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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 92/100

10:00 a.m., August 3, 1992

M. Camdessus, Chairman
R. D. Erb, Deputy Managing Director

Executive Directors	Alternate Executive Directors
M. Al-Jasser	
	L. E. N. Fernando
Che P.	Wei B.
	G. Lindsay-Nanton, Temporary
T. C. Dawson	Q. M. Krosby
	J. Prader
E. A. Evans	R. L. Knight
R. Filosa	J. Papadakis
M. Finaish	
I. Fridriksson	
	S. Shimizu, Temporary
B. Goos	
	C. D. Cuong, Temporary
A. Kafka	J. C. Jaramillo
J.-P. Landau	I. Martel
A. Mirakhor	
L. B. Monyake	
	P. Wright
G. A. Posthumus	R. Meron, Temporary
C. V. Santos	A. R. Ismael, Temporary
	E. Martínez-Alas, Temporary
A. Végh	A. G. Zoccali

L. Van Houtven, Secretary and Counsellor
M. J. Miller, Assistant

Also Present

H.E. Abdallah Ahmed Abdallah, Ambassador of Sudan. IBRD: A. G. Vaughn, Africa Regional Office. African Department: M. Touré, Counsellor and Director; G. E. Gondwe, Deputy Director; E. L. Bornemann, Deputy Director; P. Dhonte, C. A. François, R. C. Williams. Central Asia Department: B. B. Aghevli, Deputy Director. External Relations Department: S. J. Anjaria, Director; A. Mountford. Fiscal Affairs Department: V. Tanzi, Director; K. Nashashibi. IMF Institute: C. J. R. Morris. Legal Department: R. H. Munzberg, Deputy General Counsel; P. L. Francotte, J. K. Oh. Middle Eastern Department: A. S. Shaalan, Director; P. Chabrier, Deputy Director; N. Abu-zobaa, M. A. El-Frian, H. P. G. Handy, C. A. Sisson, M. A. Tareen, J. F. Wilson. Monetary and Exchange Affairs Department: D. Hoelscher. Policy Development and Review Department: T. Leddy, Deputy Director; L. D. Everaert, N. L. Happe, G. R. Kincaid. Research Department: M. Mussa, Economic Counsellor and Director. Secretary's Department: J. W. Lang, Deputy Secretary. Southeast Asia and Pacific Department: K. Saito, Director. Statistics Department: J. B. McLenaghan, Director. Treasurer's Department: D. Williams, Treasurer; L. Aylward, J. E. Blalock, W. J. Byrne, E. R. D. Canetti, Z. Farhadian-Lorie, D. Gupta. Personal Assistant to the Managing Director: B. P. A. Andrews. Advisors to Executive Directors: M. B. Chatah, M. Galán, Y. Patel. Assistants to Executive Directors: G. Bindley-Taylor, S. K. Fayyad, H. Golriz, W. Laux, R. Meron, F. L. Ochoa, E. H. Pedersen, E. Quattrociocche, D. Sparkes, T. P. Thomas, R. Thorne.

1. SUDAN - 1992 ARTICLE IV CONSULTATION; AND OVERDUE FINANCIAL - OBLIGATIONS - REVIEW FOLLOWING DECLARATION OF INELIGIBILITY

The Executive Directors considered the staff report for the 1992 Article IV consultation with Sudan (SM/92/126, 6/24/92), together with a staff paper containing supplementary information on the staff report and material for the further review of Sudan's overdue financial obligations to the Fund following the declaration of its ineligibility to use the Fund's general resources effective February 3, 1986 (EBS/92/120, 7/27/92). They also had before them a background paper on recent economic developments in Sudan (SM/92/130 7/2/92). Mr. A. A. Abdallah, Ambassador of Sudan to the United States, was also present.

The staff representative from the Treasurer's Department stated that on July 31, 1992, Sudan had made a payment to the Fund of SDR 0.2 million. Sudan's payments since the last review of its overdue financial obligations to the Fund therefore amounted to SDR 0.4 million, or 1.7 percent of obligations falling due. The payment entailed some minor changes to the proposed decision on the review of the arrears which the staff would describe at the time of the Board's consideration of the draft decisions later in the meeting.

Mr. Abdallah made the following statement:

> It is again my privilege to be present at the Executive Board of the Fund as it takes up the 1992 Article IV consultation with Sudan and the further review of Sudan's overdue financial obligations.
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> As the staff papers make clear, a great deal has happened since the last consultation. The Government of Sudan has adopted a radical and far-reaching program of economic reforms aimed at freeing up the economy, bringing down inflation, and creating a climate conducive to the revitalization of the private sector. This has included the dismantling of all controls on prices, investment and trade, the elimination of virtually all budgetary subsidies, implicit and explicit, the lifting of most restrictions on external transactions, the adoption of a unified floating exchange rate, and the launching of a wide-ranging program of privatization. These steps, which mark an unprecedented shift in Sudan's economic policy, have been undertaken in close consultation with Fund staff. They have involved difficult choices and considerable hardship as the economy enters the initial stages of a major adjustment effort. These important policy actions have already begun to bear some fruit.
>
> My Government is fully aware that the steps taken to date are only the beginning of the adjustment process. We would like to be able to report today that even more has been accomplished, but I can affirm that the Government is fully committed to the process

that is now well under way. Sudan intends to build on the recent reforms as quickly as possible, in continued cooperation with Fund staff, toward a comprehensive adjustment program. To this end, my Government is ready to enter into discussions with the staff which, subject to the Board's agreement, are to begin in the next few days, aimed at agreeing on an informal monitoring and management arrangement to cover the period July-December 1992. My authorities have expressed their determination to do everything possible to cooperate with the Fund in the coming months so as to pave the way for Sudan to take advantage of the rights approach as a basis for normalizing its relations with the Fund.

It is very encouraging that, in light of recent discussions between Sudan and Fund staff and management, the staff papers before the Board today envisage the possibility of discussions on a rights accumulation program beginning toward the end of this year. As I have indicated already, my Government does not underestimate the efforts that will be needed on its part to meet the criteria required to embark on this course. However, given the distance we have already traveled toward closing the gap--a gap that seemed unbridgeable not long ago--we are confident that, with your help and support, we can go the extra mile. But your help and support will be very vital to us.

On the policy side, technical assistance will be essential. Initially, and most urgently, this will be needed to help Sudan achieve a better functioning of the new foreign exchange market and in devising and launching government debt instruments. Beyond that, there will be a pressing need for additional technical assistance in developing the financial sector and in the fiscal and statistical areas. We sincerely hope, therefore, that the Board will approve the proposal that technical assistance be made available to Sudan in support of its efforts to formulate and implement a comprehensive adjustment program.

We will also be looking to the Fund at the appropriate time for help in approaching prospective donors and creditors. As Executive Directors are aware, external economic assistance to Sudan has dwindled in recent years. What we have already achieved was done in the absence of external assistance flows. But we hope that as the new economic reforms take hold, the donors will look more favorably on Sudan, and help us to rebuild our economy. For Sudan to both effectively and fully meet its overdue financial obligations, and successfully implement and sustain a strong comprehensive adjustment program, the resumption of international support is indeed essential. Therefore, the Fund's role in providing the required direct assistance, as well as in catalyzing support from the international donor community, cannot be overemphasized. As Directors know, the Fund's needed catalytic role would be heavily influenced by the Board's decision now. We would urge that the Fund be prepared to share its findings with regard to the economic progress and prospects in Sudan with its sister organizations in the international financial community and prospective donors, and would welcome any public disclosure or endorsement of all actions.

We believe that the present adjustment strategy, combined with the additional measures the Government is committed to undertaking in the near future, will lay the basis for strengthening the economy and the balance of payments over the coming years. The process may be gradual, but it will be sustained. This provides our best guarantee to the Fund that we will eventually be able to grapple with the payments issue. For the immediate future, however, the Government has made a specific commitment regarding payments to the Fund for 1992/93. We recognize that the amount committed to the Fund is small in relation to the overdues, and will not be sufficient to avert a further increase in arrears. But when you evaluate our efforts in this regard, I would ask you to give consideration to the following.

First, foreign exchange is critically short in Sudan. Payments to the Fund on a scale needed to freeze the arrears--about $75 million over the next 12 months, or some 12 percent of total current account receipts as estimated by Fund staff--would add more than 20 percent to the Government's domestic borrowing requirement, while adding further pressures on domestic prices and the exchange rate. At the same time, of course, some vitally needed imports would be displaced, particularly essential agricultural imports.

Second, although Sudan is continuing to make debt-service payments to other creditors, these are exclusively directed to multilateral institutions that are continuing to disperse funds to us, namely, the World Bank, the African Development Bank, and the OPEC Fund for International Development. In 1992/93, these amounts will total $26 million. This amount, even if diverted to the Fund in full, would still leave us far behind the requirement for freezing our arrears to the Fund, while at the same time prompting the other multilaterals to suspend disbursements on ongoing projects.

Third, Sudan fully recognizes its financial obligation to the Fund, and is committed to making its best efforts in this regard. The Finance Minister has recently given his assurance to the Fund's management that Sudan will do its best to surpass the amount of payments committed over the next 12 months if our export earnings or foreign assistance receipts exceed present expectations. We recognize that payments on a scale sufficient to freeze our arrears to the Fund is an essential element of a rights program, and we are determined to achieve that goal as quickly as possible. But, in this regard, we need your understanding and your support.

We are anxious to move forward with the Fund in a joint effort to tackle Sudan's longstanding economic and financial difficulties. The process has been initiated in what we perceive as a positive and constructive spirit on both sides. The exercise is long overdue, and we intend to persevere with it. In the months ahead, we will continue to look to the Fund for guidance and support as we seek to expedite this process.

