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February 11, 1982

To: Members of the Executive Board  
From: The Secretary  
Subject: Zaire - Use of Fund Resources - Compensatory Financing Facility

Attached for consideration by the Executive Directors is a paper on a request expected to be received from Zaïre for a purchase equivalent to SDR 106.9 million under the compensatory financing facility. A draft decision appears on page 17.

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

ZAIRE

Use of Fund Resources--Compensatory Financing Facility

Prepared by the Research and African Departments

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

Approved by Wm. C. Hood and J.B. Zulu

February 10, 1982

The Managing Director has been informed that the Zairian authorities will shortly request a purchase of SDR 106.9 million (46.9 per cent of quota) under the compensatory financing decision. The request is being made with respect to an export shortfall for the calendar year 1981, of which data for the second half are estimated. If approved, the proposed purchase would raise Zaire's outstanding purchases under the CFF from 3.1 per cent to 50 per cent of quota and the Fund's holdings of Zaire's currency to 267.4 per cent of quota. <sup>1/</sup> A waiver of the limitation in Article V, Section 3(b)(iii) of the Fund's Articles of Agreement will be required and is being proposed.

This paper, which is being circulated in advance of the formal request from Zaire, is presented in five sections and an annex. The sections deal with: (1) the balance of payments position and cooperation with the Fund; (2) estimation of the export shortfall; (3) causes of the shortfall and export prospects; (4) repurchase; and (5) staff appraisal and proposed decision. The annex provides a summary of Zaire's relations with the Fund.

1. Balance of payments position and cooperation with the Fund

a. Balance of payments <sup>2/</sup>

Following several years of inappropriate investment and other domestic policies, coupled with large recourse to external borrowing on terms and conditions often inconsistent with Zaire's debt-servicing capacity,

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<sup>1/</sup> Zaire's last purchase under the CFF, which amounted to SDR 28.25 million, was made in May 1977; of that purchase, SDR 7.0 million, or 3.1 per cent of quota, is currently outstanding.

<sup>2/</sup> A fuller explanation of Zaire's balance of payments position is contained in the staff report on the 1981 Article IV consultation (SM/81/241, 12/15/81 and Supplement 1, 1/19/82) and the background paper on recent economic developments (SM/82/3, 1/11/82), which are to be considered concurrently with this request.

the Zairian economy was ill-prepared to absorb the shock accompanying a 40 per cent deterioration in its external terms of trade in 1975. This was aggravated by a subsequent erosion of private sector confidence that has, inter alia, adversely affected capital inflows, as well as by insufficient recovery of export prices, particularly of the price of copper, the leading export. To abate the serious consequences for imports and thus for domestic production, adjustment policies and measures have been implemented, including a devaluation of the zaire by a cumulative 84 per cent vis-à-vis the SDR since October 1978; substantial debt relief has been sought and obtained through rescheduling; a small amount of emergency balance of payments assistance has also been secured; and a sizable deterioration has been permitted in the country's net external reserve position. Despite these policies and measures, imports of essential raw materials, spare parts, and fuels have had to be curtailed and external payments arrears have been accumulated.

During the period 1979-81 the overall balance of payments deteriorated markedly, from annual deficits of about SDR 180 million in 1979 and 1980 to a deficit of some SDR 570 million in 1981 (Table 1). This deterioration reflected a decline in exports, a virtual cessation of private capital inflows, and an increase in external debt service payments due before rescheduling. Total exports in 1981 were 14 per cent below average realizations in 1979-80. At the same time, public capital inflows rose much less in absolute terms—from SDR 154 million in 1979 to about 190 million in 1981—whereas debt service payments due increased from SDR 318 million in 1979 to SDR 589 million in 1981. There have also been leads and lags in the repatriation of investment income and receipts from other services, as well as significantly negative flows in the form of private capital and errors and omissions.

Thus, despite the containment of imports, the current account balance shifted from a surplus of SDR 11 million in 1979 to a deficit of SDR 418 million in 1981, equivalent to almost 9 per cent of GDP. The capital account balance stayed negative throughout this period at a level averaging 14 per cent of export earnings. Gross international reserves, the bulk of which is pledged or earmarked, have declined relative to imports from 4.4 months at the end of 1980 to 3.4 months at the end of 1981. Net external reserves at the end of 1981 were negative (by about SDR 80 million).

#### b. Cooperation

Since the proposed purchase of SDR 106.9 million would have the effect of raising Zaire's outstanding purchases under the CFF to 50 per cent of quota, it has to meet the test of cooperation applicable to the lower tranche of the facility, namely that the Fund be satisfied that the member will cooperate with the Fund in efforts to find, where required, appropriate solutions for its balance of payments difficulties. For reasons outlined below, the staff is of the opinion that this requirement is met in the case of Zaire.

