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November 17, 1997

To: Members of the Executive Board

From: The Acting Secretary

Subject: Sudan—Staff-Monitored Program—Report on Developments Through
October 1997

Attached for the information of the Executive Directors is a report on developments through October 1997 under the staff-monitored program for Sudan.

Mr. V. Sundararajan (ext. 38573), Mr. Shabsigh (ext. 35364), or Mr. Treichel (ext. 34045) is available to answer technical or factual questions relating to this paper.

Unless the Documents Preparation Section (ext. 36760) is otherwise notified, the document will be transmitted, in accordance with the procedures approved by the Executive Board and with the appropriate deletions, to the WTO Secretariat on Tuesday, November 25, 1997; and to the African Development Bank (AfDB), the Arab Monetary Fund (AMF), the European Commission (EC), and the Islamic Development Bank (IsDB).

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INTERNATIONAL MONETARY FUND

SUDAN

Staff-Monitored Program—Report on Developments Through October 1997

Prepared by the Middle Eastern and Policy Development
and Review Departments

Approved by P. Chabrier and T. Leddy

November 17, 1997

1. This note provides information on recent developments in economic performance and policies under Sudan's staff-monitored program, and reports on compliance with the quantitative benchmarks through end-September 1997 and the structural benchmarks for October 1997.¹ Six reports on developments from April through September 1997 have been issued to date for the information of the Executive Board. In addition, the staff report, that reviewed performance under the program during the first half of 1997 and reported on compliance with the quantitative benchmarks through end-June 1997 and the structural benchmarks for July 1997, was considered by the Executive Board on August 29, 1997.²
2. Recent developments are in line with the objectives for the staff-monitored program; specifically, payments to the Fund through October were effected as committed, for a total of US\$50.4 million since the start of the year;³ the structural benchmarks for the month of October were met as detailed in Table 2, and further discussed in paragraphs 8 to 11 ; and data and economic information have been reported to the Fund as specified under the program.

¹The staff team that visited Khartoum during the period October 20–29, 1997, comprised Messrs. Sundararajan, Shabsigh, and Treichel (all MED), and overlapped with a Fiscal Affairs Department technical assistance mission to assist in value-added tax (VAT) and tariff reform. The mission met with the Honorable Abdallah Hassan Ahmed, Governor of the Bank of Sudan, Dr. Saber Mohamed Al-Hassan and Dr. Izzedin Ibrahim, State Ministers of Finance, and other senior officials.

²See EBS/97/151, 8/15/97, considered at EBM/97/89, 8/29/1997.

³This includes an additional monthly payment of US\$0.7 million in October, with a view to stabilizing Sudan's arrears to the Fund in SDR terms.

3. Progress on macroeconomic stabilization remains good. Inflation has continued to fall, reaching 19 percent (year-on-year) in October 1997 compared to 114 percent in December 1996; the CPI declined in October by 2.2 percent, following a decline by 1.9 percent in the previous month, reflecting both the policy tightening and improved food production, that contributed to a decline in food prices, in particular of meat and vegetables, which exceeded the expected seasonal deceleration of food prices. The exchange rate in the accounts-to-accounts market has remained stable since the beginning of the year. The spread between the official exchange rate and the accounts-to-accounts rate amounted to 7.6 percent in early November (compared to 23 percent at end-December 1996 and the program ceiling of 8 percent for end-1997). The real effective official exchange rate at end-October 1997 appreciated by 0.4 percent from December 1996 and the average real rate for the period January-October appreciated by 3 percent.

4. Fiscal performance through September was mixed. Despite a significant decline of revenue collections on account of low receipts from customs (reflecting a sharp drop in imports in August and September), weaker than expected performance of the revenue measures enacted in August,⁴ and administrative delays in transfers from some public enterprises, government borrowing from the Bank of Sudan (BOS) remained in line with the programmed ceiling. To maintain the deficit at the targeted level, the government curtailed primarily some of the discretionary new spending programs initiated in the supplementary budget in August, and continued to limit the operational budgets of ministries. Payments were made or committed only for about half of the new programs of development and nondevelopment expenditures under the supplementary budget.⁵ The remaining programs were either canceled or postponed pending better revenue performance. However, spending on key capital programs (emergency electricity repairs and national insecticide/pesticide) were preserved.