Mr. Monyake said that he endorsed the remarks made by the Ambassador. He then made the following statement:

Since the last review of Sudan's economic situation by the Board, the authorities have taken bold steps, under very difficult circumstances, to implement far-reaching adjustment measures to stem the persistent economic decline and create a more congenial macroeconomic environment for attracting the much-needed support from the international community. Indeed, the basis for the resumption and strengthening of cooperation between the Fund and the Sudanese authorities that should lead to an enduring solution to Sudan's economic malaise has been laid. The authorities are appreciative of the good gestures demonstrated by the staff and management in this regard, and they look forward to agreeing on a comprehensive adjustment program to be monitored by the Fund.

The policy actions taken since October 1991 embraced the liberalization of pricing and exchange rate systems. Measures were also taken to encourage private sector participation in the economy as a strategy for reducing the role of the Government. Additional policies adopted since March 1992 include the elimination of budgetary subsidies in some major areas, particularly on domestic prices of petroleum products. These and other measures have yielded encouraging results, as reflected in the impressive growth of real output--of the order of 9.6 percent in 1991/92, compared with 1.2 percent in 1990/91--the more than doubling of central government revenue, and the strong rebound of nontraditional export commodities.

Nevertheless, the authorities appreciate the enormity of their economic problems, and are aware that more action will be required to effectively address the problem of widening budgetary and external sector deficits, the mounting pressures on domestic prices, and the exchange rate. The authorities are in agreement with the staff that the attainment of these goals would require further strengthening of macroeconomic adjustments and continued commitment to the ongoing structural reforms. In that vein, the 1992/93 budget represents a major step toward restoring fiscal discipline. This latest budgetary effort by the authorities aims at bringing down the budget deficit significantly, with its domestic bank financing being reduced from 6.9 percent of GDP in 1991/92 to 4.6 percent in 1992/93. In this regard, the pursuit of a tight fiscal policy that emphasizes expenditure cuts and revenue enhancement is critical. They have adopted a package of measures to make this target achievable, and stand prepared to consider additional measures if the existing measures prove inadequate.

Revenue efforts will include an increase in tax rates, adjustment in the custom and excise duties in line with the current exchange rate changes, and an improvement in tax collection through the introduction of penalties for late payments. With regard to expenditures, overall budgetary outlays will be contained within budgetary appropriations through close monitoring and strict control on disbursements, while emphasizing spending in productive sectors. To start with, the authorities intend to disburse only 80 percent of the proportional share of the budgeted expenditures for the first half of the fiscal year, and this is expected to be sustained during the second half in order to achieve the programmed reduction in the fiscal deficit. The authorities have also eliminated subsidies to enterprises--except for a few utility companies--and they are embarking on an ambitious privatization program of public entities.

In the area of monetary policy, a restrictive monetary stance has been put in place to complement the tight fiscal policy. As a matter of priority, the authorities have embarked on the pursuit of an active interest rate policy by doubling the minimum lending rate. Depository institutions are also encouraged to offer market-related rates of return on financial savings. The Government will take the lead in this regard by introducing its own debt instruments with market-related rates of interest by December 1992. The attractiveness of these securities, with an initial issue of LSd 500 million, is expected to encourage nonbank participation and lead to a fall in monetary financing of the Government's fiscal deficit. Measures are also being taken to expand and improve the efficiency of the banking system.

On the external front, steps have been taken to further liberalize the exchange system, and the existing restrictions on the import and export of domestic and foreign currency have been eliminated. The authorities are also seriously committed to setting up, as soon as the needed technical expertise is made available to them, a foreign exchange market, through which the exchange rate could be determined by market forces. Until such a more efficient alternative system is put in place, the current arrangement of exchange rate determination by a banking committee will continue.

The deteriorating balance of payments position continues to be a matter of major concern to the authorities. Since 1988/89, the current account deficit has widened, as exports have been declining due largely to poor weather conditions and the weakening of international prices, particularly the prices of gum arabic.

Despite the deteriorating export sector performance, private and official transfers declined to their lowest levels in years, thus leading to the sharp depletion of external reserves and further accumulation of external debt-payments arrears. In 1991/92, the value of imports of goods was more than four times that of the total export earnings, and debt-servicing requirements stood at a high level. This trend has continuously reduced the amount of foreign exchange available to the economy, and imposed serious constraints on the authorities' ability to make payments to the Fund and other creditors on an increasing and sustained basis. All these problems have resulted, as the authorities admit, in token and erratic payments to the Fund. As a matter of fact, they are facing tremendous difficulties in servicing short-term obligations critical to maintaining the minimum level of economic activity.

Under the current situation, characterized by an adverse external environment and domestic problems related to security and drought, the authorities have made tremendous efforts in the area of policy implementation, and they continue to have a positive dialogue with the staff and management. They are fully aware of the need to service their obligations to the Fund, but as the balance of payments profile shows, they lack the capacity to increase substantially their payments to the Fund. The seemingly higher payments made to some other creditors is predicated on the need to ensure the minimum flow of financing to allow imports of essential commodities and other inputs to run the economy.

At this crucial stage, the Sudanese authorities are faced with a very difficult situation. While they remain strongly committed to the adjustment effort, they lack the necessary international financial and technical support to sustain this effort. In this regard, timely support from the international community would not only help the authorities to safeguard the progress already made, but would also facilitate the implementation of additional measures to bring the economy back on the path of sustainable growth and address the problem of arrears to the Fund. It is, therefore, of the utmost importance that the Fund, as a cooperative institution, should stand ready to recognize the progress made thus far, and assist the authorities to build on their achievement, perhaps by promptly endorsing a Fund-monitored program. This would help to catalyze the much-needed assistance, while creating a favorable political environment for further reform within the country itself. More importantly, the success of such a program would pave the way for the resolution of the longstanding problem of the protracted arrears to the Fund and other creditors, to the long-term benefit of the country and the creditor community alike.

Mr. Mirakhor made the following statement:

The authorities should be commended for their decisive and realistic policy initiatives undertaken under extremely difficult circumstances. The untiring efforts of the staff in assisting the authorities in this task deserve our appreciation. The authorities' determination to come to terms with the fact that the deteriorating economic situation in Sudan required a drastic reorientation of their policy stance, along with valuable staff assistance, have led to the emergence of a set of policy measures that provides strong foundations for a comprehensive program of stabilization, reform, and adjustment.

If the heavily front-loaded and wide-ranging measures already adopted are sustained and strengthened, there is the likelihood that Sudan will be in a position to remove the root causes of severe domestic and external economic and financial imbalances that have plagued the economy for so long.

The statements of Ambassador Abdallah and of Mr. Monyake, together with the staff report, are comprehensive in their coverage of the measures adopted so far. These measures--which include, inter alia, the rationalization of subsidies, liberalization of investment opportunities, a very serious attempt at rationalizing government expenditures and reducing government reliance on bank financing--go a long way in changing the bleak and discouraging policy prospects that faced the Board as late as last March. The slashing of the domestic borrowing requirement from 90 percent of the opening money stock to 37 percent in a very short time span is an illustration of the seriousness of the authorities' intent to deal with the enormous task of implementing the needed stabilization, reform, and adjustment measures. The reduction of the domestic borrowing requirement will stem the tide of inflationary pressures and help the emergence of positive real rates in the banking system. In this context, I wonder whether the staff has quantified the relationship between domestic borrowing and inflation, so as to give us some idea of the efforts that can realistically be expected in order to bring inflation down to more tolerable levels. It is encouraging to learn that the authorities have committed themselves to the introduction of securities in the course of 1992/93. They have, however indicated that Fund technical assistance is needed in this task. They have also requested Fund technical assistance to ensure that further liberalization of the exchange and trade system is implemented and that greater market responsiveness to the exchange rate is effected.

Given the authorities' demonstrated strong commitment to the implementation of a comprehensive and integrated adjustment program and the enormity of the task ahead, timely technical and financial support would greatly assist the authorities to sustain the measures already taken, enhance their ability to implement further reform measures, and allow them to strengthen their efforts to embark on a concrete program of settling the problem of protracted arrears to the Fund.

I was pleased to see that clear and specific steps have been recommended by the staff which, if followed, would lead to the lifting of the declaration of noncooperation. As I understand the process, the staff now feels that the present policy stance provides a strong enough foundation upon which to build a comprehensive and integrated adjustment program. Pending approval by the Executive Board, the staff will travel to Sudan immediately to draw up, in collaboration with the authorities, a framework for the informal monitoring of Sudan's macroeconomic policies and their payments performance vis-à-vis the Fund for the rest of this year. This will then be the basis upon which Sudan's track record, in terms of its cooperation with the Fund, will be judged. Assuming that this track record is judged satisfactory by the Board, discussions of a possible rights accumulation program will take place during December 1992. In the meantime, if in the judgment of the staff strong prospects of sustainability of the measures already taken exists, the staff is prepared to intervene on behalf of Sudan with prospective donors. The latter step would be essential in enhancing the authorities' capacity to sustain their adjustment program, as well as their expressed determination to improve substantially their payments performance vis-à-vis the Fund.

We endorse this process, and we hope that the experience with Sudan is a resounding success that would encourage the emergence of a clear and transparent process the observance of which by members declared as noncooperative will lead to the lifting of declarations of noncooperation. This will help further clarify and enhance the arrears strategy. We endorse the thrust of the staff appraisal and the proposed decisions.