Table 1. Zaire: Balance of Payments, 1979-81

(In millions of SDRs)

	1979	1980	1981 <u>1/</u>
A. Current account surplus or deficit (-)	<u>11</u>	<u>1</u>	<u>-418</u>
Trade account	<u>563</u>	<u>579</u>	<u>344</u>
Exports	(1,420)	(1,502)	(1,255)
Imports	(-857)	(-923)	(-911)
Services	-604	-680	-852
Of which: interest on public debt <u>2/</u>	(-126)	(-163)	(-287)
Unrequited transfers	52	102	90
B. Capital account	<u>-209</u>	<u>-197</u>	<u>-166</u>
Public capital	<u>-38</u>	<u>18</u>	<u>-112</u>
Of which: public debt amortization <u>2/</u>	(-192)	(-274)	(-302)
Private capital and errors and omissions	-171	-215	-54
C. SDR allocation	<u>16</u>	<u>16</u>	<u>16</u>
D=A+B+C Overall deficit (-)	<u>-182</u>	<u>-180</u>	<u>-568</u>
Financing	<u>182</u>	<u>180</u>	<u>568</u>
Debt rescheduling and emergency assistance	51	1,254	432
Payments arrears (decrease -)	168	-1,050	-65
Of which: cash payments	(-20)	(-50)	(-40)
Net Fund credit	-11	13	91
Purchases	(20)	(78)	(195)
Repurchases	(-31)	(-65)	(-104)
Other net reserve movements (increase -)	-26 <u>3/</u>	-37	110
<u>Memorandum item:</u>			
Gross international reserves equivalent in months of imports	3.8	4.4	3.4

Sources: Data provided by the Zairian authorities; and staff estimates.

1/ Revised estimates.

2/ Due before debt rescheduling.

3/ Includes valuation gains on gold sales of SDR 11 million.

Under an 18-month stand-by arrangement approved by the Executive Board on August 27, 1979, Zaire purchased the full amount of SDR 118 million specified in the arrangement. Subsequently, a three-year extended arrangement for an amount of SDR 912 million (400 per cent of Zaire's quota) was approved on June 22, 1981. Zaire made two purchases totaling SDR 175 million under the arrangement, but has not been able to make the third scheduled purchase of SDR 100 million because of failure to observe three of the four performance criteria established for end-September 1981. Indications are that certain of the performance criteria for end-December have also not been observed. Zaire's right to make purchases under the arrangement remains interrupted.

Developments in 1981 and the factors that led to nonobservance of the performance criteria are reviewed in the staff report on the 1981 Article IV consultation (SM/81/241 and Supplement 1) which is scheduled to be considered by the Board concurrently with the CF request. The report confirms that the policies and measures implemented in the context of the 1981 program, particularly the sizable devaluation of the Zaire and the substantial liberalization of the domestic pricing system, helped move the economy in the intended direction; but the envisaged performance could not be realized owing to several factors, some of which were clearly outside the control of the authorities. Export earnings in 1981 are estimated to have fallen 17 per cent below the level envisaged in the program, while none of the anticipated SDR 100 million of new loan disbursements for an important rehabilitation project was realized. As a result, imports fell significantly below the programmed level, and budgetary revenue was seriously affected. Concurrently, however, the budgetary policies followed led to a continued high level of expenditure in several areas, notably the Presidency and the Political Institutions, and education; there have also been certain unbudgeted outlays, including a large subsidy to the state oil importing company, cost overruns for a number of capital projects, and apparent slippages in the effectiveness of revenue collection.

In view of the adverse effects of external factors on the Zairian economy and the policy shortcomings noted above, there is a clear need for the adoption and implementation of further adjustment measures to deal with the difficulties faced by Zaire. The authorities are aware of the seriousness of these difficulties, and they have indicated that they intend to take additional measures to promote adjustment in cooperation with the Fund.

## 2. Estimation of the export shortfall

The Zairian authorities have requested that calendar 1981 be treated as the shortfall year. Since detailed data on actual export earnings are available only through June 1981, the staff in cooperation with the authorities has estimated exports for the second half (July-December 1981) of the shortfall year ended December 1981. <sup>1/</sup>

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<sup>1/</sup> Exports for the six months July-December 1981 have been estimated at a monthly average of SDR 93.4 million, compared with SDR 118.5 million per month for the corresponding period of 1980.

Total exports in 1981, estimated to have amounted to SDR 1,274 million, were 17 per cent below the average of SDR 1,536 million for the two preceding years and 18 per cent less than projected earnings of SDR 1,559 million for the two following years. On the basis of these export movements, the shortfall for the calendar year 1981 is estimated at SDR 215 million, which is more than twice the amount of the proposed purchase (Table 2).

Table 2. Zaire: Estimation of the Export Shortfall

(In millions of SDRs)

	Calendar Years				
	1979	1980	1981	Projected Exports 1/ 1982	1983
Exports 2/	1,460	1,616	1,274	1,430	1,700
Shortfall			214.9		
Proposed purchase			106.9		

1/ Based on the judgmental forecast of earnings given in Table 3.

2/ These export data differ from those compiled by the Bank of Zaire and used in the balance of payments, because the exports of copper, cobalt and zinc sold from Belgium are recorded when sales occur, whereas the Bank of Zaire data relate to the payments receipts, of which only a part is received at the time of shipment (i.e., pre-financing). Data for other exports and for copper, cobalt and zinc shipped direct to markets are those compiled by the Bank of Zaire.

