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0404

INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 87/92

10:00 a.m., June 19, 1987

R. D. Erb, Acting Chairman

Executive Directors	Alternate Executive Directors
	J. M. Jones, Temporary
	Song G., Temporary
	M. Lundsager, Temporary
	H. S. Binay, Temporary
	M. Hepp, Temporary
	M. B. Chatah, Temporary
	A. Bertuch-Samuels, Temporary
	A. Iljas, Temporary
	J. Hospedales
	D. A. Woodward, Temporary
	M. A. Khylberg, Temporary
	G. D. Hodgson, Temporary
Mawakani Samba	
	I. A. Al-Assaf
	C. Noriega, Temporary
H. Ploix	
G. A. Posthumus	
C. R. Rye	
	O. Kabbaj
	L. E. N. Fernando
	T. Morita, Temporary
S. Zecchini	

J. W. Lang, Jr., Acting Secretary
B. J. Owen, Assistant

Also Present

IBRD: B. Varon, Western Africa Regional Office; S. Voyadzis, Latin America and the Caribbean Regional Office. African Department: A. D. Ouattara, Counsellor and Director; L. M. Goreux, Deputy Director; E. L. Bornemann, J. Harnack, T. P. McLoughlin. Exchange and Trade Relations Department: S. Kanesa-Thasan. Legal Department: H. Elizalde, J. V. Surr. Treasurer's Department: D. Berthet, J. E. Blalock, J. C. Corr. Western Hemisphere Department: M. Caiola, J. Ferrán, T. Gudac, C. G. Muñiz B., T. M. Reichmann. Advisors to Executive Directors: L. P. Ebrill, J.-C. Obame, K. Yao. Assistants to Executive Directors: A. R. Al-Abdullatif, O. Isleifsson, S. King, R. Manfredi Selvaggi, D. V. Nhien, L. M. Piantini, D. Saha.

1. GUYANA - OVERDUE FINANCIAL OBLIGATIONS - REVIEW FOLLOWING DECLARATION OF INELIGIBILITY; AND NOTICE OF FAILURE TO SETTLE TRUST FUND OBLIGATIONS

The Executive Directors considered a staff paper on the further review of Guyana's overdue financial obligations following the declaration of Guyana's ineligibility to use the general resources of the Fund on May 15, 1985, together with a notice of Guyana's failure to settle obligations to the Trust Fund (EBS/87/131, 6/15/87; and EBS/87/120, 6/1/87).

Mr. Hospedales said that economic conditions in Guyana remained difficult, indeed critical, and the liquidity situation was precarious. As an illustration, Guyana's total overdue financial obligations to the Fund of SDR 59.9 million were more than 1,000 percent of its gross international reserves. Notwithstanding, since the previous review in December 1986, Guyana had made payments to the Fund totaling SDR 1.6 million and would continue to make payments, with some commencing in the fourth quarter of 1987. The authorities were firmly committed to meeting those overdue obligations and maintaining normal relations with the Fund.

His Guyanese authorities had asked him to assure the Executive Board that they were determined to press ahead with the implementation of a strong and comprehensive economic adjustment program, Mr. Hospedales stated. In that respect, they valued highly the advice they had been receiving from the staffs of the World Bank and the Fund. While they believed that sustained implementation of a strong growth-oriented program must be supported by external concessionary resources, they saw significant benefits from an early start to the process. To that end, a number of initial measures had been put in place in early January--a substantial devaluation of the Guyanese dollar, the establishment of a foreign exchange window at commercial banks that would permit a market-related rate, and adjustment of a number of important prices, including petroleum and rice prices. Later on, in April, additional measures had been taken--in the main, increases in utility and transportation rates and certain controlled prices, cuts in expenditure plans of the public corporations, and liberalization of the regulations for the foreign exchange window.

In the view of the authorities, that approach to adjustment could provide a basis for an arrangement with the Fund under the structural adjustment facility once Guyana had become current in its financial obligations, Mr. Hospedales commented. Pursuant to that end, the authorities had been formulating the medium-term objectives and policies for a policy framework paper. They expected to complete that formulation shortly and the draft would be reviewed by the staffs of the World Bank and the Fund. His authorities in Guyana were hopeful that that process of discussions and negotiations could be speeded up so that Guyana could restore normal debtor/creditor relations with the international financial community, including the Fund, and culminating in a package of financial assistance to ensure that the adjustment efforts were supported and sustained.

Mrs. Hepp said that she regretted that Guyana had not been able to make further payments of its overdue obligations to the Fund. She could go along with the proposed decisions, but noted the authorities' intention to undertake the measures needed to redress the country's severe economic difficulties, as discussed with the staff and with the World Bank in recent months. The measures implemented in January and April 1987 were welcome first steps in the right direction toward a more comprehensive economic package. She urged the authorities to continue along those lines, preparing and formulating the needed medium-term program that could provide a basis for an arrangement under the structural adjustment facility once the overdue obligations to the Fund had been fully settled. She looked forward to the next review of Guyana's financial situation and to hearing about further developments in the direction she had outlined.

