank and as the present level is close to that ceiling, most of this credit will be extended for purposes other than the Government budget. Since commercial banks' liquidity has now been largely absorbed, they will have to finance a large part of their additional credit operations through rediscounting with the Central Bank. Thus, the Central Bank will be in a better position to control credit expansion; in order to limit total credit to CFAF 41 billion, the BEAC intends to limit its total rediscounts, including rediscounts of customs duty bills and advances to banks, to CFAF 12 billion at the end of 1977, compared to CFAF 8.4 billion at the end of August 1976.

Trade and Payments Policies

6. The Government of the People's Republic of the Congo intends to maintain its present liberal system of trade and payments and does not intend to introduce new restrictions on imports for balance of payments reasons or on payments and transfers for current international transactions.

Consultations with the Fund

7. The Government of the People's Republic of the Congo believes that the measures set forth in the present letter will enable it to achieve the objectives of its financial program, but it will take any further measures that might become appropriate for this purpose. During the period of the stand-by arrangement the Government will consult with the International Monetary Fund on the adoption of any measure as might be necessary at the initiative of the Congo or at the request of the Managing Director of the International Monetary Fund if the objectives set forth in paragraphs 3 and 5 are not met, or if the Managing Director considers that consultation on the program is desirable.

Accept, Sir, the assurances of my highest consideration.

/s/

A. S. POATY  
Minister of Finance

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