The last compensatory financing purchase by Zaire, for an amount equivalent to SDR 28.25 million, was made in May 1977 in respect of a shortfall of SDR 133.9 million estimated for the calendar year 1976. When actual data for 1977 and 1978 became available, the shortfall for calendar 1976 was calculated to be SDR 99.8 million, smaller than the original estimate, but still more than three and a half times the purchase made.

### 3. Causes of the shortfall and export prospects

Out of the overall net shortfall estimated at SDR 215 million, SDR 173 million, or 80 per cent, was contributed by the principal minerals. The principal agricultural exports accounted for a shortfall of SDR 24 million. The two largest shortfalls were incurred by copper (SDR 74 million) and cobalt (SDR 78 million); smaller shortfalls are

Table 3. Zaire: Export Earnings and Shortfalls by Major Commodities

(In millions of SDRs)

	Years Ending December				Shortfall	
	1979	1980	1981	1982	1983	Geometric Arithmetic
<b>Total exports</b>	<u>1,459.7</u>	<u>1,616.5</u>	<u>1,273.5</u>	<u>1,430.0</u>	<u>1,700.0</u>	<u>214.9</u> <u>222.4</u>
Principal mineral exports	(1,250.2)	(1,354.1)	(1,093.0)	(1,210.0)	(1,450.0)	(172.6)
Copper	530.8	710.2	623.3	760.0	925.0	74.3
Cobalt	490.9	355.0	139.1	115.0	175.0	78.5
Zinc	20.9	15.9	48.7	50.0	60.0	-14.2
Diamonds	76.2	74.0	54.1	60.0	70.0	12.2
Petroleum	131.4	199.0	227.8	225.0	220.0	-31.0
Principal agricultural exports	(119.2)	(141.8)	(102.6)	(130.0)	(145.0)	(24.1)
Coffee	106.3	125.8	88.6	114.0	127.0	22.8
Rubber	12.9	16.0	14.0	16.0	18.0	1.3
Other exports	90.3	120.5	77.9	90.0	105.0	17.8
						18.8
(Annual Rate of Change in Earnings from Previous Years)						
<b>Total exports</b>	<u>90.8</u>	<u>10.7</u>	<u>-21.2</u>	<u>12.3</u>	<u>18.9</u>	
Principal mineral exports	(63.4)	(8.3)	(-19.3)	(10.7)	(19.8)	
Copper	3.7	33.8	-12.2	21.9	21.7	
Cobalt	120.7	-27.7	-60.8	-17.3	52.2	
Zinc	-32.1	-23.9	306.3	2.7	20.0	
Diamonds		-2.9	-26.9	10.9	16.7	
Petroleum		51.4	14.5	-1.2	-2.2	
Principal agricultural exports	(19.0)	(19.0)	(-27.6)	(26.7)	(11.5)	
Coffee		18.3	-29.6	28.7	11.4	
Rubber		24.0	-12.5	14.3	12.5	
Other exports		33.4	-35.4	15.5	16.7	

Source: Data provided by Zairian authorities and Fund staff estimates. See also footnote 2 to Table 2.



Table 4. Zaire: Value, Volume and Unit Value by Major Commodities

(1981=100)

	Value Share in Total Exports in 1981 (In Per Cent)	Years Ending December						Shortfall in Per Cent of Level in Shortfall Year
		1978	1979	1980	1981	1982	1983	
<u>Value</u>	<u>93.8</u>	<u>64</u>	<u>115</u>	<u>125</u>	<u>100</u>	<u>112</u>	<u>133</u>	<u>16.4</u>
Principal mineral exports	85.7	(70)	(114)	(124)	(100)	(111)	(133)	(15.9)
Copper	48.9	82	85	114	100	122	148	11.8
Cobalt	10.9	160	353	255	100	83	126	56.6
Zinc	3.8	63	43	33	100	103	123	-29.1(excess)
Diamonds	4.2	--	141	137	100	111	129	22.6
Petroleum	17.9	--	58	87	100	99	97	-13.5(excess)
Principal agricultural exports	8.1	--	(116)	(138)	(100)	(127)	(141)	(23.4)
Coffee	7.0	--	120	142	100	129	143	25.7
Rubber	1.1	--	92	114	100	114	129	9.1
<u>Volume</u>		<u>95</u>	<u>111</u>	<u>107</u>	<u>100</u>	<u>108</u>	<u>118</u>	<u>8.6</u>
Principal mineral exports		(104)	(112)	(107)	(100)	(107)	(118)	(8.6)
Copper		100	83	99	100	105	110	-1.0(excess)
Cobalt		344	276	182	100	133	200	67.9
Zinc		85	47	36	100	92	103	-30.7(excess)
Diamonds		--	122	129	100	105	110	12.7
Petroleum		--	103	91	100	99	97	-2.1(excess)
Principal agricultural exports		--	(97)	(114)	(100)	(115)	(117)	(8.3)
Coffee		--	100	118	100	116	117	9.9
Rubber		--	80	93	100	110	114	-1.4(excess)
<u>Unit value</u>		<u>67</u>	<u>103</u>	<u>117</u>	<u>100</u>	<u>104</u>	<u>113</u>	<u>7.2</u>
Principal mineral exports		(67)	(102)	(116)	(100)	(104)	(112)	(6.6)
Copper		82	102	115	100	116	135	12.9
Cobalt		47	128	140	100	62	63	-6.9(excess)
Zinc		75	92	91	100	112	119	2.2
Diamonds		--	115	106	100	106	118	8.8
Petroleum		--	56	96	100	100	100	-11.7(excess)
Principal agricultural exports		--	(120)	(121)	(100)	(110)	(121)	(14.1)
Coffee		--	120	121	100	111	122	14.5
Rubber		--	115	123	100	104	113	10.7