Mrs. Krosby made the following statement:

When the Board last met to discuss Sudan, it was suggested that, in general, the initiation of normalization of relations between a country in arrears to the Fund and the Fund could begin to progress relatively rapidly once the country's authorities had decisively indicated their desire to be more cooperative. The events of recent months between Sudan and the Fund now show the reality of this hypothesis. On the basis of the policy measures described by the Ambassador, we are prepared to be more supportive of Sudan's efforts than in the past, and we can approve the proposed decision for an informal monitoring arrangement as the best approach under the circumstances. Our only regret is that Sudan's payments performance to the Fund to date has not matched its policy efforts.

The policy area of most concern to us in the past was the extremely high level of monetization of large fiscal deficits and the accompanying inflation potential. Therefore, the authorities' understanding of, and action to address, this point during discussions with the staff are highly welcome, and probably the most convincing aspect of their commitment to an economic adjustment program. We would suggest that the authorities go the next step in limiting monetization this fiscal year even further, not only because of its positive economic impact, but also because it would be an impressive symbol of their overall commitment to the process.

The authorities have now agreed to build on those structural reforms already taken to improve the competitive workings of the economy. In the next six months, some important and necessary measures are planned which should be a sharp and welcome change from past practices. Interest rates, despite a recent doubling of minimum lending rates, are still negative, and will remain so if they stay at this nominal level through the end of the year--even with the projected improvement in inflation. For the success of the introduction of government securities--particularly as an eventual monetary policy tool--some measures pinpointed at unsticking interest rates will be needed to provide the appropriate market setting. The unification of the exchange rate and more liberalized pricing policies should also have a salutary effect on improving the ability of the market mechanism to work efficiently in the Sudanese economy.

Meeting all of these commitments on schedule will strongly influence our future position as to whether or not to encourage or support Sudan in moving to a more formalized Fund-supported program that would be underpinned by a comprehensive economic adjustment plan.

We support the renewed extension of technical assistance in the areas proposed in the staff report, and we suggest further that the inconsistencies in the official budget projections might make technical assistance in this area useful as well.

The results of an analysis of the two criteria for determining cooperation with the Fund are unfortunately lopsided. Against the sharp improvement in policy implementation, the recent performance on payments to the Fund appears all the more limp. In the last six months, the level of payments, which had already been small--only about 5 percent of obligations falling due--decelerated even further. We welcome the news of the last payment, but until it is followed by subsequent and increasing payments, it does little to reverse the record of erratic and small efforts to meet Fund obligations. A sustained record of efforts on payments --one that is basically the reverse of the record to date, including payments in amounts that are at least sufficient to keep up with current obligations--will be necessary before we can approve the lifting of the declaration of noncooperation or a more formalized Fund-supported program.

At this point, we would like to emphasize that our support for the informal monitoring suggested today is obviously conditional on keeping commitments already made, on an acceleration of the reform effort, and on reversing the current extremely poor payments record. In particular, we would like to emphasize that the best method of establishing the necessary solid track record is by keeping faithfully to targets and policy commitments reached in the understandings with the Fund.

Overall, it is with considerable pleasure that we are able to support the adoption of any sort of monitoring framework for Sudan, given that, in the relatively recent past, this stage would have seemed a very distant prospect. It is to the strong credit of the Sudanese authorities, and to the staff working with them, that we are here to take this decision.

Mr. Filosa made the following statement:

In the last several years, the Sudanese authorities have persistently deviated from the cooperative behavior that is required from the Fund's members. The economic policy followed by Sudan has consistently disregarded the recommendations made by the staff and the Executive Board, thereby making the economy even worse. In addition, Sudan has been in arrears to the Fund since 1984 and, notwithstanding the repeated warnings of the Executive Board, it has constantly ignored the preferred creditor status of the Fund, giving priority to payments due to other creditors. As a result, overdue obligations to the Fund have grown to more than 6.5 times Sudan's quota, and the unavoidable declaration of noncooperation was issued in September 1990.

At this stage, the Sudanese authorities have to clearly and promptly demonstrate to the Fund their determination to correct their past behavior, in order to comply with the basic principles governing international financial relations. This is the first time since 1984 that a certain willingness on the part of the authorities to resume cooperation with the Fund has been shown. We welcome this change of attitude because, given the delays already experienced and the extent of the economic and social crisis in the country, any further postponement of action would only bring Sudan closer to economic collapse, and to the adoption of the additional remedial measures envisaged in the Fund's arrears strategy.

Indeed, what is most needed, as pointed out on several previous occasions, is the immediate implementation of comprehensive macroeconomic and structural policies along the lines suggested by the staff, and the early resumption of adequate payments to the Fund.

Concerning economic policies, a piecemeal and gradual approach to adjustment, as we have witnessed so far in Sudan, would not be of much help in correcting the serious domestic and external imbalances which affect the economy. As a result, the rapid GDP increase estimated for 1991/92 might turn out to be unsustainable.

In the real sector, not all of the measures either taken or envisaged by the authorities appear to be consistent with this purpose. The decision to retain the system of government directives on the areas to be devoted to the cultivation of specific crops, for example, runs counter to the announced program of liberalization in the agriculture sector. Also, the attempt to pursue a program of privatization in the public enterprise sector has few chances of success if sound economic and financial policies are not firmly in place. Indeed, the lack of firm policies has resulted in a lack of confidence on the part of private investors so far and, in fact, only 5 out of the 13 companies selected for disposition in 1991/92 had been sold by May 1992.

Concerning fiscal policy, the budget for the current fiscal year shows that, despite the prospective adoption of some measures, both revenues and expenditures as a ratio to GDP will remain broadly unchanged relative to last year's figures. In addition, in comparing the estimated outcome for the current fiscal year with the results obtained two years ago, one cannot fail to notice that revenues are projected to increase by a slim 1 percent of GDP, while expenditures will be growing by a robust 7 percent relative to GDP. Domestic bank borrowing, although receding from the stunning figure registered last year, is projected to be equal to 37 percent of the opening money stock--the same figure as in 1990/91. For these reasons, I am surprised that, while the staff considered it possible to keep the

Government's domestic borrowing requirement to a level not exceeding 25 percent of opening money stock through the adoption of additional fiscal actions, it is now satisfied with the Government's target of 37 percent. Although this represents a considerable improvement with respect to past performance, it still entails an average inflation rate of 85 percent in 1992/93, with the risk that any deviations from the target might call into question the viability of the new pricing policy and exchange rate regime. In addition, the authorities have indicated that they see "considerable difficulties in adopting further measures at this time." This concern is amplified by the limited scope for an independent monetary policy in Sudan. A wide-ranging reform of the banking system and of the financial sector is needed if long-lasting results in curbing inflation are to be achieved. This reform can certainly be regarded as a medium- to long-term goal, but it is regrettable that, in the meantime, little progress has been made in implementing measures to improve rates of return on financial instruments and to introduce government securities with market-related rates of return. The request for technical assistance from the Fund in this area is appropriate, as it would help the Government accomplish its task, especially in issuing new, market-based financial instruments by the end of the year, as announced by the authorities.

On the exchange rate side, the steps taken by the Government to further liberalize the exchange system after the adoption of a freely floating exchange rate in February this year are to be welcomed. In particular, the adoption of a market-based approach in setting the exchange rate will help overcome the rigidities and the substantial complexity that has emerged with the committee system presently in operation. In this regard, once again, I deem appropriate the request for technical assistance from the Fund, in the hope that it will help put in place a more efficient exchange market.

Overall, the envisaged measures do not seem to be much more than a promising start. Regarding the problem of arrears to the Fund, the picture is, unfortunately, even less encouraging. Since the last review of Sudan's arrears, payments to the Fund have amounted to a little more than 1.5 percent of obligations falling due, and cannot be interpreted as a sign of the authorities' intention to achieve arrears stabilization soon. Indeed, the schedule of payments envisaged by the Government will lead, in the best of circumstances, to the fulfillment of about 9 percent of obligations falling due during fiscal year 1992/93.

Even taking into account the serious problems affecting Sudan's economy, I cannot help remarking that such a poor performance is also the outcome of the regrettable choice of the authorities to service the debt of only those creditors who are still disbursing funds, thus discriminating against the Fund, disregarding the huge amount of financing obtained from this institution, and the financial burden that they are imposing on the entire membership of the Fund.

On such premises, the degree of cooperation of Sudan with the Fund in terms of payments cannot be considered sufficient. The token payments on July 31 do not change this assessment. Unless the Sudanese authorities realize that they have to engage in a much more substantial effort to fulfill their obligations, not only do the prospects for a rights accumulation program become evanescent, but the decision leading to further remedial measures also becomes hard to avoid.

In the coming months, Sudan should make significant efforts to strengthen its economic program in the context of the informal monitoring framework that the staff is planning to establish. In addition, Sudan should seriously consider that the stabilization of its arrears to the Fund is an essential element for the approval of a rights accumulation program by the Board. It is only in the expectation that Sudan will take this last chance to set its record straight that I can support the proposed decisions.

Mr. Wright made the following statement:

Like other speakers, I think that the staff report on the latest developments in Sudan is an encouraging one. There has been an ongoing policy dialogue between the staff and the authorities, and many of the measures which the Ambassador outlined to the Board in March have now been implemented. Although these fall short of a comprehensive reform program, they do represent a significant and very welcome change in the direction of economic policy. These measures will need to be sustained and built upon as part of a formal monitored program with quantified targets set by the Fund. I am pleased that the authorities feel able to request such an arrangement, which would be a first step toward a rights accumulation program and the eventual resolution of the arrears problem. It should also pave the way for a resumption of adjustment lending by the World Bank.