Mr. Noriega remarked that the continued difficulties standing in the way of setting Guyana's economy on a recovery path and of the settlement of overdue financial obligations were of great concern to his chair. Therefore, although he had noted the authorities' intentions to clear their arrears, and in particular, the proposal to settle the overdue obligations to the Trust Fund in the last quarter of 1987, he urged them to attach top priority to their relations with the Fund. He recalled that on the occasion of the previous review, the Fund had called on the authorities to move toward a more liberalized system of relative prices, including the exchange rate. It must be acknowledged that several measures aimed in that direction had been adopted, and that the authorities had maintained close contacts with the staff, as Mr. Hospedales had confirmed. Those contacts were greatly to be encouraged. Prompt completion and announcement of a comprehensive economic program should facilitate the task of attracting foreign resources. The fact that the total overdue obligations to the Fund represented a substantial amount in relation to the value of Guyana's external trade was precisely one of the reasons why the economic program being formulated should be geared toward overcoming the structural imbalances in the productive system and the public sector. He endorsed the proposed decisions and exhorted the authorities to address those fundamental economic issues.

Mr. Hodgson asked the staff whether it had any additional details on the multilateral and bilateral lenders and donors that had been mentioned on page 3 of EBS/87/131 as being expected to arrange a package of financial assistance with Guyana.

The staff representative from the Western Hemisphere Department responded that the sizable amount of external assistance that would be required to support an economic program for Guyana would need to take the form first, of a rescheduling of those arrears that could be rescheduled; second, a rescheduling of some payments of principal and interest that would fall due during the program period; and third, new money in an amount that was likely to be sizable. As for specific sources of financing, the staff understood that the Guyanese authorities had been approaching some of the major donors and creditors. In the context of the latest meeting of the Caribbean group in January 1987, the staffs of the Fund and the World Bank had indicated to donors and creditors the type of measures that Guyana had taken and the sort of program envisaged. However, at that time, no specific commitments had been made by any donor or creditor of the amount of relief that could be forthcoming, although all had welcomed the measures. The intention of the staff was to approach creditors and donors again, in coordination with the World Bank staff, once a policy framework paper had been discussed with the authorities. One of the problems that had to be faced was that creditors and donors had been unwilling in the past, and rightly so, to indicate any commitment to Guyana, while at the same time the authorities had been reluctant to enter into a program that was not adequately financed. The hope of the staff was that some progress could be made once a policy framework paper had been drawn up.

Mr. Hodgson commented that the staff representative had outlined the correct sequence of developments if Guyana's economic problems were to be resolved successfully. Those problems had been so difficult for so long that it had been very hard for any donor or creditor to make an advance commitment in the absence of a complete set of comprehensive adjustment measures. Therefore, his chair reiterated the position that it had taken in the past by urging the authorities to prepare a package of measures under a policy framework paper before expecting any donor assistance to be mobilized. He supported the proposed decisions.

Ms. Lundsager said that she fully endorsed the comments by Mr. Hodgson. Since the Board's previous review of Guyana's overdue obligations, the authorities had paid some charges in SDRs and some overdue Trust Fund obligations totaling SDR 1.6 million. While those payments gave some indication that the authorities were concerned about their overdue obligations, the payments offered little reason to believe that full clearance of arrears could be expected any time soon. That situation was clearly disappointing, as the matter had been under review for several years. On many occasions, the Executive Board had urged the authorities to implement a comprehensive economic adjustment program that would begin to bring economic activity out of the parallel market and back into official channels. Only if they succeeded in doing so would the official foreign exchange market recover and the fiscal situation improve. One year previously, Mr. Greenidge had attended the Board meeting and outlined some policy measures taken by his Government. The indications were that Fund and Bank teams would visit Guyana to help the authorities formulate an economic reform program that could be presented to donors and creditors. At the Board meeting in December 1986, little progress in that area could be reported. In fact, while some policy measures had been taken, strong actions to restore the appropriate structure of relative prices had not occurred and, as a result, there were few signs of the underground economy disappearing. The brief staff paper before the Board at the present meeting showed that recorded economic activity had remained stagnant in 1986, and that while the fiscal deficit had decreased, it still consumed about half of recorded GDP. Under such conditions, it was hard to imagine that private sector confidence could be easily restored.

What was clearly needed was a strong and decisively implemented adjustment program that restored appropriate incentives, Ms. Lundsager observed. Some recent exchange rate actions had narrowed the discount of the currency on the parallel market. Nonetheless, it appeared that liberalization of the trade and exchange system in the context of a market-determined exchange rate would be needed to diminish the extent of the parallel economy. Decontrol of domestic prices and restrained financial policies would also have to be supportive of such efforts.