5. Monetary developments remain in line with program targets. Preliminary data indicate that bank credit to nongovernment sectors—in particular credit to finance trade—continued to be restrained below the programmed level in September. The slow growth of credit to nongovernment sectors reflected partly a fall of credit demand on account of the high real cost of borrowing⁶ and a slowing of credit supply as banks stepped up their efforts to recover loans and limit credit extensions in response to a tightening of banking supervision by the BOS,

⁴Most of the new revenue measures were based on taxing imports (see EBS/97/151, August 15, 1997) and were adversely affected by the decline in imports during August and September.

⁵For details of the new programs, see EBS/97/151, August 15, 1997.

⁶The real effective cost of borrowing under a typical Murabaha contract is estimated to have risen by the end of September to 20 to 40 percent from negative levels at the beginning of the year.

specifically the tightening of the banks' internal control procedures to deal with nonperforming loans and loan recovery, and the enforcement of a revised deadline of end-1997 for compliance with risk-weighted capital adequacy norm by all banks. The stock of the banking system's net domestic credit amounted to only LSd 930 billion as of end-September, or over 3 percent below the program target, notwithstanding a decline of central government deposits with the BOS by LSd 10 billion. Partly as a result of the sluggish growth of credit, banks' excess reserves continued to rise, and reserve money grew about 3 percentage points more than projected under the program. The growth of the broad money supply decelerated through September 1997 to 27 percent compared to 52 percent over the same period in 1996. Also, the reintermediation in the financial sector strengthened further, as reflected in the decline of the cash-deposit ratio from 107 percent in December 1996 to 91 percent in September on account of a sizeable increase of demand and investment deposits. The staff stressed the importance of taking measures—including a rapid introduction of market-based instrument of government funding (see paragraph 11)—to take control of the growing excess reserves before considering any moves to reduce the cost of borrowing in line with lower inflation.

6. Over the period December 1996 through September 1997, substantial inflows of foreign exchange (mostly on account of private remittances) occurred, partly reflecting the tight liquidity conditions. After increasing by about US\$60 million to US\$272 million in the first seven months, foreign currency deposits at commercial banks have remained roughly unchanged since July 1997. Net foreign assets of commercial banks increased by about US\$39 million from US\$176 million in December 1996 to US\$215 million. Net foreign assets of the BOS⁷ improved by US\$47 million since December 1996, and by about US\$13 million since June 1997, mainly on account of a decline in liabilities to the Fund.

7. Export performance continued to be affected by the deterioration in the international prices of key commodities (in particular of cotton). The value of exports in U.S. dollar terms during January–September 1997 declined by 9 percent compared to the same period in 1996, despite significantly higher export volumes. The value of imports through August also declined by almost 14 percent compared to the same period in 1996, reflecting mainly a sharp fall in food imports, and this helped to keep the trade deficit at about the programmed level.

8. The authorities are continuing to make significant progress toward adopting a General Sales Tax based on the value-added tax principle. The draft VAT law, which had been completed in early September 1997, and a timetable for the introduction of the VAT, was reviewed in detail in collaboration with a Fund technical assistance mission (an end-October benchmark). The authorities are now preparing a revised draft, and are considering a timetable for passing the law through the executive branch and submitting it to the national assembly by mid-1998. Simultaneously, the authorities have made further progress in the

⁷For program purposes, the NFA of the BOS are valued at the December 1996 U.S. dollar/SDR exchange rate and exclude nonresident foreign time liabilities.

administrative preparations for the newly established value added tax (VAT) department withing the Ministry of Finance. They also reviewed with Fund staff the structure of indirect taxes, and are considering a rationalization of the excise tax system, as well as the phasing out of export taxes, in order to facilitate a phased introduction of VAT in 1998.