The Sudanese authorities find themselves poised at a critical juncture. These recent measures, welcome though they are, represent only the first step on what will undoubtedly be a very long and difficult path. Indeed, given the extent to which financial relations with the Fund have deteriorated, it is not entirely clear at this stage how the arrears problem will be resolved. But, however this is to be achieved, the establishment of a dialogue in which the authorities are willing--at least--to speak the same language as the Fund is a development of considerable importance. It follows from this that the Sudanese authorities must resist any temptation to see the recent measures as a token designed merely to head off a further deterioration in relations with the international community. Nothing less than a comprehensive and mutually supporting package of reforms will be sufficient to arrest the decline of the Sudanese economy, re-establish private sector confidence, and generate the necessary external supports. The authorities' strategy still seems to be defined in rather general terms, and the present policy mix remains a risky one. I share many of the concerns outlined by Mr. Filosa in this regard. It is essential that the recent liberalization of prices and the exchange rate be supported by more stringent fiscal and monetary discipline if inflation is not to increase further, which would undermine all of the good work that has been done so far.

There seems considerable scope for increasing the very low level of government revenues. Public spending should be better prioritized to ensure that resources are targeted at the social sectors. The remaining price controls need to be scrapped to encourage a private sector response and prevent re-emergence of unintended subsidies. Across-the-board pay increases will have to be resisted. There is no doubt that defense spending exceeds the level that the economy can afford. I wonder whether the staff can clarify the extent of budgetary subsidies to the public utilities.

The underdeveloped financial system, in the absence of any means to finance the deficit in a noninflationary way, makes fiscal adjustment all the more urgent. While I fully respect the authorities' wish to reform the financial system in a way consistent with Islamic doctrine, there is no escaping the fundamental need for a soundly based monetary policy within such a framework.

The seeds of Sudan's economic decline were sown 20 years ago, when an attempt was made to boost and develop the economy through nationalization and low productivity, with public sector investment financed by foreign borrowing. The situation was aggravated by price and trade controls, discretionary tax and tariff systems, subsidies, and an overvalued exchange rate. Many of these debilitating features of a command economy remain in place today. It is essential that fiscal retrenchment go hand in hand with a complete orientation of the economy toward the private sector. This is a formidable challenge, one which is not, of course, peculiar to Sudan. I hope that the World Bank will be called upon to play a full part in this transformation process.

Regarding Sudan's overdue obligations, it is very disappointing that only two very modest payments have been made to the Fund since the last review, despite the fact that Sudan has remained fully current on its obligations to the World Bank and several other creditors. There must be a real question about whether it is possible for Sudan to stabilize its arrears completely in the present circumstances. This is an indicator of the seriousness of the problem facing the authorities. The Board will need to consider Sudan's capacity to make payments very carefully in the context of any request for formal Fund assistance. Clearly, however, the Board will expect Sudan to establish a regular payments record before going very much further along the path of cooperation.

I am sure that the authorities and the staff are aware that the resumption of program aid by donors will depend on progress in economic areas, as well as a variety of other areas.

The recent change in the direction of policy in Sudan gives us grounds for optimism, even though it is no more than a start, as others have emphasized--and which cannot be emphasized too often. I very much hope that the momentum of reform will be stepped up and that there will soon be a realistic possibility of getting to grips with the arrears problem. I can support the draft decisions, including the important one concerning a resumption of Fund technical assistance to Sudan.

Mr. Goos stated that he, like the previous speakers, had been glad to note from the staff papers and from the presentation made by the Ambassador the substantial progress that had been achieved in the recent discussions between the authorities and the staff toward the formulation of a comprehensive program of adjustment and reform. Such a program could eventually serve as the basis for a rights accumulation program and for the normalization of Sudan's relations with the Fund. The progress achieved, including the encouraging policy measures already implemented under admittedly difficult circumstances, and the recent policy commitments, constituted a most welcome reorientation away from years of gross economic mismanagement. That reorientation had been more than overdue, as evidenced by the prolonged economic decline, the suffering of the Sudanese people, by the staggering--and still growing--stock of external arrears, and the accompanying increasing isolation of the country by the international financial community.

While it was never too late for a new beginning in the economic life of a country, it was clear that the task of economic rehabilitation and restoration of confidence could be achieved only if it were to be pursued persistently in the framework of a resolute and credible effort over a number of years, Mr. Goos observed. For that very reason, the authorities should integrate their program in the medium-term adjustment strategy, which would also be essential for their program to qualify as a comprehensive effort, as required under the Fund's arrears strategy.

The staff had pointed out other weaknesses in the authorities' adjustment effort that should be urgently addressed, Mr. Goos continued. Without wishing to detract from other critical areas of adjustment, he would like to associate himself especially with the concerns of the staff in respect of the still negative levels--in real terms--of the present rates of return and charge on financial instruments. In view of the importance of those rates for the mobilization of domestic and external financial resources and their efficient allocation, and for the inflation goals and the stability of foreign exchange markets, the authorities should follow the staff's advice on interest rate policy without delay. The same applied to the advice to redouble their efforts at fiscal consolidation in order to ease the burden on monetary policy, and redirect available resources to the private sector. Unfortunately, the encouraging progress that had been made on the economic policy front was not being matched by a comparable improvement in Sudan's payments performance vis-à-vis the Fund, as all of the previous speakers had stated.

The authorities' view--as expressed at the most recent discussion in the Fund and as reiterated by the Ambassador--that Sudan's ability to pay would be extremely limited in the absence of external assistance and other factors was somewhat difficult to understand, for several reasons, Mr. Goos commented. First, it appeared that such a view constituted an unfortunate backtracking from the position the authorities had taken at the time of the consultation in Khartoum. At that time, according to the staff report, the authorities had apparently been willing not only to resume monthly payments to the Fund, but also to increase those payments, so that by the end of 1992 the payments would be sufficient to stabilize the stock of arrears. Compared to that, what the authorities were currently offering would imply the continued accumulation of substantial additional arrears. Second, the position of the authorities with regard to their payments performance vis-à-vis other creditors clearly contradicted the preferred creditor status of the Fund. Third, the alleged inability to pay the Fund was difficult to reconcile with the authorities' refusal to raise the rates of return and charge on financial instruments, as was their hesitation to further tighten financial policies. Scenario B in the staff report clearly indicated that, with more appropriate policies, Sudan could significantly widen the scope for payments to the Fund.

With respect to the assumptions underlying Scenario B, he was not fully convinced of the need for a further modest real depreciation, whatever "modest" might mean in that context, Mr. Goos noted. It appeared, for example, that Sudan's exporters still enjoyed a considerable competitive margin, and even the standard gauge normally used by the staff--the spread between the exchange markets, which at present was nonexistent in Sudan--did not seem to lend much credence to the staff's devaluation advice. However, the agreement on exchange rate policy appeared somewhat irrelevant to the issue of whether or not the authorities should--or could--raise significantly their payments to the Fund in order to fully meet the criteria for satisfactory cooperation with the Fund.

With respect to the further application of the Fund's arrears strategy, he could endorse the approach outlined in the staff appraisal in the supplementary paper, Mr. Goos concluded. In recognition of the authorities' comprehensive adjustment efforts and their improved cooperation with the Fund, he could also support their request for technical assistance by the Fund for the development of government borrowing instruments and the reform of the exchange system, which were indeed critical areas for the success of the stabilization strategy. He would even be willing to go a step further and endorse the authorities' request that the Fund recognize publicly their adjustment and reform effort. Such a recognition could be phrased along the lines of paragraph 3 of the proposed decision in the supplementary paper. It could also include--subject to the implementation of further adjustment measures and satisfactory payments to the Fund--the willingness of the Fund to engage in a rights accumulation program with Sudan at a later time, and to rescind the declaration of noncooperation. He could endorse the thrust of the staff's recommendations, as well as the proposed decisions.

Mrs. Martel made the following statement:

At the last Board meeting on Sudan, we decided to review the matter of Sudan's overdue financial obligations to the Fund in the context of whether Sudan's cooperation with the Fund, in the areas of payments to the Fund and policy implementation, had been substantially improved.

It is obvious that, since the last review, Sudan's payments performance has continued to be poor, even taking into account the very recent payment made to the Fund, and that its commitment to making future payments is not all that it might be.

However, like other speakers, we acknowledge and welcome the fact that Sudan has taken steps to reorient its economic policy toward the correction of economic and structural imbalances. Some of the courageous measures already taken--notably in liberalizing the economy--as important as they may be, are rooted in a comprehensive program of macroeconomic adjustment.

I share the staff's recommendations and the remarks of previous speakers as to the necessity of strengthening fiscal and interest rate policy and accelerating structural reforms. The first recommendation is the further reduction of the Government's borrowing requirement in 1992-93 to the equivalent of about 25 percent of opening money stock. The authorities have already implemented a package of measures to bring down the deficit and to reduce its domestic bank financing, but reducing inflation more rapidly will require that additional measures are taken on the budgetary side.

In this regard, I welcome the intention of the authorities to disburse only 80 percent of the proportional share of the budgeted expenditures for the first half of the fiscal year, and to keep to that path during the second half. There is clearly some room for maneuver on the current expenditure side.

I noted the very large increase in wages and salaries--more than 280 percent between 1991-92 and 1992-93--and, while I am aware of the need to allocate an adequate amount of compensation to the poor segments of the population, I would appreciate some comments from the staff on the wages policy of the authorities.

Some measures on the revenue side, such as an increase in tax rates and adjustments in customs duties, have been taken, but further actions aimed at broadening the tax base and reducing exemptions should be considered as part of the comprehensive adjustment program, as the staff rightly emphasized.

The recommendations for introducing more realistic interest rates are also important. I welcome the recent increase in lending rates, but I encourage the authorities to take additional steps to increase real rates of return, which is essential for eliciting an appropriate level of domestic private savings.