The Fund and the Bank had been providing technical assistance to Guyana, and the authorities were currently looking to external creditors and donors to help provide financing to clear arrears, Ms. Lundsager noted. However, at the present stage, with the long history of weak performance, she thought that creditors and donors would only be interested in supporting a fully articulated adjustment program that was already being forcefully implemented. Indeed, one year previously, her chair had hoped that Guyana would be at that stage by the fall of 1986. Any further delays would not make it any easier to solve the problem, and she strongly urged the authorities to implement fully all the necessary measures being recommended by the Fund and Bank so that creditors and donors could be approached for assistance. Until the authorities did so, she did not believe that donors and creditors would provide firm indications of financial support. Finally, she supported the proposed decisions, in the hope that it would be the last time that the Board had to consider the matter.

Mr. Fernando said that he had noticed from the staff paper that Guyana's arrears to the Fund represented 8 percent of total arrears. The payments made to the Fund had certainly been much less than was required. His question was whether any other payments had been made to either official or other creditors and if so in what proportion of the total outstanding.

Mr. Zecchini said that he fully shared the views of Mr. Hodgson and Ms. Lundsager. In order to stress the relationship between the adjustment program that was required and the likelihood of forthcoming support by creditor and donor countries, he proposed that paragraph 3 of the draft decision be amended to state that without the formulation and implementation as a matter of urgency of a strong and comprehensive adjustment program, the external financing that was required to clear the arrears would not be forthcoming.

Mr. Bertuch-Samuels said that he too supported the comments made by Mr. Hodgson and Ms. Lundsager. The partial payments made by Guyana, the reaffirmation by Mr. Hospedales of the authorities' commitment to settle in full their overdue obligations to the Fund, and the recent steps mentioned by him as having been taken were welcome. But it appeared from the staff paper that the measures taken so far were insufficient to overcome the serious imbalances in the economy. Therefore, he encouraged the authorities to make further rapid progress in the direction indicated by Mr. Hospedales, namely, to agree with the staff on a medium-term policy framework, and then to start right away to implement a strong program that would convince donors and creditors to lend their financial support.

Mr. Woodward said that he welcomed the payments made by the authorities to the Fund since the previous review, although he noted that they had been limited in relation to the total amount of outstanding arrears. He fully recognized the very difficult economic situation faced by the authorities and thus the very real constraints on the rate at which they could settle their overdue obligations to the Fund. The situation had arisen partly because of adverse external circumstances, but also to a great extent because of the inappropriate policies pursued by the authorities in response to those circumstances. He therefore greatly welcomed the substantial progress made in recent months toward improving the macroeconomic policy stance. There was still quite a long way to go but a major first step had been taken. He also welcomed the authorities' intention to formulate, with the Fund and Bank staff, the basis for a policy framework paper with a view to ultimate use of Fund resources under the structural adjustment facility.

Finally, Mr. Woodward reiterated that Guyana's continuing large-scale arrears to the Fund remained a matter of the greatest concern to the Board. Those arrears represented a serious obstacle that would need to be overcome if Guyana were once again to benefit from the use of Fund resources. He supported the proposed decisions.

The staff representative from the Western Hemisphere Department said that a specific breakdown of arrears and payments to each multilateral institution was not available. In broad terms, the increase in arrears of principal and interest to multilateral agencies had been of the order of $20 million in 1986, whereas the amounts actually paid were of the order of $10 million.

Mr. Hospedales observed that in establishing priorities with respect to payments to multilateral financial institutions, Guyana was obviously faced with the difficulty of allocating among creditors an amount that was too small to go around. They had been forced, therefore, to operate on the basis of trying to protect existing critical flows, the further interruption of which would involve a considerable reduction in their capacity to service their existing needs as well as future debts.

He wished to thank Executive Directors for their generally supportive comments that he would transmit to his authorities in Guyana, Mr. Hospedales concluded. It was clear that events were moving in the right direction. The authorities had made a commitment to wide-ranging structural reform, and political support for the program was being forged. He hoped that the formulation of a well-designed, comprehensive framework of adjustment, fully backed by the international financial community, could be speeded up and put in place so that the growth process could be resumed in Guyana.

He could go along with the suggestion by Mr. Zecchini for amending paragraph 3 of the proposed decision, Mr. Hospedales concluded.

The staff representative from the Treasurer's Department said that Mr. Zecchini's suggestion could be implemented by adding to paragraph 3 as drafted the clause "which is needed to attract external financial support."

The Executive Board then took the following decisions:

Review Following Declaration of Ineligibility

1. The Fund has reviewed further the matter of Guyana's continuing failure to fulfill its financial obligations to the Fund in light of the facts and developments described in EBS/87/131 (6/15/87).

2. The Fund deeply regrets the continuing failure by Guyana to fulfill its financial obligations to the Fund and again urges Guyana to make full and prompt settlement of those obligations.

3. The Fund welcomes the recent measures adopted by Guyana and again stresses the need for Guyana to formulate and implement as a matter of urgency a strong and comprehensive economic adjustment program, which is needed to attract external financial support.

4. The Fund will review again the matter of Guyana's overdue financial obligations to the Fund at the time of the 1987 Article IV consultation with Guyana or within six months of the date of this decision, whichever is earlier.