9. The authorities also prepared a plan for tariff reform in collaboration with Fund technical assistance (an end-October benchmark). The plan includes proposals for a further reduction of the number of tariff bands from 7 to 5, a decrease in the maximum tariff rate from 250 percent to 50 percent, an increase in the minimum rate and a significant reduction in the number of exemptions. In addition, specific tariff reductions applicable to certain transactions and sectors of the economy are proposed to be phased out. In addition, the trade system, in particular the role of the export committees and the licensing and authorization process for exports, was reviewed by the government and a reform plan is being formulated, so as to create a regulatory framework conducive to the promotion of exports (an end-October benchmark).

10. The mission reviewed with the authorities the consolidated budget statement for federal, state and local governments and public enterprises that had been prepared at the end of September. The statement consolidates the data on the original budget estimates, since the information on the actual budget outcome still remains incomplete; it is therefore only indicative of the relative shares in revenue and expenditure of the different levels of government. State and local government revenue amount to about 55 percent of central government revenue and 35 percent of total revenue in the consolidated budget. The share of development expenditures in the state and local budgets was slightly higher than in the central government budget (32 versus 22 percent).

11. A proposal, for the introduction of new market-based instruments of government funding, based on IMF technical assistance in June 1997, was submitted to the High Shariaa Supervisory Council (HSSC) in September. In discussions with the High Shariaa Supervisory Council during the staff visit in October, Fund staff clarified several issues and questions raised by the HSSC, in particular concerning the proper determination of the rate of return of the proposed government funding instrument. The HSSC agreed to reconsider the staff proposal, and the staff will continue to work with the authorities during the next staff visit in late November on the appropriate design of the instrument.

12. The staff will undertake a comprehensive review and assessment of macroeconomic performance and structural reforms in 1997, in the context of the Article IV consultation discussions in November, and discussions in January 1998 on a staff-monitored program for 1998. Preliminary discussions on a 1998 program were initiated already in the October visit.

During the November visit, the staff will also assess the implications of the recent tightening of economic sanctions against Sudan by the United States (effective November 4, 1997) for the program and balance of payments prospects.⁸

⁸The new sanctions will freeze Sudan's financial assets in the United States, and prohibit U.S. trade and financial transactions with Sudan. The order allows the U.S. administration to grant exemptions on a case by case basis.

Table 1. Sudan: Quantitative Benchmarks, September 1997

(In billions of Sudanese pounds, except if indicated otherwise)

| | Cumulative Change 1/ | | | | | | |
|--|----------------------|-------|------|-------|------|-------|-------|
| | June | July | | Aug. | | Sept. | |
| | Act. | Prog. | Act. | Prog. | Act. | Prog. | Prel. |
| Benchmarks | | | | | | | |
| Ceiling on the net domestic credit of the banking system | 881 | 24 | 35 | 49 | 29 | 81 | 49 |
| Ceiling on net credit to government 2/ | 634 | 9 | 7 | 15 | 14 | 20 | 20 |
| Ceiling on new nonconcessional borrowing contracted or guaranteed by the government | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Floor on NFA of the Bank of Sudan (in millions of US\$) 3/ 4/ | -2,653 | 0 | 2 | 0 | 13 | 0 | 13 |
| Payments to the Fund (in millions of US\$) 5/ | 4.3 | 4.3 | 4.3 | 4.3 | 4.3 | 4.3 | 4.3 |
| Memorandum items | | | | | | | |
| Reserve money | 690 | 16 | 43 | 25 | 39 | 33 | 56 |
| Central government revenue | 480 | 101 | 92 | 210 | 194 | 334 | 282 |

Sources : Bank of Sudan; and staff estimates.

1/ Outstanding stocks in June 1997; cumulative since June 30, 1997.

2/ Excluding changes in government deposits with the Bank of Sudan.