estimated for coffee (SDR 23 million), diamonds (SDR 12 million), rubber (SDR 1 million), and "other exports" (SDR 18 million). Excesses are estimated for petroleum (SDR 18 million) and zinc (SDR 14 million).

The sizable earnings shortfall for copper, as well as the much smaller one for rubber, are entirely attributable to price shortfalls; weak international markets for these commodities caused the unit values of Zaire's exports to fall, and market improvement is expected to lead to a recovery in the post-shortfall period. The relatively small shortfall for diamonds is attributable about equally to price and volume factors, with poor world demand, compared with that in the preceding years, being the major reason for reduced exports in 1981; again some improvement is anticipated in 1982-83. The earnings shortfall for coffee was due mainly to a price shortfall, but a volume shortfall caused by ICO quota restrictions was a contributory factor. The shortfall for "other exports," most of which are minor minerals, was also attributable to adverse demand factors. The sum of the foregoing shortfalls is SDR 128 million, which accounts for 60 per cent of the overall net shortfall, and this portion of the shortfall in total earnings is attributable to factors clearly beyond the member's control.

In the case of cobalt, the shortfall in earnings is entirely related to a drop in volume, and the question to be addressed is whether the shortfall in cobalt was attributable to factors outside the control of Zaire. The staff believes that weak demand conditions were the principal cause of the drop in cobalt earnings in 1981, and that the country's marketing policy has probably had no effect on the size of the calculated shortfall. The reasons for this conclusion are set out below.

Developments regarding Zaire's cobalt situation since 1978 can be summarized as follows:

(i) Following a surge in world demand, Zaire, which is the largest producer and exporter of cobalt, raised its cobalt price in October 1978 from \$6.4 per pound to \$20 per pound. <sup>1/</sup> Its export earnings in that year increased by 36 per cent to SDR 222 million, almost entirely because of higher prices; the export unit value for the year averaged \$8.4 per pound, compared with \$5.9 in 1977 (Table 5).

(ii) In February 1979 Zaire raised its price to \$25 per pound. The value of its cobalt exports more than doubled to SDR 491 million, again entirely because of higher export unit values (\$23.7 per pound); the volume of exports declined by 20 per cent (to 12,000 tons) and stocks increased by 1,700 tons to 15,800 tons.

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<sup>1/</sup> The invasion in May 1978 of Shaba, the province where cobalt is produced in Zaire, caused considerable anxiety to consumers about the continued availability of adequate supplies of cobalt, which is used chiefly in industrial purposes such as aircraft engines.

Table 5. Zaire: Cobalt Production, Stocks, and Exports

	World	Zaire				
	Production	Production	Exports <u>1/</u>	Stocks	Export Unit Value	Export Earnings <u>1/</u>
		(1,000 tons)			(\$/lb.)	(SDR millions)
1975	36.3	13.6	11.5	21.6	3.7	76.5
1976	28.7	10.7	11.5	20.8	4.6	100.1
1977	32.6	10.2	14.9	16.8	5.9	163.0
1978	34.0	13.1	15.0	14.1	8.4	222.4
1979	32.0	14.0	12.0	15.8	23.7	490.9
1980	29.8	14.5	8.0	22.4	25.0	355.0
1981		11.0	4.5	29.7	16.5	139.1
1982		11.0	6.0	34.7	10.0	115.0
1983		10.0	9.0	35.7	10.0	175.0

1/ Export data from 1971 through 1977 are taken from data provided in connection with the previous CF request by Zaire (EBS/77/120, 4/20/77); and from 1978 on, they are taken from data used in connection with the present CF request.

(iii) By the middle of 1980, there was a shift in demand as consumers had acquired ample stocks and industrial activity began to slow down; thus, at the fixed price of \$25 per pound, Zaire could sell only 8,000 tons or 33 per cent less than in 1979, and the value, at SDR 355 million, was 28 per cent lower than in 1979. Zaire accumulated 6,600 tons of stocks (to 22,400 tons).