Decision No. 8625-(87/92), adopted
June 19, 1987

Notice of Failure to Settle Trust Fund Obligations

1. On June 1, 1987, the Managing Director issued a notice to the Executive Board (EBS/87/120) setting out the basis on which it appeared to him at that time that Guyana was not fulfilling its obligations under Decision No. 5069-(76/72) with regard to the Trust Fund to repay a disbursement under its Trust Fund loans in the amount of SDR 985,552, and pursuant to Decision No. 8165-(85/189) G/TR to pay special charges of SDR 2,499 on overdue Trust Fund obligations.

2. Having considered the notice of the Managing Director, and the views of Guyana, the Fund finds that Guyana has failed to fulfill its obligations under the Trust Fund as stated in paragraph 1 above.

3. The Fund regrets the nonobservance by Guyana of its obligations relating to the Trust Fund and urges Guyana to resume their observance forthwith. The Fund decides that, if Guyana would become otherwise eligible to make use of the general resources of the Fund, the Fund would take into account the existence of any overdue obligations to the Trust Fund in considering any request by Guyana for the use of the general resources of the Fund.

Decision No. 8626-(87/92) TR, adopted
June 19, 1987

2. CHAD - 1987 ARTICLE IV CONSULTATION AND STRUCTURAL ADJUSTMENT FACILITY - POLICY FRAMEWORK PAPER

The Executive Directors considered the staff report for the 1987 Article IV consultation with Chad and the policy framework paper under the structural adjustment facility (EBS/87/98, 5/8/87). They also had before them a background paper on recent economic developments in Chad (SM/87/122, 5/28/87), and a statement by the Managing Director relating to the policy framework paper, which read as follows:

> There follows for the information of Executive Directors the text of a memorandum that I have received from the President of the World Bank to serve as the basis for my statement on the matter to the Board. This text summarizes the main points covered by the Executive Directors of the Bank and IDA in their June 2, 1987 discussion in Committee of the Whole of a paper entitled "Chad: Policy Framework Paper, 1987-89."
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> 1. The Directors commended the realistic, pragmatic and cautious approach adopted. The absence of basic data was noted, and concern was expressed that the many studies identified in the paper should be executed rapidly.
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> 2. The Directors noted the narrow productive base of Chad and emphasized that the Bank should support all possible diversification measures.
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> 3. It was also noted that since Chad has not introduced many of the regulations and restrictions that constrain economic activities in other countries, the program was much more a reconstruction program for a war-devastated country rather than an economic restructuring program. This was deemed appropriate.
>
> 4. Chad will need massive external assistance on grant or very concessional terms. Aid coordination to secure such aid flows must be vigorously pursued. The environment encouraged private sector and NGO activity, which will be helpful in the new stability brought by improved security.

5. Some speakers commented on the absence of detailed discussion of the monetary and exchange rate issues. Although the membership of Chad in the Central African Monetary Union was noted, it was felt that more discussion of these issues would have been welcome.

6. The determination of the Chadian Government to undertake a comprehensive restructuring program in the face of tremendous difficulties was warmly received. The collaboration of the IMF, the Bank and the Government to produce this policy framework paper was commended.

Mr. Mawakani made the following statement:

The economic and financial situation of Chad remained difficult in 1986. Real GDP is estimated to have declined while the internal and external disequilibria widened. My authorities are concerned about the deterioration in Chad's economic and financial situation and are determined to address the financial and structural difficulties facing their country and to pursue their ongoing efforts to diversify the economy.

Developments in 1986/87

In the real sector, performance was adversely affected by a decline in foodcrop production and in manufacturing output. Foodcrop production decreased by about 2 percent in 1986/87 owing to irregular rainfall in some parts of the country. Cotton output also declined but only marginally. However, livestock production increased slightly but its level remained below potential. Activity in the manufacturing sector which contributes about 20 percent to GDP, registered a slight decline in output reflecting partly the difficulties encountered by COTONTCHAD, one of the most important enterprises operating in this sector. On the whole, as a reflection of the depressed activities in the production sector, real GDP is estimated to have decreased by 2.3 percent in 1986 compared to an increase of 29 percent in 1985.

In the fiscal sector, the financial position of the Central Government deteriorated sharply. The overall government deficit (on a commitment basis) increased from about 10 percent of GDP in 1985 to about 19 percent in 1986. This unfavorable outcome reflects a sharp decline in budgetary revenue and a substantial increase in capital expenditure. The shortfall in revenue was mainly due to the suspension of taxes on cotton exports and could not be offset by new taxes and higher taxes on beer and cigarettes introduced in late 1986.