3/ Liabilities to the Fund are valued at the constant end-December 1996 US\$/SDR exchange rate.

4/ NFA data were revised, so as to exclude nonresident foreign time liabilities.

5/ Monthly flows.

Table 2. Sudan: Status of End-October Structural Benchmarks

| Benchmarks | Implementation |
|---|---|
| October payment to the Fund of US\$4.3 million. | US\$5.0 million received on October 16, 1997, of which US\$0.7 million to stabilize Sudan's arrears to the Fund in SDR terms. |
| Adjustment in domestic petroleum prices to eliminate any remaining subsidization and ensure the budgeted contribution. | Domestic petroleum prices remain higher than international prices. Price of gasoil raised by 11 percent in September 1997, and of Kerosene by 9 percent in October. |
| Finalizing the draft VAT law at the federal level, and propose a time table for passing the law through the executive branch and submission to the National Assembly with a view to begin a phased implementation of the VAT during 1998. Further rationalization of the tax system toward the eventual adoption of VAT will be considered in the context of the 1998 budget. | VAT law and timetable for introduction reviewed in collaboration with FAD technical assistance. Proposals toward the rationalization of the indirect tax system identified (para. 8). |
| Finalize the plan for tariff reform in coordination with the introduction of the VAT. | Plan has been formulated in collaboration with FAD technical assistance. (para. 9). |
| Undertake comprehensive review of the trade system with the view to establishing time-bound plan to rationalize the trade regime and simplify administrative procedures governing foreign trade. | Trade system was reviewed and a reform plan is being formulated (para. 9). |
| Statistical reporting. | Observed. |

Table 3. Sudan: Selected Economic and Financial Indicators, 1995-97 1/

| | 1995 | 1996 | 1997 | | | | |
|--|-------|-------|-----------------------|--------------|--------------|---------------|---------------|
| | | | Staff Mon. Prog. 2 | July Act. | Aug. Act. | Sept. Act. | Oct. Prel. |
| (Annual changes in percent) | | | | | | | |
| National income, prices and exchange rate | | | | | | | |
| Real GDP (at factor cost) | 4.4 | 4.7 | 5.5 | ... | ... | ... | ... |
| Consumer prices (month on year ago month) | 71 | 114 | 55 | 37 | 32 | 27 | 19 |
| Consumer prices (period average) | 68 | 133 | 53 | ... | ... | ... | ... |
| Official exchange rate end of period (LSd/US\$) | 838 | 1,460 | ... | 1,615 | 1,635 | 1,655 | 1,660 |
| Real effective exchange rate | | | | | | | |
| (period average: depreciation -) | -22.9 | -0.4 | ... | 2.5 3/ | 3.2 3/ | 3.3 3/ | 3.0 3/ |
| (end period: depreciation -) | -24.2 | 14.5 | ... | 3.8 3/ | 8.3 3/ | 4.1 3/ | 0.4 3/ |
| Central government operations 4/ | | | | | | | |
| Total revenue | 75.5 | 72.3 | 85.2 | 49.1 5/ | 57.9 5/ | ... | ... |
| Total expenditure (including interest arrears) | 95.7 | 171.6 | 8.0 | ... | ... | ... | ... |
| Expenditure (excluding interest arrears) | 87.7 | 94.6 | 34.2 | 50.3 5/ | 58.8 5/ | ... | ... |
| External sector | | | | | | | |
| Exports, f.o.b. | 31.8 | 11.6 | -2.3 | -6.2 6/ | -3.1 6/ | -9.4 6/ | ... |
| Imports, c.i.f. | 19.1 | 26.9 | -4.2 | 0.0 6/ | -13.8 6/ | ... | ... |
| (In percent of GDP) | | | | | | | |
| Central government operations | | | | | | | |
| Total revenue | 8.7 | 6.2 | 7.0 | ... | ... | ... | ... |
| Total expenditure (including interest arrears) | 24.0 | 26.7 | 17.6 | ... | ... | ... | ... |
| Expenditure excluding interest arrears | 12.1 | 9.6 | 7.8 | ... | ... | ... | ... |
| Overall balance (on an accrual basis) | -15.3 | -20.5 | -10.6 | ... | ... | ... | ... |
| Overall balance (on a cash basis) | -3.2 | -3.4 | -0.9 | ... | ... | ... | ... |
| Primary balance | -2.3 | -2.4 | -0.2 | ... | ... | ... | ... |
| Balance of payments and external debt | | | | | | | |
| Current account deficit | | -25.0 | -23.1 | ... | ... | ... | ... |
| Exports, f.o.b. | 7.8 | 8.1 | 7.5 | ... | ... | ... | ... |
| Imports, c.i.f. | 17.2 | 20.2 | 18.2 | ... | ... | ... | ... |
| External debt | 272.0 | 267.5 | 262.6 | ... | ... | ... | ... |
| External interest due | 12.9 | 13.5 | 13.3 | ... | ... | ... | ... |
| External debt paid 7/ | 1.0 | 0.7 | 0.8 | ... | ... | ... | ... |