(iv) In February 1981 Zaire reduced its price to \$20 per pound, which still proved too high, and sales could be effected only at substantial discounts. Following sales to the U.S. government stockpile at \$15 per pound, Zaire reduced its official price to \$17.5 per pound in August 1981. The average price for 1981 fell to \$16.5 per pound and export volume to 4,500 tons, <sup>1/</sup> which was 44 per cent lower than in 1980; the combined effect was a 61 per cent drop in earnings to SDR 139 million. Even though production was scaled down, an increase of 7,300 tons in stocks could not be avoided; stocks at the end of 1981 totaled 29,700 tons, nearly three times Zaire's output of cobalt in that year.

(v) Zaire announced a further price reduction to \$12.5 per pound effective February 1, 1982. Zaire's production is expected to be maintained at 11,000 tons in 1982, but to decline to 10,000 tons in 1983; export volume is projected to recover to 6,000 tons in 1982 and to 9,000 tons in 1983, and export unit values to average \$10 per pound in each year. Earnings for the two post-shortfall years are projected to average little more than the 1981 level of SDR 139 million.

The relevant question, so far as the shortfall calculation is concerned, is whether Zaire's marketing policy over the five-year trend period, particularly in the shortfall year, has had the effect of destabilizing earnings from cobalt exports in such a way as to cause a shortfall to occur in 1981; the question can be raised in two parts:

(i) Could Zaire's earnings during the shortfall year have been higher? and

(ii) Are projected earnings for 1982-83 realistic?

The world demand for cobalt was severely depressed in 1981. Some users had already begun to substitute other materials for cobalt, consumer stocks had already been built up, as previously noted, and, most important, economic activity slowed down substantially as industrial countries moved into recession. In the circumstances, had Zaire offered to sell in 1981 additional quantities from its huge stocks of cobalt (equivalent to 90 per cent of annual world production), its earnings in that year would have been lower than the earnings it actually realized. In other words, there was in all likelihood no reduction in price and consequent stimulation of sales that could have improved cobalt export earnings in 1981.

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<sup>1/</sup> Including about 1,500 tons out of the 2,360 tons sold to the U.S. Government stockpile.

It may also be argued that Zaire's cobalt earnings in the two pre-shortfall years were high because of an excessively high level of prices set by Zaire. Zaire's pricing policy was obviously motivated by a desire to maximize earnings, but the crucial fact is that it was the shift in demand which caused the increase in prices. Indeed, Zaire resisted raising its prices in line with the much higher prices (of \$50 per pound) reached on the free market at the height of the crisis in the first quarter of 1979. It is reasonable to conclude that, while its aim was to maximize earnings, Zaire was also conscious of the adverse effects of high prices on long-term demand for the metal.

As regards the reasonableness of the projections for 1982-83, it is the judgment of the staff that, because of the anticipated slow pick-up in demand for cobalt, the best that Zaire could expect is to avoid a further drop in earnings. This can be achieved only by lowering prices, and at the same time increasing the volume of exports. Projected volume increases, however, represent only a partial recovery and imply a further increase in stocks, though in smaller quantities than were accumulated during the shortfall year.

To summarize, the staff believes that: (a) the variation in world demand for cobalt is the principal source of the instability in Zaire's earnings during the five-year trend period 1979-83; (b) Zaire's policy of setting the export price of cobalt had to be adjusted to conform to market conditions; (c) the accumulation of stocks in the shortfall year did not cause earnings to decline in that year and was not effected in anticipation of higher prices during the two post-shortfall years; and (d) further stock accumulation, not decumulation, is expected during the two post-shortfall years.

#### a. Principal minerals

These minerals accounted for 86 per cent of Zaire's exports in 1981, and the aggregate shortfall of SDR 173 million estimated for them represented 80 per cent of the overall net shortfall. Zaire is the world's leading exporter of cobalt and industrial diamonds and it produces a wide range of other minerals. Excesses for 1981 are estimated only for zinc and crude petroleum.

All Zaire's minerals, except petroleum and the copper produced by SODIMIZA, which is exported direct to Japan, are marketed by SOZACOM, the state-owned mineral marketing agency. In the case of copper, cobalt, and zinc, significant quantities are shipped to Belgium for processing and sale by SGM, in addition to the quantities shipped by SOZACOM from Zaire direct to markets. For these three metals, the export data used in this paper relate to the volumes and values of the metals sold by SGM from Belgium at the time of their sale, as well as to the values and volumes of metals sold by Zaire direct to markets. Prefinancing (i.e., advance payments by SGM to Zaire on account of metal shipped to Belgium, but not yet sold) is ignored. For this reason, the data for these metals do not correspond to data compiled by the Bank of Zaire.

The following is a review of the situation and outlook for Zaire's major exports, except for cobalt which was discussed above.

(1) Copper

Copper accounted for nearly half of Zaire's total exports in 1981 and the estimated shortfall of SDR 74 million amounted to more than one third (35 per cent) of the overall shortfall.