Developments in the monetary sector reflected to a large extent the difficulties in the cotton sector and those associated with the financing requirements of COTONTCHAD. As indicated by the staff, the sharp increase in domestic credit in recent years should be considered against the background of the severe crisis in the cotton sector. This has drastically reduced the ability of COTONTCHAD to repay crop credits and has led to a substantial decline in budgetary revenue, thus leading to an increase in net claims of the banking system on the Government. The authorities are of the view that without a significant improvement in the export price of cotton to more remunerative levels, the crisis in the cotton sector will persist and the banking system in Chad will continue to face severe financial difficulties. In the meantime, the fact that the BEAC agreed in late 1986 to reschedule the entire amount of arrears of COTONTCHAD to the domestic banking system, over a ten-year period, will give some relief to the banking system.

Economic prospects and medium-term policies

On the basis of the recent economic and financial developments described above and in light of the staff medium-term scenario presented in Table 6 of EBS/87/98, there is no doubt that the economic prospects of Chad are difficult and are likely to remain so in the medium term. These prospects underscore the need for undertaking a comprehensive adjustment program which could address the financial difficulties and the structural problems facing the country.

The main objectives of the medium-term program and the policies the authorities intend to implement thereafter are well described in the policy framework paper. The program aims at achieving two broad objectives: one is to achieve an annual rate of economic growth of 2 percent in a noninflationary environment; the other is to attain viability in the external accounts. The strategy for attaining these objectives is based on measures aimed at strengthening the financial performance of the cotton sector, which remains the driving force of the Chadian economy, and at diversifying the productive base. In this respect, the Government will continue the rehabilitation program launched in 1985. Most of the measures under it have already been implemented and a timetable has been established for implementing the remaining measures.

Regarding the diversification of the economy's productive base, the Chadian authorities intend to concentrate their efforts on the agricultural sector, particularly foodcrop production. To this end, they have launched a comprehensive study focusing on the role of irrigation and improvement of incentives for private sector involvement in cereal marketing. The livestock subsector, which is also an important contributor to GDP, will continue to be promoted.

In the manufacturing sector, the Government's objective is to encourage small and medium-sized enterprises. To this end, the investment code is being reviewed, with a view to providing incentives for the creation of such enterprises. Efforts will be made toward the preparation and the implementation of a realistic investment program with the assistance of the World Bank.

The demand-management policies to be implemented in the context of the medium-term program will be aimed at strengthening the position of public finances through revenue-increasing and expenditure-containing measures. On the revenue side, the authorities will pursue their efforts to increase revenue by improving collection of existing taxes, and to this end, tax administration will be strengthened. In addition, the current review of the structure and the level of petroleum taxation is expected to increase revenue from petroleum products. On the expenditure side, the authorities will pursue an austerity policy with emphasis on containing current expenditure. All in all, they intend to maintain the deficit of the Central Government's financial operations at about 2.4 percent of GDP during the program period.

Regarding the banking system, the authorities are aware of the need to improve the liquidity position of commercial banks in order to achieve the growth objective of the program. In that regard, Fund assistance is being requested to undertake a study on the implications of ending the moratorium under which all deposits with the commercial banks were frozen. Meanwhile, credit to the private sectors will be strictly controlled with priority given to the productive sector of the economy.

In sum, the authorities of Chad are aware that the country is facing a very difficult economic and financial situation. However, it should be recognized that, over the past few years, they have shown their resolve to address these difficulties by implementing corrective and reform measures in a severe economic and political environment. Given the magnitude of the task that the authorities have to accomplish, they hope that the international financial community will provide their country with timely and sufficient assistance in order to support their ongoing efforts.

Mrs. Ploix made the following statement:

Because Chad has neither an overdeveloped public sector, nor an oversized public investment program, nor a huge wage bill, as the staff clearly states, Chad needs more of a reconstruction program than an adjustment program. Chad needs to follow macroeconomic and sectoral strategies that will reconstruct its administration and infrastructure and place its economy on the path of sustainable growth.

In accomplishing such a task, the policy framework paper is helpful; it sets out certain pitfalls to Chad's future development, and pinpoints priority sectors for the allocation of scarce human and financial resources and I can endorse most of its objectives, particularly the following:

First, the continuation of the Government's liberal economic policy. In this regard, we welcome the authorities' intention to review the role of several institutions in order to rely as much as possible on private initiative. These institutions are the National Cereals Office, SOTERA (the livestock enterprise), the Petroleum Products Intervention Fund, and the Sugar Price Stabilization Fund.

Second, the strengthening of the budget should be a priority, especially on the revenue side. Revenue collection could be improved through a more efficient administration, the reduction of exemptions, and, finally, through fiscal reforms aimed at regulating imports that currently manage to evade official channels. On the expenditure side, there is much less room for maneuver since, as mentioned in the staff report, the current level of expenditures is insufficient to ensure the proper functioning of the administration. Given the national reconciliation policy being pursued, the authorities will face strong pressures in the months to come--pressures to increase civil servants' wages and to hire additional civil servants. In this context, the authorities' intention to limit new hirings and to freeze real wages is very welcome and should be pursued consistently.