Table 3. Sudan: Selected Economic and Financial Indicators, 1995-97 1/

| | 1995 | 1996 | 1997 | | | | |
|--|--------|--------|-----------------------|--------------|--------------|---------------|---------------|
| | | | Staff Mon. Prog. 2 | July Act. | Aug. Act. | Sept. Act. | Oct. Prel. |
| (Changes as percent of beginning stock of broad money) | | | | | | | |
| Money and credit | | | | | | | |
| Net foreign assets | -462.9 | -267.3 | -161.2 | -30.4 | -31.8 | -39.0 | ... |
| Net domestic assets | 137.7 | 56.1 | 14.6 | 10.6 | 10.2 | 13.8 | ... |
| Net domestic credit | 46.4 | 59.3 | 14.5 | 8.5 | 8.0 | 9.6 | ... |
| Net credit to the central government | 31.2 | 31.7 | 4.8 | 4.3 | 4.2 | 5.6 | ... |
| Claims on nongovernment sector | 15.2 | 27.5 | 9.7 | 4.1 | 3.8 | 3.9 | ... |
| Other items (net) | 91.3 | -4.7 | 0.0 | 2.1 | 2.2 | 4.2 | ... |
| Counterpart to valuation changes | 472.4 | 281.1 | 182.7 | 40.6 | 45.4 | 52.3 | ... |
| Money and quasi-money | 147.2 | 65.2 | 36.1 | 20.8 | 23.8 | 27.1 | ... |
| Reserve money | 76.7 | 81.8 | 15.0 | 12.9 3/ | 12.3 3/ | 14.9 3/ | ... |
| Velocity (GDP/average M2) | 7.5 | 10.6 | 12.1 | ... | ... | ... | ... |
| (As percent of total current account receipts unless otherwise indicated) | | | | | | | |
| Total external debt service | | | | | | | |
| Commitment basis | 160.6 | 185.5 | 181.1 | ... | ... | ... | ... |
| Actual payments 7/ | 9.7 | 8.0 | 8.5 | ... | ... | ... | ... |
| Memorandum item: | | | | | | | |
| Nominal GDP (annual; in billions of Sudanese pounds) | 4,179 | 10,203 | 16,700 | ... | ... | ... | ... |

Sources: Fund staff estimates and projections based on information provided by the Sudanese authorities.

1/ Starting in 1996, all official accounts moved from a fiscal year (July-June) to a calendar year basis.

2/ EBS/97/151.

3/ Cumulative percent change during 1997.

4/ Revenue and expenditure data for 1996 and 1997 exclude taxes collected on behalf of and transferred to the States.

5/ Cumulative percent change during 1997 relative to program target.

6/ Percent change during 1997 over the same period in 1996.

7/ Including payments of arrears to the Fund and burden sharing refunds.

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