Export earnings from copper, after rising by 34 per cent in 1980, were 12 per cent lower in 1981, but are expected to recover at an annual rate of 22 per cent in 1982 and 1983. The shortfall was entirely price related. Production of copper in 1981, estimated at 462,000 tons, was slightly higher than in 1980 (460,000 tons), in spite of shortages of skilled personnel and spare parts for mining machinery. Sporadic transportation difficulties prevented a larger increase in the volume of exports than the one per cent increase realized in 1981. Export unit values, however, were, on average, 13 per cent lower than in 1980, owing to the very weak state of world industrial demand. The London Metal Exchange (LME) spot price, on which most copper sales outside North America are based, averaged 79 U.S. cents per pound in 1981, some 20 per cent below the average of 99 cents per pound in 1980. Activity in the transportation, construction, and electrical industries--all large users of copper--was at a low ebb, and extensive production cuts were made in a number of countries, particularly in North America.

In the post-shortfall period, a modest rise in the volume of Zaire's copper exports, of the order of 5 per cent a year, is foreseen, with production being maintained at a level close to that of 1981. On the other hand, export unit values are projected to recover at an annual average rate of 16 per cent in 1982 and 1983. The projected recovery is based on a revival of demand beginning around the middle of 1982 and gaining strength in 1983. World stocks of copper in late 1981, estimated at less than one million tons, were the lowest for at least five years and about half their 1977 level. High interest rates have discouraged consumers from holding more than their minimum essential requirements, and producers' stocks are not excessive because of production curtailments. The low price in 1981 caused a sharp reduction in the production of secondary metal. Any revival in demand accompanied by reduced interest rates will lead to sharply rising copper prices as consumers compete to replenish their stocks. It will take time to restore productive capacity which has been idled for lack of demand, and new capacity due to come on stream in the next two years is not very considerable (approximately 120,000 tons in 1982). There are uncertainties over the size of supplies from such producers as Poland (about 340,000 tons in 1980), and Canada (708,000 tons in 1980) where all labor contracts in the copper mining industry are due for renewal during 1982. In 1983 labor contracts in the U.S. industry are due for renewal at mid-year, and the prospect of strikes has traditionally led to precautionary stockpiling by consumers. For all these reasons, a significant improvement in the copper market is expected in the next two years.

Taking account of the price and volume movements over the five-year trend period 1979-83, a shortfall of SDR 74 million is estimated for copper in 1981.

(2) Zinc

Zinc, which accounted for less than 4 per cent of total export earnings, recorded an export excess of SDR 14 million in 1981.

As in the case of copper and cobalt, some of Zaire's zinc is exported direct to markets and the remainder is exported through Belgium. The value of total zinc exports in 1981 was three times greater than in 1980, but is expected to increase much more moderately in 1982 and 1983. The excess in 1981 was entirely volume related. Although production is estimated to have increased by over 30 per cent to approximately 57,000 tons in 1981, the trebling of export volume in that year was due largely to the sale of almost 40,000 tons of stocks, which had accumulated in 1980 owing to marketing difficulties in that year. Export unit values for zinc in 1981 were also higher than in the two previous years, by about 10 per cent, reflecting a stronger market for zinc than most other metals, because of lengthy strikes in at least two producing countries which created a shortage of zinc concentrates.

In 1982 and 1983 Zaire's zinc output is expected to increase to slightly over 60,000 tons, but by contrast with 1981, exports will not include the sale of stocks carried over from a previous year. Volume is expected to fall moderately in 1982 but to resume growth gradually in 1983, while export unit values are projected to increase significantly in anticipation of a general strengthening of world demand.

(3) Diamonds

Zaire is the world's leading exporter of industrial diamonds, and such diamonds accounted for slightly more than 4 per cent of the value of Zaire's total exports in 1981. The estimated shortfall of SDR 12 million was related rather more to volume than to price factors.

Owing to the recession and the generally low level of economic activity, world demand for industrial diamonds weakened considerably in 1981, as demonstrated by the fact that sales of the Central Selling Organization of the DeBeers group in 1981 were 46 per cent lower than in 1980. Although smuggling of part of Zaire's diamond output has not been stamped out, the level of this kind of activity is believed to be declining following the introduction in February 1980 of a system of direct payment in foreign exchange for diamonds purchased from small-scale miners. In spite of this, the volume of official diamond exports in 1981 was 20 per cent below the average level of the two preceding years. In addition to poor demand, this decline was partly due to difficulties with the treatment plant, as well as to the exhaustion of high-content gravel stocks. Export unit values in 1981 were also nearly 10 per cent lower. Consequently, the value of Zaire's exports in 1981 was 28 per cent below the average level for 1979-80.

A recovery is projected for 1982-83. In 1981 the authorities decided to terminate the arrangement of 14 years' standing with the DeBeers group, whereby that group had the sole selling rights for Zaire's diamonds, and they have entrusted future sales to SOZACOM. It is too early to predict the effects of this new arrangement on future export sales, but in anticipation of a gradual improvement in world demand, the volume of Zaire's exports is projected to increase by about 5 per cent per annum in 1982 and 1983. Export unit values are projected to increase by 6 per cent in 1982 and by a further 11 per cent in 1983.