Third, I can also go along with the preparation of a plan aimed at improving efficiency in the parapublic sector. Among the various issues, the central and most immediate one is the restoration of the profitability of the cotton sector. The difficulties of this sector are often presented somewhat inadequately and in a way that could lead one to the conclusion that a substantial reduction of cotton output or an additional reduction in producer prices would solve the problem. Indeed, it might solve the cotton sector problem but it would also create additional problems for Chad, since any slowing down of cotton production--an activity which accounts for 50 percent of export earnings, 25 percent of the added value of the manufacturing sector, and the bulk of monetized income--would inevitably be translated into a slowing down of the whole Chadian economy.

Since there is no visible substitute to activity in this sector in the medium term, its protection is clearly vital for Chad. During the last twelve months many steps have been taken in this direction and substantial results have been obtained--production costs have been cut by more than 20 percent; returns to the producer have been reduced by about one third and are anticipated to decline further next year as producers gradually take on the total cost of fertilizers. Moreover, a comprehensive program of action supported by the World Bank, the European Communities, the Netherlands, and France has been implemented recently; its objective is to restore profitability by the 1990/91 crop season. These factors demonstrate that, with the support of the donor community, Chad can solve this very difficult problem.

In conclusion, I would like to comment on the Fund's contribution to Chad's recovery process. I must say that the Fund started out well by playing a useful role in bringing the World Bank to resume its operations in this country, but I have the impression that the Fund is now lagging behind. Although the Chadian authorities have implemented most of the Fund's recommendations, negotiations have been under way for more than a year, and the two-stage approach to a structural adjustment arrangement is causing even more delays. The World Bank is contributing aid to Chad; now it is up to the Fund to make its financial contribution in the form of an arrangement under that facility--the sooner the better. I would be interested to hear what the Fund is planning in this regard.

Ms. Lundsager made the following statement:

The Chadian authorities have faced a number of severe difficulties: an earlier drought, the more recent decline in cotton prices, and the security situation caused severe physical dislocation and financial disorder. Despite these seemingly overwhelming problems, the authorities are working with bilateral donors and the international institutions to formulate a cohesive response to these imbalances. The policy framework paper serves the very important functions of delineating the areas that need work and laying out the initial policy steps. We welcome in particular the emphasis on the cotton sector and hope to see strong actions on several fronts continued under the planned structural adjustment arrangement. In that regard, we welcome the opportunity to discuss the relevant issues today.

The process of rehabilitation of the economy will be lengthy, and the cotton sector is the key. What is unusual in this case is that real returns to cotton producers are being eroded, as producer prices are not being adjusted and input subsidies are being phased out. This strikes us as a particularly painful way of promoting agricultural sector diversification out of cotton. The references in the staff paper to the limitations of the exchange rate system remind us that exchange rate adjustment would normally be a central policy tool in a country facing such a critical need to promote a strong supply response, particularly diversification. While we recognize the very important benefits arising from membership in the monetary area, we wonder whether the time has not come for the member countries to consider this issue.

This issue also assumes more importance in the case of Chad because of the limited scope for containing the fiscal situation, given the diminished tax base now that receipts from the cotton sector have diminished. We recognize that stronger budgetary actions are being taken, that firmer controls over expenditures are being exercised, and that prospects for containing military expenditures are now greatly improved. We welcome the plans to engage in a civil service reform that could eventually permit higher salaries to a smaller pool of civil servants. In that regard, we would have preferred that, instead of guaranteeing government employment to returning Chadians, the Government perhaps engage an external donor in providing seed monies for new private sector activity. Mr. Mawakani has mentioned a new investment code, which could be supportive of just such a program.

Despite these measures to contain spending, efforts are required to broaden the tax base, and for the time being, there may be a need to rely on some critical excise taxes, for instance, on petroleum. We would hope to see clear actions to improve collections as part of a structural adjustment arrangement. It is important that progress also be made on reducing exemptions and exonerations. Such measures are planned, although the policy framework paper is not clear on the pace of such actions.

Finally, the formulation of the first investment budget in years is welcome, and the willingness of donors to provide full financing of their projects, freeing the Government of the need to generate counterpart funds, is an indication of donors' strong commitment to assist in the restructuring of the Chadian economy.

The audits of the public enterprises are also appropriate, and we note that by next June, an examination of the role of some of the public entities will be initiated. These other entities, particularly those engaged in manufacturing and other services, could be considered for divestment, in an effort to improve efficiency and reduce the overall fiscal burden.

For such a program to be effective, a more efficient credit allocation system needs to be instituted. In particular, we hope that adequate credit to the private sector could be forthcoming, in order to support the desired diversification. In that regard, the policy framework paper provided only limited information on the future plans for rehabilitation of the banking system, which is still subject to a moratorium. The staff report, however, did indicate some steps planned in this area. We urge that action begin under a structural adjustment arrangement so that confidence could be restored in the banking system and financial savings could be encouraged.

In sum, a good beginning is being made in addressing the rather wide scope of economic problems in Chad. Our major concern is that this rehabilitation effort will be slow, given the limited range of policy tools that can be used to promote economic growth and diversification. Finally, we hope that implementation of the measures under the structural adjustment arrangement would lead to the attainment of a viable balance of payments position in the medium term.