Regarding the normalization of Sudan's relations with the Fund, the efforts of the Sudanese authorities to stabilize the level of arrears have not been sufficient so far. The payment to the Fund of SDR 0.4 million is still disappointing. I welcome the commitment of the authorities to make payments of at least $6 million during the present fiscal year, but I note that it represents only 9 percent of obligations falling due to the Fund during the period.

I share the staff's view that substantial increases in payments to the Fund on a regular basis, and at a level that would freeze Sudan's arrears to the Fund, would be an essential element of the concrete implementation of the cooperative strategy.

The economic measures already taken by the authorities and their commitment, as emphasized by Ambassador Abdallah, to put in place a comprehensive adjustment program with the assistance of the Fund argue in favor of giving Sudan more time to establish the necessary track record. I support the proposed decisions.

Mr. Fernando made the following statement:

Over the last few months, clear signs have emerged of Sudan's close cooperation with the Fund in finding solutions to its deep-seated economic problems. This is the result of a deliberate change of policies initiated by a new administration and a new team of policymakers. Even if the economic havoc has been largely self-inflicted, the new administration has acted decisively in making radical shifts in economic policy. As noted by many, the reforms in pricing and the exchange system, together with trade liberalization, are far reaching; indeed, perhaps some elements may be too far reaching, because it might be premature to lift restrictions on capital transfers. We would also like the staff to comment on how export surrender requirements--as a policy--are compatible with the freedom of commercial banks to sell foreign exchange for capital transfers. More generally, we commend the authorities for intensifying the policy dialogue, and we are encouraged to learn from the staff that the fiscal outlook has improved substantially since the previous Board review.

Even though the reform policies have to operate in a situation of acute financial crisis, the ensuing hardship, through its uneven distributional effects, will keep policies under constant and intense pressure. Although wage increases and targeted transfers can meet immediate concerns, the real challenge to the authorities will be to maintain course toward program objectives. Containment of inflation and a visible supply response will be crucial to maintaining policy credibility. In this context, the strong revival in agricultural output and the resulting food security is a strong incentive for the authorities to put behind them a critical mass of reforms.

We generally agree with the staff appraisal, and we would particularly endorse the conclusion that fiscal policy should provide strong support for the attainment of the monetary policy objectives. Efficient instruments of monetary policy and a market system are largely absent. Monetary financing of the budget should thus be rapidly curtailed so as to rein in undue expansion of monetary aggregates. The imperative of reducing monetary financing of the budget is directly linked to the overall strategy of private sector-led revival. Even in the circumstances of the financial crunch, adequate liquidity should be available to the private sector and the liberalized public enterprises, so that they will be able to provide the supply response on which the sustainability of the reform effort rests.

At this stage of stabilization, a credible fiscal policy requires a strong revenue effort. The downside risks to a strategy that emphasizes more efficient collection are very high. Even if such a strategy can yield results, the time scale required would likely outstrip the urgency of short-term stabilization. A self-evident case exists for the use of taxation to capture windfall profits arising from exchange depreciation and price deregulation. Given pervasive state involvement in commercial activity, the scope for monopoly rents arising from price deregulation is large. There is also a potential for output losses when the prices of items produced under monopoly conditions are deregulated. Such tendencies can undermine the reform exercise, and this argues for the imposition of taxes to offset such monopoly rents. If an overall improvement in the budget results from these expedients, the authorities could have a greater latitude for targeted income transfers in order to support the supply response of the economy.

Although revenue measures take up the burden of short-term fiscal stabilization, expenditures will need to be kept firmly in check in the period beyond. Some receipts are one-off inflows, such as those coming from the privatization of state firms. They cannot be counted on for the outer years, as the salability of public enterprises will be limited by questions about their economic viability under a competitive regime after a certain point.

Trade liberalization and exchange reforms have been fundamental and far reaching. Since they were taken up front, they typically deserve balance of payments support, which is required not merely to stabilize market conditions, but also to do so in a way that would allow such stability to occur without an undue compression of economic activity. Sadly, in Sudan's case, we do not see clear signs yet of such external financing support. At a minimum, therefore, we strongly support the resumption of technical assistance. The trade and exchange areas are particularly complex for any country that is breaking out of government controls to deal with. Besides, we would note that technical assistance would help upgrade the quality and timeliness of data, as the Fund would itself need reliable indicators by which to assess the impact of policy reform.

The objective of all policies should be the re-establishment of domestic confidence, which is essential to relieve growth constraints and keep exports competitive. The authorities should be firmly convinced of the benefits of improved domestic confidence, as the behavior of capital and private transfers can quickly transform the balance of payments. The fight against inflation should not be compromised by excessively optimistic expectations regarding external assistance. It is essential to demonstrate the authorities' belief that economic reform is primarily for domestic benefit. This can be achieved only by the steadfast implementation of policy, and hopefully, by the necessary international goodwill to support Sudan's policies through finance on the appropriate terms.

Concerning payments to the Fund, we share the sense of disappointment that has been expressed and we urge that more be done. In the June staff report, it is said that the authorities stand ready to resume monthly payments on a scale rising to a level needed to freeze arrears to the Fund toward the end of 1992. However, in the supplementary paper, there is no assurance that this point will be reached even in mid-1993. A clarification from the staff might therefore be helpful.

The staff representative from the Middle Eastern Department stated that the borrowing requirement of the Government that the staff was currently anticipating for fiscal year 1992/93--LSd 34 billion--was consistent with an average annual inflation rate of 85 percent in that fiscal year, with a downward trend over the course of the year, leading to an inflation rate of the order of 55 percent on a 12-month basis at the end of the fiscal year. If the borrowing requirement could be brought down closer to LSd 25 billion--a target that the staff advocated--the rate of inflation would be lowered even more--to perhaps 75 percent, with the end-year rate coming down to about 40-45 percent. The annual rate of inflation was not moving very much because the rate had been very high in the course of the previous fiscal year, so that even if prices remained steady throughout the current fiscal year, the average annual inflation rate would still remain as high as 60 percent. The staff hoped to see a faster reduction in inflation in the course of the current fiscal year, as the monthly inflation rates fell.

The extent of the fiscal adjustment did not appear to be particularly impressive on the basis of the table presented in the supplement to the staff report, the staff representative agreed. However, it needed to be borne in mind that in fiscal year 1991/92, the true fiscal position had been obscured by the extent of price distortions in the economy and of implicit subsidies. Since then, the exchange rate had moved from about LSd 15 per US$ the beginning of the fiscal year, to close to LSd 100 per US$ at the end of the fiscal year, and the widespread price controls and implicit subsidies had been eliminated by the end of the year. Therefore, drawing conclusions from the trend was probably unwarranted, because of the discontinuity in the nature of the fiscal data. It might also be recalled that at the time of the Board's previous discussion of Sudan's arrears in March 1992, the domestic borrowing requirement had been of the order of 90 percent of the opening stock of liquidity on an annual basis. That level of the borrowing requirement would have been likely to result if no further measures had been taken. At present, the borrowing requirement was about 35 percent of the opening stock of liquidity, which reflected the measures that the authorities had taken since February 1992, including--for example--the adjustment of petroleum prices to world market levels, improved procedures for the collection of income taxes, and increases in customs duties.

The staff was discussing with the authorities the possibility of reducing the borrowing requirement in fiscal year 1992/93 below the presently projected 37 percent of opening period money stock, the staff representative related. The authorities had indicated their intention to hold expenditures at 80 percent of allocations in the first half of the fiscal year, and to review the situation around December 1992, in consultation with the staff, to consider further measures, as necessary. There was thus some scope for expenditure cuts in the course of the year that would bring the borrowing requirement down below what was currently envisaged. If expenditures were maintained at 80 percent of budgetary allocations throughout the fiscal year, then the borrowing requirement would be reduced to about LSd 23 billion or LSd 24 billion--about two thirds of the present projection.

The only budgetary subsidies being provided to the public utilities at present were to the water and electricity corporation, the staff representative stated. The subsidies would amount to about LSd 4 billion in the course of the year--out of a total domestic cash expenditure of about LSd 100 billion. The Government had emphasized its determination not to allow those subsidies to exceed that limit, and the other public enterprises had been instructed to adapt their policies to ensure that they would not need to have recourse to any government support in the course of the year.

The commitment the authorities had made to the staff at the time of the Article IV consultation discussions to stabilize Sudan's arrears to the Fund toward the end of 1992 had presupposed the renewal--to some extent--of external assistance to Sudan in the course of the current fiscal year, the staff representative explained. Under more realistic assumptions as to the level of external assistance that could be expected, such a commitment was obviously overoptimistic, and the authorities had subsequently decided that they could commit to making only a limited amount of payments to the Fund, which would not be sufficient to keep the stock of arrears from growing.

The staff had assumed a modest real exchange rate depreciation in the balance of payments projection for 1992/93 because, following a period in which the exchange rate had been quite sticky, between February and May 1992 the exchange rate had appreciated in real effective terms by about 30 percent, the staff representative stated. If it were assumed that the exchange rate in February was in any way an equilibrium rate, the appreciation that had taken place over the ensuing months had been quite significant, with a further appreciation since then, as the rate had remained at or near LSd 100 per US$. As the Government moved to improve the functioning of the foreign exchange market over the course of the year, therefore, it could be expected that the rate would become more mobile, and that it would depreciate in real terms to offset to some extent the previous real appreciation.