(4) Petroleum

An export excess of SDR 31 million is estimated for petroleum, which accounted for nearly 18 per cent of total exports in 1981. The value of exports increased by more than 14 per cent in 1981, but in the post-shortfall period is expected to average about 2 per cent less.

All Zaire's production of crude oil is exported. After declining by 12 per cent in 1980 because of intermittent pressure losses in the wells, the volume of output and exports recovered in 1981, but is projected to remain at a slightly lower level in 1982-83. Unit values, which had increased by over 70 per cent in 1980, rose by only 4 per cent in 1981, and are projected to remain at the same level in the post-shortfall period. The excess is attributable mainly to price.

b. Principal agricultural products

The two major agricultural commodities, coffee and rubber, together accounted for one twelfth of Zaire's total exports in 1981, and the estimated shortfall of SDR 24 million for them accounts for 11 per cent of the net overall shortfall.

(1) Coffee

The third largest shortfall, SDR 23 million, for any single commodity is estimated for coffee, rather more because of price factors than because of volume factors. The value of exports fell by nearly 30 per cent in 1981, but is expected to recover significantly in 1982-83.

After rising by 18 per cent in 1980, the volume of Zaire's coffee exports, mostly of the robusta variety, returned in 1981 to the 1979 level. This was due partly to distribution difficulties and some increase in smuggling along the border areas, but mainly to a 15 per cent cut by the International Coffee Organization in Zaire's 1980/81 (October-September) export quota to 61,700 tons, compared with an original quota for the year of 72,000 tons. The unit value of Zaire's coffee exports, which had remained steady in 1979 and 1980, fell by 17 per cent in 1981 because of the weak market conditions. Zaire's ICA export quota for October 1981/September 1982 has been raised back to 72,000 tons, and hence the volume of its coffee exports is projected to rise by 16 per cent in 1982 and to remain close to that level in 1983. The year 1981 is seen as the low year



for international coffee prices, since the effect of the Brazilian frost in the middle of that year will begin to be reflected in supply availabilities from mid-1982. Increases of 11 per cent per annum in export unit values are projected for 1982 and 1983.

## (2) Rubber

In 1981 natural rubber accounted for only about 1 per cent of total exports, and incurred a small shortfall, estimated at SDR 1.3 million, entirely on account of price factors. The volume of exports increased in both 1980 and 1981, but owing to the weakness of world demand during the recession, export unit values dropped by 19 per cent in 1981. Modest increases in both volume and price are projected for 1982-83, the former as a result of the coming into production of hevea trees planted several years ago, and the latter on account of the improvement anticipated in the market for natural rubber when industrial activity recovers.

## c. Other exports

This category of exports includes a large number of relatively minor minerals, such as gold, silver, cadmium, tungsten, tin, cassiterite, tantalite, and monazite; a variety of agricultural products such as, cocoa, tea, wood, palm and palm kernel oil and oil-cakes, and cinchona; and several manufactured products, such as cement. Together, all these products accounted for 6 per cent of the total value of Zaire's exports in 1981, and the shortfall of SDR 18 million estimated for them represents 8 per cent of the overall net shortfall.

The value of "other exports" fell by 35 per cent in 1981, in some cases such as wood, palm kernel oil and cake, and cement, largely on account of reduced volumes due to smaller output, but in most of the other cases, particularly silver, tin, cassiterite, cadmium, tungsten, tantalite, cocoa, and cinchona, on account of price declines, reflecting weak market conditions. For some of the items, there were declines in both volume and price. For 1982 and 1983, earnings from other exports are projected to grow at an annual rate of 16 per cent, partly because of expected price improvements.

## 4. Repurchase

In accordance with paragraph 7 of the compensatory financing decision, the Zairian authorities are expected to represent that they will make a repurchase in respect of any outstanding part of this purchase if the amount purchased on the basis of partly estimated data (i.e., estimates for the six-month period July-December 1981) exceeds the amount that could have been purchased on the basis of actual data for the entire shortfall year. The amount to be repurchased would be equivalent to the excess amount purchased by using partly estimated rather than actual data for the entire shortfall year.

5. Staff appraisal and proposed decision

The Zairian authorities are expected to request a purchase equivalent to SDR 106.9 million, or 46.9 per cent of quota, under the compensatory financing facility in respect of a shortfall for the calendar year 1981, which is estimated to be SDR 215 million. The proposed purchase would raise Zaire's outstanding purchases under the facility to 50 per cent of quota. Exports for the last six months of the shortfall year have been estimated by the staff in cooperation with the authorities and, consequently, the request for the purchase is expected to include a representation by the authorities that they will make a prompt repurchase of the amount of any overcompensation calculated on the basis of actual data for the whole shortfall year rather than of partly estimated data for the year.

The overall balance of payments deficit is estimated to have increased by SDR 388 million to SDR 568 million in 1981, owing to a sharp deterioration in the current account deficit. Gross international reserves at the end of 1981, most of which were pledged or earmarked, amounted to the equivalent of about three and a half months of imports. The staff considers that the balance of payments need of Zaire justifies the proposed purchase. The staff also believes that the requirement of cooperation relating to a compensatory financing purchase by Zaire that would raise the member's outstanding purchases under the facility up to 50 per cent of quota is met.