Mr. Bertuch-Samuels said that he was in broad agreement with the thrust of the staff appraisal. He also shared many of Ms. Lundsager's views. Following the civil war in 1982, the Chadian authorities had made commendable progress in restoring normalcy to economic and political life. Unfortunately, extremely adverse external circumstances had complicated the process and a military conflict continued to limit the Government's room for economic maneuver. He shared the view of Directors of the World Bank that with these constraints in mind, it was appropriate for the authorities to adopt a realistic, pragmatic, but cautious approach.

With the main focus on reconstruction and financial rehabilitation, however, it had to be recognized that economic growth over the medium term would fall short of what would be desirable, Mr. Bertuch-Samuels went on. While the authorities seemed to be fully aware of the need to diversify the productive base in order to reduce the overwhelming dependence on the cotton sector and create the foundation for a more broadly based recovery of output and exports, it was equally clear from the outline of policies and structural reform measures that tangible results in that area could be expected to show up only several years ahead. Thus, he encouraged the authorities to make every effort, together with the World Bank and external donors, to speed up the process of diversification wherever they could. Perhaps the staff could indicate to what extent the possibly faster recovery of world market prices for cotton might provide the authorities with a margin of maneuver to achieve a speedier adjustment than presently envisaged, thus enabling them to effect a somewhat faster shift of resources to the noncotton sector.

As far as the outline of the financial program was concerned, it appeared appropriate under current assumptions, Mr. Bertuch-Samuels commented, and he hoped that the negotiations on the first annual program could be finalized soon. However, he cautioned against relying too much on financing the projected balance of payments deficit by drawing on the country's already very low reserves. It would clearly be preferable if the balance of payments gap could be financed as much as possible by other means. But, as he had indicated already, it appeared that the staff's export projections were based on a rather conservative assumption on cotton prices so that that question might not even arise. Perhaps the staff could provide an updated projection, if not right away, then in the context of the forthcoming request for the use of resources under the structural adjustment facility.

Mr. Noriega said that he fully supported the position stated by Mrs. Ploix. Although financial support was critical at the present juncture in the rehabilitation of the public system in Chad, emphasis should be given to the support that the Fund provided through its technical assistance. Therefore, he asked the staff whether there were any specific ways in which the Fund could act to help Chad cope with its structural problems.

Mr. Kabbaj said that he agreed with the thrust of the staff appraisal, and could support the proposed decisions. In reference to what Mrs. Ploix had said about delays in finalizing a program under the structural adjustment facility for Chad, he had noted from Appendix II of the staff report on financial relations with the World Bank group that an economic mission, including a Fund mission, had taken place as long ago as November 1986 in order to prepare the policy framework paper. He wondered whether such delays in finalizing a structural adjustment arrangement were normal, and why they had occurred in Chad. During the discussion on "the review of the structural adjustment facility," many Directors had referred to the necessity of a certain flexibility, especially for countries that were in difficult and special situations. To wait for a perfect program could mean discussions over a period of a year or more.

The staff representative from the African Department explained that, given the long-term nature of Chad's balance of payments problems, the relatively weak data base and administrative shortcomings, the staff had felt that it was desirable to approach the case on a two-stage basis. As a result, in November 1986 a mission had been sent to assist the authorities in the preparation of a policy framework paper. Following the mission, the policy framework paper had been processed in the regular fashion, both in the Fund and in the Bank. As a result of the normal processing delays, it had not been possible formally to negotiate the policy framework paper until March 1987. Consequently, it had not been feasible to present the policy framework paper to the Executive Board any earlier. The future plans envisaged that a mission would go to Chad as soon as convenient to the authorities to negotiate the first annual program. The expectation at the present stage was that the program would be presented to the Executive Board for consideration before the end of 1987.

On the question of cotton prices, the staff representative noted that there had been additional indications since the staff report had been issued that world cotton prices were firming up faster than expected. The reason was essentially that producers in a number of countries had responded quite strongly to the decline in prices by reducing output. It was tentatively envisaged that Chad might in fact attain a balance of payments surplus approximately one year earlier than indicated in the staff report, namely, in 1991. However, the projections and the impact on the government budget were so tentative that the staff saw no reason to consider undertaking additional expenditure, especially given the rather tight budget.

With respect to technical assistance, the Fund had been providing an advisor to the Minister of Finance on all aspects related to public finance, the staff representative from the African Department explained. The expert had been in Chad for two years and would remain for one additional year. In January 1987, a technical assistance mission from the Central Banking Department had advised the authorities on various technical problems associated with the COTONTCHAD arrears problem and the termination of the moratorium on commercial bank deposits. In addition, Chad was receiving considerable bilateral technical assistance. At the present time, no further requests for technical assistance by the Fund had been received from the authorities.

Mr. Mawakani thanked Executive Directors for their encouraging comments, which he would convey to his authorities.