The line item for wage outlays in the budget, which indicated an increase in public sector pay of about 180 percent in the present fiscal year over the previous year, needed to be interpreted with some caution, the staff representative pointed out. The increase reflected mainly the cost of living adjustments that had been granted in October 1991 and again in February 1992, following the very sharp depreciation and price adjustments, largely to unskilled or lower-level civil servants. Pay for the senior civil servants was scattered throughout a number of different items in other parts of the budget, and the staff did not have a clear idea of what the public sector wage bill really was--one of the many weaknesses in the fiscal data that the staff would wish to correct. Nevertheless, it appeared that total increases in pay for civil servants in 1991/92 had been of the order of 80-90 percent on an annual basis, which, in light of the ongoing rate of inflation, was not very far from keeping wages constant in real terms--but with some loss of real purchasing power.

With respect to the social safety net, the Government had established in March 1992 a new program to provide identified poverty groups with a small monthly payment--about LSd 500 a month per family, the staff representative noted. About 500,000 families had been targeted to receive it. The staff would examine how the program was operating.

The staff had stressed to the authorities the fact that the export surrender requirements no longer had any meaning given the extent of the exchange liberalization, and had encouraged them to move away from them, the staff representative commented. Although an exporter was obligated to surrender his earnings to the market, he was entitled to return to the banks the next day and purchase the foreign exchange for any purpose he desired. The authorities had expressed a preference for retaining export surrender requirements for the time being, but the staff had asked them to consider lifting them.

In response to a question from Mr. Fernando, the staff representative said that, with respect to the maintenance of controls on capital transfers, the authorities had expressed their determination to try to free up the exchange system completely, which should be possible once the exchange rate and interest rates were realistic. However, on the one hand, because the staff and the authorities entertained considerable concerns about the realism of the interest rate structure in the economy--and in particular, about an inadequate interest rate policy--they feared that completely freeing capital movements would lead to the hemorrhaging of capital out of the country. On the other hand, of course, the authorities wished to encourage capital inflows, which had traditionally been an important element of the balance of payments, moving over the years in reaction to the quality of the economic policies. As policies strengthened, as the exchange rate became more realistic, and as the interest rate policy improved, it was to be hoped that substantial reflows of capital would occur.

Mr. Shimizu made the following statement:

> It is encouraging to note that there have been positive developments in the implementation of adjustment policies, such as the unification of the exchange rate and in the fiscal area. In addition, I welcome the authorities' intention to initiate a Fund-monitored program in the latter part of this year as evidence of the authorities' willingness to cooperate with the Fund. I would stress the importance of reducing the budget deficit and the domestic borrowing requirement--and its monetization--in the program.
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> Like other speakers, I regret that there has been no progress at all in Sudan's payments to the Fund. It is disappointing that, since the last review in March, the authorities have paid far less

to the Fund than the obligations that fell due, thus increasing the total amount of the arrears. One may argue, therefore, that the authorities failed to observe the conditions set at the last Board meeting in terms of payments, and that the Board should decide to initiate procedures in accordance with the decision. However, in light of the positive developments in the policy field, I can go along with the staff's recommendation not to initiate the procedures.

The authorities argue that, because of the low level of foreign assistance, they cannot afford to pay the full amount of their obligations. However, they should realize that the normalization of relations with the Fund--by way of payments to the Fund--is the prerequisite for the release of aid by donors. In addition, stabilization of the level of overdue obligations to the Fund is absolutely necessary before a rights accumulation program can be considered. In this connection, it is regrettable to learn that there has been a backtracking in the authorities' commitment. I support the proposed decisions.

Mr. Ismael made the following statement:

We are pleased to note from the latest staff report that an understanding has been reached with the Sudanese authorities on additional adjustment measures to broaden and strengthen the important policy measures taken in the course of 1991/92. We are encouraged by the staff assessment that implementation of the additional policy measures would carry forward the policy reorientation introduced during the last year, and that the policy program adopted by Sudan could achieve its objectives. We share this assessment.

However, as noted by the staff and other speakers, there are considerable risks for slippages to occur, thus, there is the need for the Sudanese authorities to adhere firmly to the agreed policy measures and to reinforce them, as necessary, in order to sustain their adjustment efforts. After the early difficulties, the Sudanese authorities have come a long way in addressing the deep-seated macroeconomic and structural imbalances confronting their economy. The road to financial equilibrium and sustainable growth will not be an easy one, and the authorities will need to be patient in their efforts, and the proper coordination and sequencing of policies will be essential. In this regard, we agree that at this juncture, a high priority should be accorded to reducing inflationary pressures in the economy and creating an environment that fosters private sector confidence and promotes private sector participation in economic activities.

Reducing the inflation rate to a level consistent with the medium-term objective will require implementation of tight fiscal and monetary policies to rein in domestic demand. In this context, the authorities' commitment to limit the Government's domestic borrowing requirement is noteworthy. Moreover, their intention to introduce financial instruments bearing realistic interest rates is also welcome.

I will not dwell any longer on the commendable and courageous measures taken by the authorities regarding the exchange system, pricing policies, and the rationalization of the budgetary process, as others have done so already. In general, we share the staff's view that "the new policy undertakings represent a major reorientation of economic policy toward the correction of economic imbalances and the removal of structural bottlenecks." Like the staff, we are satisfied that Sudan is cooperating with the Fund with regard to policy implementation.

Sudan's payments record to the Fund should be assessed against the very difficult circumstances facing Sudan. Indeed, the external position continues to be under severe pressure, as export receipts declined further in 1991/92, while external assistance continued to contract. Moreover, the debt-service obligations have risen to 300 percent of external current account receipts in 1991/92. Nevertheless, in view of the actual payments to other creditors, we urge the Sudanese authorities to increase and maintain regular payments to the Fund.

We are very much encouraged by Ambassador Abdallah's statement on the effort and commitment of the Sudanese authorities to reform their economy. Therefore, we support the proposed decisions, in particular the decision on the provision of technical assistance and on the review of the overdue financial obligations to the Fund. The latter decision provides enough time for the authorities to develop further their adjustment program. We encourage them to take advantage of the extension of the availability of the rights approach to establish a good track record in order to enter soon into a rights accumulation program.

Mr. Végh made the following statement:

I endorse the staff appraisal, and support the proposed decisions. This chair welcomes the recent reorientation of economic policies in Sudan, implying a shift away from interventionism and controls toward allowing a freer operation of market forces and expanding the role of the private sector. Particularly important are the actions taken in the areas of fiscal policy, price liberalization, investment deregulation, and the exchange system. However, in a subsistence economy heavily dependent on weather conditions, suffering from a severe debt overhang, and with a high proportion of the population living in extreme poverty, these changes represent just the beginning of the path toward the resolution of the country's serious and deep-rooted problems. Consequently, more profound and comprehensive measures are needed to secure the success of any stabilization and reform effort.

The most pressing policy challenge in the short run is the correction of the major macroeconomic imbalances, particularly in the public and external sectors. The accrued overall deficit of the Central Government is expected to be 26 percent of GDP during the present fiscal year. Correspondingly, the fiscal deficit would be 1.3 times greater than the total flow of expected revenues if full forgiveness of the public debt were granted and no interest service was performed. This clearly reflects the unsustainability of the present fiscal situation and its spillover effects into monetary policy and inflationary pressures.

The improvement of the public finances requires a major effort in the mobilization of resources through the tax system, by improving tax administration and by imposing--or increasing--less distortionary taxes, such as sales and tangible wealth taxes. The latter seems particularly suitable for Sudan, given the predominance of agricultural activities. Privatization of unprofitable public enterprises may also contribute to this purpose. On the expenditure side, it is critical to cut unproductive expenditures. The significant increase in budgeted defense outlays runs against this objective and, most important, has a huge social opportunity cost. Furthermore, subsidies to electricity and water consumption are being kept. Given that these subsidies constitute a small proportion of total expenditures, they might be eliminated completely, unless there are efficiency considerations against that. It might be noted that such subsidies mainly benefit the high-income groups, which are the largest users of these utilities. I would appreciate some comments from the staff on those points.

The correction of the external imbalances requires the setting in place of an efficient structure of incentives through--essentially--the adjustment of relative prices of tradable goods. This has become crucial given Sudan's urgent need to improve rapidly its ability to service its foreign debt. At the same time, it is by now evident that it is impossible for Sudan to escape the "debt trap" without a substantial forgiveness of its foreign debt obligations.

I share the disappointment expressed by other Directors--particularly by Mrs. Krosby and Mr. Goos--about Sudan's payments performance to the Fund. We are indeed very far from the minimum target that has been established in other cases of stabilizing the volume of arrears. Furthermore, as Mr. Goos has suggested, the situation has deteriorated since the Board's consideration in March 1992 of Sudan's overdue financial obligations to the Fund, and the commitment of the authorities today is less ambitious than that expressed on that occasion. The staff's explanation of this matter leaves me rather uneasy, because it means that there is a lack of support from the governments of the major countries and other international institutions to help find a solution to Sudan's arrears problem with the Fund. This means that, in practice, our status as preferred creditor is not recognized, and our risk exposure increases. I have referred to this problem in the context of financing assurances of Fund-supported programs in the Eastern European countries, where our institution is assuming the main burden regarding up-front financing, while the commitments of other international institutions and official bilateral donors are not fulfilled. This has a consequence of leading to a further deterioration in the quality of the Fund's portfolio. I call the attention of the Executive Board to this matter.

Mr. Martínez-Alas stated that earlier in 1992, the Sudanese authorities had initiated a long-overdue process of adjustment. More recently, they had taken some additional measures aimed at arresting the sharp deterioration of the economy. Although those measures were steps in the right direction, the current situation and prospects were not yet totally satisfactory. He welcomed the authorities' intention to implement a comprehensive and far-reaching adjustment program in close consultation with the staff. He was confident that, upon the correction of the unsound economic policies that had been applied until recently, the Sudanese economy would begin on a long process of recovery. The road to steady growth and external viability was paved with painful and rather unpopular measures, but it would be in the best interests of the Sudanese people to take them. He was glad to see that the Sudanese authorities understood the importance of implementing a comprehensive economic adjustment program.