Total export earnings in 1981 (SDR 1,274 million) are estimated to have fallen 17 per cent below the average of the two preceding years (SDR 1,536 million) and to be 18 per cent below the average projected for the two succeeding years (SDR 1,559 million). On this basis, the shortfall estimated for 1981 is SDR 215 million. Shortfalls are estimated for all the major commodities and "other exports," except for petroleum (an excess of SDR 31 million) and zinc (an excess of SDR 14 million). All of the shortfalls are attributable to factors largely beyond the member's control. The large shortfall for copper (SDR 74 million) was entirely price related, stemming from the weakness of world demand and low prices in 1981, and the recovery projected for 1982-83. The third largest shortfall, of SDR 23 million, for coffee, is attributable to both price and volume factors which were largely beyond Zaire's control: a world oversupply situation in 1981 led both to lower prices and a reduction of export quotas under the provisions of the International Coffee Agreement; some improvement is expected in 1982-83, because the 1981 frost in Brazil, the leading producer, should reduce the coffee supplies available in those years. The shortfall of SDR 12 million estimated for diamonds was also due to both price and volume factors, relating mainly to the recession in 1981 and the expected recovery in 1982-83. The small shortfall for rubber (SDR 1 million) was caused entirely by price factors--prices slumped in 1981, but are expected to strengthen when demand improves in the next two years. The shortfall of SDR 18 million for "other exports," which include a wide variety of mineral, agricultural, and manufactured products, can also be traced mainly to weak demand.

The large shortfall of SDR 78 million for cobalt is entirely related to a drop in volume. The weakness of demand during the recession caused the volume of Zaire's cobalt exports to fall by 44 per cent in 1981, in spite of a 34 per cent decline in price, and the value of these exports was 61 per cent lower. The staff believes that the reduction in cobalt earnings in 1981 resulted from weakness in world demand; a further reduction in price would not have improved sales significantly, and in all likelihood earnings would have declined more steeply. The price is expected to be reduced further, by 39 per cent in 1982-83, and with a gradual recovery in demand, the volume is projected to increase by a third in 1982 and by a half in 1983. These projections imply a 17 per cent decline in value in 1982, followed by a 52 per cent rise in 1983.

The staff considers that the overall shortfall of SDR 215 million is attributable to circumstances largely beyond the control of Zaire. In the light of the recovery projected, the staff also considers that the shortfall is temporary in character. Recent economic developments and performance by Zaire under the extended arrangement are reviewed in the staff report on the Article IV consultation, which is expected to be considered by the Executive Board at the same time as the request for a CF purchase. The request is expected to include a statement that Zaire will cooperate with the Fund in efforts to find, where required, appropriate solutions for its balance of payments difficulties. The staff therefore believes that the expected request will meet all the requirements set forth in the compensatory financing decision. Accordingly, the following draft decision is proposed for adoption by the Executive Board after a duly authenticated request has been received:

1. The Fund has received a request from the Government of Zaire for a purchase of the equivalent of SDR 106.9 million under the Decision on Compensatory Financing of Export Fluctuations (Executive Board Decision No. 6224-(79/135), adopted August 2, 1979).
2. The Fund notes the representation of Zaire and approves the purchase in accordance with the request.
3. The Fund waives the limitation in Article V, Section 3(b)(iii).

Zaire - Relations with the Fund

Date of membership	September 28, 1963
Quota	SDR 228 million
Status	Article XIV
Exchange system	The zaire is pegged to the SDR. As of January 31, 1982 the rate was Z 1 = SDR 0.1575.
Fund holdings of Zaire's currency (January 31, 1982)	SDR 501.56 million (219.98 per cent of quota), of which SDR 7.0 mil- lion (3.09 per cent) was related to - purchases under the compensatory financing facility and SDR 17.8 mil- lion (7.8 per cent) to purchases under the oil facility.
SDR holdings (January 31, 1982)	SDR 12,022, equivalent to 0.01 per cent of the net cumulative allocation of SDR 86.3 million.
Direct distribution of profits from gold sales	US\$17.96 million.
Gold distribution (four distributions)	96,708.971 fine ounces
Trust Fund loan disbursements	SDR 110.43 million.
Technical assistance	Five CBD experts, including a Principal Manager, are currently serving in the Bank of Zaire.  A technical assistance mission from FAD visited Zaire in August- September 1981, and its report is under preparation.
Staff contacts	Discussions regarding the authorities' program of economic and financial adjustment for 1981-83, which is being supported by the current extended arrangement, were held both in Kinshasa and Washington over the period from late November 1980 to early May 1981. Zaire's

Staff contacts (continued)

request for the extended arrangement (EBS/81/126) was approved on June 22, 1981.

A staff team visited Kinshasa during the period October 15-25, 1981 to review the latest monetary accounts and to suggest improvements in the Bank of Zaire's balance sheet.