The Acting Chairman made the following summing up:

> Directors were in general agreement with the appraisal in the staff report for the 1987 Article IV consultation with Chad. They noted the considerable progress made by Chad in recent years in recovering from the combined effects of prolonged drought and civil unrest and welcomed the adjustment measures that had been undertaken to date. Nevertheless, Directors added, the persistence and magnitude of the structural and financial problems that remained were a source of considerable concern. In that connection, an urgent task of the authorities was to implement suitable macroeconomic and also structural adjustment policies to facilitate the reconstruction of the economy, while minimizing the impact of the cotton crisis on both public finances and the balance of payments. Therefore, Directors welcomed the adoption by the Chadian authorities of a medium-term policy framework.
>
> Noting the importance of the cotton sector to the economy, Directors welcomed the efforts and plans to rehabilitate the cotton sector and, in particular, the rehabilitation program for COTONTCHAD. It would be important to persevere with the rehabilitation program and, in particular, to implement a realistic producer price policy which took account of the need to re-establish the cotton sector on a sound financial footing as soon as possible.
>
> Directors remarked that the continuation of a restrained fiscal policy was appropriate in the circumstances and, in this respect, strict discipline in the area of the wage bill would continue to be necessary. Efforts to improve tax collections should also be strengthened and the possibility of increasing revenue through the use of petroleum taxation should be examined. Directors also stressed the need to contain the financing requirement to a level which could be covered by projected levels of foreign budgetary assistance.

With respect to credit policy, Directors expressed the view that the rate of expansion of domestic credit should be slowed significantly in the period ahead, but that the noncotton sector should be allowed additional access to credit. They welcomed the decision of the BEAC to reschedule the arrears of COTONTCHAD and expressed the hope that a formal agreement would soon be signed.

Directors recognized that, given the depressed level of cotton prices and the limited prospects for export diversification, Chad's growth and balance of payments prospects would remain difficult for several years. In the circumstances, they stressed the need for additional concessional assistance and urged the authorities to consider the possibility of a multilateral approach to rescheduling.

The role of technical assistance provided by the International Monetary Fund was also underscored. Directors expressed the hope that negotiations would begin in the near future on possible arrangements under the structural adjustment facility and stressed that, given the structural nature of Chad's problems, close collaboration with the World Bank would continue to be essential.

The next Article IV consultation with Chad would be held on the standard 12-month cycle.

The Executive Board then took the following decisions:

Decision Concluding Article XIV Consultation

1. The Fund takes this decision in concluding the 1987 Article XIV consultation with Chad, in the light of the 1987 Article IV consultation with Chad conducted under Decision No. 5392-(77/63), adopted April 29, 1977, as amended (Surveillance over Exchange Rate Policies).

2. The Fund notes that Chad continues to maintain an exchange system that is free of restrictions on payments and transfers for current international transactions other than the restrictions on tourism and business travel allowances as described in SM/87/122 (5/28/87).

Decision No. 8627-(87/92), adopted
June 19, 1987

Structural Adjustment Facility - Policy Framework Paper

The Fund takes note of the policy framework paper, dated March 21, 1987 from the Minister of Finance and Computing Services of Chad, which describes the major economic problems and challenges facing Chad; the objectives of a three-year medium-term program; the priorities and the broad thrust of macroeconomic and structural adjustment policies; and the likely external financing requirements, together with the available sources of such financing.

Decision No. 8628-(87/92), adopted
June 19, 1987

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/87/91 (6/18/87) and EBM/87/92 (6/19/87).

3. BOLIVIA - STAND-BY ARRANGEMENT - EXTENSION

1. The Government of Bolivia has requested that the period of the stand-by arrangement for Bolivia (EBS/86/120, Sup. 1), scheduled to expire on June 18, 1987, be extended. The Fund grants approval of this extension through July 20, 1987.

2. Paragraph 1 of the stand-by arrangement is amended by the substitution of July 20, 1987 for June 18, 1987. (EBS/87/130, 6/15/87)

Decision No. 8629-(87/92), adopted
June 18, 1987

4. EXECUTIVE DIRECTORS' OFFICES - ELECTRONIC DATA PROCESSING (EDP) SUPPORT

The Executive Board approves the recommendations regarding electronic data processing support for Executive Directors' offices as set forth in EBAP/87/136 (6/15/87).

Adopted June 18, 1987

5. EXECUTIVE DIRECTORS - SECRETARIAL AND CLERICAL ASSISTANTS - GRADING

The Executive Board approves, with an objection from Ms. Bush, the recommendations for the grading of Secretarial and Clerical Assistants to Executive Directors as set forth in EBAP/87/137 (6/15/87) and Supplement 1 (6/19/87).

Adopted June 18, 1987

6. APPROVAL OF MINUTES

The minutes of Executive Board Meetings 86/171 and 86/172 are approved. (EBD/87/158, 6/12/87)

Adopted June 18, 1987

7. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors as set forth in EBAP/87/140 (6/17/87) is approved.

APPROVED: December 21, 1987

CHRISTIAN BRACHET
Acting Secretary