Sudan's overdue obligations to the Fund were a matter of great concern, Mr. Martínez-Alas concluded. He regretted that the Sudanese authorities had made only a small payment on their overdue obligations. He urged the authorities to resume their payments on current maturities. In light of the efforts made by the Sudanese authorities, he could support the proposed decisions.

Mr. Fridriksson made the following statement:

It is now more than six years since Sudan was declared ineligible to use Fund resources, and the arrears to the Fund have reached an extremely high level however they are assessed. Recently, there has been a change in the Sudanese authorities' attitude toward the Fund, and a number of important economic reform measures have been implemented. I note in particular the improvements in pricing policies and in the exchange system, and the elimination of most budget subsidies. My authorities very much welcome this development. I also welcome the information contained in Mr. Monyake's statement about the Government's intentions to intensify the adjustment effort, as well as the statement to the same effect by His Excellency the Ambassador.

However, not much has changed as far as payments performance vis-à-vis the Fund is concerned. Sudan continues to make only token payments to the Fund, whereas debt to a number of other multilateral creditors continues, by and large, to be serviced. Apparently, no significant change in this policy is envisaged in the near future, as the scheduled monthly payments to the Fund are far below what I would consider to be the minimum in the circumstances. The Sudanese authorities' continued disregard for the Fund's preferred creditor status is unacceptable, and a substantial increase in payments to the Fund must be a prerequisite for the possible consideration of a rights accumulation program.

Although they are steps in the right direction, neither the policy measures already taken nor those envisaged for the near future are in themselves sufficient to qualify Sudan for a rights accumulation program. I strongly encourage the authorities to come to an agreement with the staff as quickly as possible on a monitoring arrangement that could lead to a more comprehensive program, thus meeting the requirements of the rights approach within the time schedule envisaged in the paper on supplementary information. A rapid move toward a credible program is essential if external financial assistance is to be mobilized.

I can support the proposed decision, including the provision for technical assistance. However, while the last sentence of paragraph 2 of the decision states that payments to the Fund sufficient to prevent the overdue obligations of Sudan from increasing further would be an essential element of a rights accumulation program, I would regard payments of that magnitude to be an absolute minimum requirement.

Mr. Finaish made the following statement:

During the Board's review of Sudan's arrears to the Fund five months ago, a number of Directors characterized the authorities' policy efforts and intentions as providing a glimmer of hope that the turnaround in Sudan had finally begun. We are heartened to see this glimmer brighten considerably since that time. By following through on the policies they had initiated in late 1991 and early 1992, and by showing readiness to adopt further difficult measures when needed--as they have done recently--the authorities have demonstrated their commitment to the corrective course they have charted, and which Sudan badly needs. For this, the authorities deserve our full commendation. We also commend the staff for its dedicated and constructive efforts. Of course, there should be no illusions about the long and difficult road ahead, given the depth of Sudan's economic decline over the past decade. Indeed, it is important to guard against unrealistic expectations about the impact of corrective measures, at least in the short term. By the same token, there are indications that the liberalization measures, including in the exchange system, pricing, and other areas, have already begun to influence economic performance positively. The hope is that policy reform and confidence rebuilding will reinforce each other in a virtuous circle, thus accelerating the pace of economic recovery.

There is no doubt that a strengthening of the fiscal position is crucial if the authorities are to succeed in bringing down the rate of inflation. This is particularly so given the liberalization of the exchange market and the need to have positive rates of return on Sudanese pound deposits. We are therefore pleased to note the staff assessment that the authorities' fiscal target for 1992/93 can indeed be achieved on the basis of measures recently adopted. We welcome in particular the authorities' intention to limit expenditures to 80 percent of budgeted levels in the first half of the fiscal year, in an effort to reduce the borrowing requirement below the ceiling of 36.8 percent of the beginning money stock. The planned midyear reassessment of the fiscal position is important, especially in light of the experience of the last fiscal year, where the implications of exchange rate and pricing measures do not seem to have been taken fully into account.

With respect to monetary policy, the staff has emphasized the need to have positive rates of return on financial assets. A strict implementation of fiscal adjustment should go a long way in achieving this objective, by bringing the rate of inflation down. But the excess liquidity in the banking system is also a problem that needs to be addressed if macroeconomic stabilization is to succeed. More generally, reform of the financial sector and the interest rate structure deserves emphasis. In this regard, we have noted the authorities' request for Fund technical assistance to help in the establishment of a market for debt instruments. We believe that the Fund should respond positively to this request, as well as to the request for assistance in the area of exchange reform.

Although the staff has not been able to provide medium-term balance of payments projections given the many uncertainties that still exist, there is no doubt that Sudan's external position will continue to be very weak for a long time to come. While the positive effect of reform on the external position will materialize only gradually, it is likely that in the short run, the balance of payments may actually weaken as a result of some of the liberalization measures. It is therefore important that the design and sequencing of policies take fully into account the impact on the external position, as well as on the fiscal position.

Regarding the issue of Sudan's arrears to the Fund and the Fund's role in Sudan in the period ahead, we can generally endorse the main elements of the approach proposed by the staff, namely, to have a staff mission proceed very shortly to Sudan to agree with the authorities on the targets and benchmarks of a transitional program for the remainder of the year to be monitored by the staff. This could be achieved rather quickly in light of the information and assessment provided in the supplement. The Fund would also provide Sudan with the requested technical assistance in the areas of exchange reform and the development of domestic debt instruments. The Fund should stand ready to provide technical assistance in other areas as well, if the need arises. The Fund should also help the authorities formulate a medium-term adjustment and reform plan which could form the basis for a rights accumulation program perhaps in the first half of next year, and assist in catalyzing the financing requirement under such a program.

In addition to the financing plan which needs to be worked out under a rights accumulation framework, and which will clearly require enormous and imaginative efforts, a more immediate question relates to the financing needs in the interim period. The availability of external support will not only affect the authorities' ability to sustain--and, indeed, to strengthen--their policies, but would also help Sudan increase its payments to the Fund beyond the planned amounts. The question is whether the Fund can play a catalyzing role at this stage. I believe that the answer is "yes." A public endorsement by the Fund of the authorities' efforts, as Mr. Monyake has noted, would help to catalyze the much-needed assistance, while creating a favorable political environment for further reform within the country itself. I understood this to emphasize the importance of such a public endorsement for the authorities inside the country itself, because reform and the taking of difficult measures sometimes are not supported by everyone. A public statement would strengthen the hand of those who are willing to take difficult measures in Khartoum.

His Excellency Ambassador Abdallah and Mr. Monyake have suggested that the declaration of noncooperation be lifted. In terms of policies and performance, I believe that there is a good justification for such an action. However, to the extent that some Directors may consider Sudan's payments record as precluding the lifting of the declaration of noncooperation, the positive turn in relations between Sudan and the Fund should at least be given as much publicity as possible. The Board's decision which will be taken today can be considered as providing such publicity, but I believe that it would also be useful for management to communicate directly to the Governors of the Fund, collectively or selectively, as well as with the heads of relevant international and regional organizations, to brief them on developments with respect to Sudan.

The Sudanese authorities have a long and difficult road before them. In their recent actions, they have demonstrated their recognition of what needs to be done, and the courage to do it. We encourage them to persist on their corrective course, and we hope that the domestic and external circumstances of Sudan in the period ahead will be conducive to further progress.

Regarding the proposed decision on arrears, I suggest a small addition to paragraph 3. At the end of the second sentence, and after the phrase " ... comprehensive adjustment program," we would replace the period with a comma and add "... that could form the basis for a rights accumulation arrangement."

Mr. Wei made the following statement:

The Sudanese authorities have continued to implement a comprehensive adjustment program since the Board reviewed Sudan's overdue financial obligations to the Fund in early March 1992. The authorities have adopted a number of bold policy changes which demonstrated their determination and firm commitment to address the economic problems of the country. The important policy initiatives included the adoption of a free float for the Sudanese pound in the context of the unification of the exchange rate system, the abolishment of all price controls for all goods and services, and the elimination of subsidies for bread and sugar. The authorities did all this under very difficult circumstances--severe drought, a decrease in export earnings because of the unfavorable terms of trade, and the sharp fall in external assistance. We are pleased to note that these policies have begun to bear fruit, and that the country achieved real output growth of 9.6 percent for 1991/92--remarkable when compared with that of many other African countries. We are in broad agreement with the staff's appraisal.

We urge the authorities to stand firm with regard to the policy measures included in the current adjustment program. On fiscal policies, strict control of expenditures should be maintained in order to keep the Government's domestic borrowing requirement within the target. Meanwhile, the authorities are encouraged to adopt enhanced measures on revenue mobilization. On monetary policies, the authorities should emphasize a comprehensive reform of the financial sector. The central bank should make every effort toward the eventual lifting of the present credit restrictions, and the utilization of indirect instruments to control the money supply. The authorities should continue to implement a tight financial policy to reduce the inflation rate, which is very high at present.

We fully understand that the country is confronted with serious economic problems, which it is impossible for the authorities to address in a short period of time. Instead, they should be addressed in a long-term strategy. In this regard, it is very important that the authorities be encouraged to cooperate closely with the Fund in the design of the broad ten-year program which is to succeed the present three-year National Salvation Program.

The Sudanese authorities have strongly committed themselves to the adjustment efforts, and they are doing what they can to pay the overdue obligations to the Fund. Although the payments they have made are small in the total amount, the Government reaffirms that it would honor all its overdue obligations to the Fund. What the authorities are requesting is a realistic period of time in which they will be able to increase their payment through a Fund-supported program. Therefore, we support the proposed decisions, and strongly urge the resumption of the Fund's technical assistance to the country. I also associate myself with the proposals of Messrs. Finaish and Goos regarding the publicizing of the efforts of the Sudanese authorities to adjust the economy. Such publicizing would be beneficial for both the Fund and Sudan.

Mr. Prader made the following statement:

Since our meeting in March 1992, the Government has formulated a set of macroeconomic policy actions aimed at durably reducing inflation, beginning with a major fiscal adjustment supported by tighter monetary policies and a deepening of Sudan's domestic financial markets. This program is consistent with the authorities' policies aimed at the correction of imbalances and the removal of structural bottlenecks. The targeted borrowing requirement in the 1992/93 budget program seems ambitious, particularly with respect to inflation. I agree with the staff that it is time to reduce inflationary pressures, but I would also like to stress the importance of ensuring the attainability of the budget targets by promptly implementing well-prepared measures in the complementary areas of fiscal, monetary, and incomes policy, which would be aimed at mobilizing revenues, rationalizing expenditures, eliminating subsidies, and terminating financial support to public enterprises.

From a review of the present initiatives and new information on plans for additional adjustment measures, it appears that the authorities have covered all the elements needing priority attention. These policies, aimed at significantly reducing inflation and reforming the exchange system, follow the Fund's usual recommendations for countries following stabilization programs.

We therefore support the proposed decision, to the effect that the adopted and planned measures make it unnecessary at present to press forward with the procedures leading to Sudan's compulsory withdrawal. We also support the Sudanese authorities' request for technical assistance and the staff's plan for informally monitoring Sudan's macroeconomic policies and payments performance vis-à-vis the Fund in the first half of the present fiscal year. Both the technical assistance and the monitoring process will sustain and reinforce the authorities' adjustment efforts and help Sudan to begin to establish a track record, correct its financial and external imbalances, and eliminate structural weaknesses.

Although the targeted domestic borrowing requirement of the Government in the 1992/93 budget is broadly consistent with present revenue and expenditure estimates--and, if attained, should generate the positive expectations needed to carry Sudan through the anti-inflation efforts of coming years--I have doubts about whether it can be achieved this year, given the state of policy preparation, the absence of external economic assistance, and the present need for Sudan to obtain a growing share of its oil imports through commercial channels.

The targeted reduction in the Government's borrowing requirement in 1992 depends critically on the success of several major revenue initiatives. Spending restraint seems limited to preventing the GDP share of public spending from exceeding its high level of 1992. Since the tax acceleration is a one-time-only measure, the durability of the revenue gain is questionable, unless comprehensive reforms are quickly initiated in the areas of tax administration and the collection of existing tax liabilities. The reforms must be comprehensive, since a piecemeal approach will simply add to the system's inefficiencies, rather than resolve its fundamental problems of tax inequity, skewed resource allocation, and financial market distortions.

In general, the 1992/93 government borrowing requirement target seems exposed to two important uncertainties. First, neither the projected revenues from direct taxes--in particular, income taxes--nor the nontax revenues from the sales of capital assets are likely to materialize particularly swiftly, and thus they will probably fall well short of expectations. Would the staff care to comment on this issue? Second, the difficulties of curbing inflation's momentum during a period of price decontrol, sharp upward adjustments of administered prices, and exchange rate adjustments, suggests that inflation will not slow down as quickly as the authorities expect. This, in turn, will put pressures on public spending.

We strongly urge the authorities to anticipate these fiscal problems and to take early corrective action. We also strongly urge the authorities to introduce government securities with market-related rates of return, a move which would go a long way toward breaking down inflationary expectations.

While we recognize their fundamental changes in economic policy, we must take exception to the Sudanese authorities' present payments policy toward the Fund--which is simply unacceptable. Therefore, we must insist that any consideration of a rights accumulation program or any public indication that such consideration is imminent would be premature. Given the great changes that have taken place in the world in recent years, and the country's need to obtain assistance from external donors, Sudan would have been forced to change its economic policies even if there had been no problem with the Fund concerning payments. We ought not to consider the present changes in economic policy as a concession to the Fund that is sufficient to compensate for Sudan's unacceptable payments record.

Mr. Goos commented that his proposition was that the Fund recognize publicly the adjustment efforts and reorientation of the economic policy stance of the Sudanese authorities under difficult circumstances. However, he would not wish to suggest that those efforts were in themselves sufficient to allow the Fund to offer Sudan a rights accumulation program, as the Sudanese authorities had not yet fulfilled the requirements for satisfactory cooperation with the Fund. In its public announcement, the Fund could specify what the next steps would be that could lead to the adoption of a rights accumulation program.

Mr. Prader said that he could accept Mr. Goos's proposal, provided that the public announcement made it clear that Sudan's payments performance vis-à-vis the Fund was unacceptable.

Mr. Mirakhor said that he could see no reason to object to the Fund's making a public pronouncement on the progress made by the authorities. He believed that there was a precedent for such a step, and that the international community ought to be informed of what had been achieved.

Mr. Knight made the following statement:

We can join others in welcoming the range of policy initiatives that have either been undertaken or are proposed to be taken by Sudan over the next few months. If fully implemented, they suggest that the authorities may now be serious about digging the economy out of its very deep hole.

The policy efforts required during the proposed four-month monitoring period are necessarily demanding. We hope that the authorities will endeavor not only to meet them, but to go beyond the initial understandings. If that occurs, the authorities might then be in a position to work out with the staff a comprehensive medium-term program aimed at bringing about eventual economic recovery.

As the staff report notes, and as other speakers have emphasized, the list of areas for reform is a very long one. It is evident that Sudan needs a fundamental change in its entire economic management approach. It needs to renounce its interventionist philosophy. It needs to scale back the omnipresent public sector and promote the development of private enterprise. It needs to embrace fiscal discipline, the lack of which has been the major cause of economic destabilization. It also needs to develop an effective monetary policy embodying positive real interest rates.

Having said this, we also recognize that the task facing the authorities is such that the Fund should be prepared to provide the necessary technical assistance to ensure the best possible chance of rehabilitation now that the authorities have expressed a commitment in that direction.

On the question of arrears, I listened carefully to the comments by Ambassador Abdallah and the staff representative, but would like to pursue one particular point.

At the Board discussion on Sudan in March of this year, I raised questions about the nature of collaboration between the Fund and the Bank on payment of arrears. It seemed quite inappropriate to me that Sudan should be current with the World Bank, while being so persistently in arrears with the Fund that we were seriously contemplating an end to Sudan's Fund membership--a step that would presumably also affect its membership of the Bank.

That situation appears to have changed very little since March. According to Appendix III of the staff report, Bank disbursements over the next two years are expected to total $120 million while, under the repayment arrangements now proposed, a total of $6 million is to be repaid to the Fund over the next 12 months, with no undertakings beyond that. I have two specific questions directed to the Bank as well as to the Fund, and I would be glad to hear from the Bank representative present.

First, have there been discussions with the World Bank on this matter, and if so, does the Bank consider its pattern of planned disbursements to be appropriate to a country the Fund membership of which is threatened through nonpayment of arrears?

Second, bearing in mind the codependent membership and the mutual obligations imposed by the Bank/Fund agreement on collaboration, can I ask what action, if any, the Bank has taken to secure repayment of Sudan's arrears to the Fund?

Ms. Lindsay-Nanton made the following statement:

At the last Board review in March 1992, this chair was emphatic in stating that, based on an assessment of the facts presented, Sudan had not attained the critical mass of measures needed to change its status from one of noncooperation to cooperation with the Fund. Moreover, we believed that the package of measures adopted by the authorities, while representing a change of attitude, fell short of the comprehensive program of economic and financial reforms needed to bring about economic adjustment in the context of Sudan.

Today, there is some basis on which to embark on a process of normalization of relations between Sudan and the Fund, in view of the policy actions taken since the last review and the new understandings that have been reached between the staff and the authorities--which I welcome.

Moreover, I would like in particular to commend the staff for its perseverance and diligence in maintaining that dialogue, which has proven to be productive and which has brought us to where we are today.

Having said this, however, the risks in the circumstances of Sudan remain high. Moreover, while one welcomes the recent reorientation of economic policies, the economic measures adopted since the last review, and the authorities' intention to implement further adjustment measures, one cannot help but express regret over the authorities' failure to settle their overdue financial obligations to the Fund, on which so much now depends, in a timely manner.

The staff is correct in emphasizing that the Government's policies at this time should aim at reducing inflation, encouraging adequate incentives for the tradables sector, and creating a climate conducive to private sector confidence and initiative.

One welcomes the improved fiscal outlook for 1992/93 as presented in the staff supplement, compared with that projected at the time of the last Board review. We nonetheless concur with the staff that, if inflation is to be brought down much more quickly, the Government's recourse to the banking system would have to be curtailed beyond the targeted LSd 34 billion. We therefore endorse the staff's call for additional budgetary measures in order to strengthen fiscal consolidation further.

In this regard, one welcomes the recent adjustments in relative prices and action on the part of the authorities to bring domestic oil prices to world market levels, which have contributed to the elimination of all budgetary subsidies other than for public utilities.

There is a clear need for decisive action as regards monetary policy. The introduction of more realistic rates of return and charge on financial instruments is imperative if the financial system is to be strengthened. We therefore welcome the authorities' commitment to introduce government securities with realistic rates of return by year-end at the latest. The authorities' intention to seek technical assistance with a view to rehabilitating the banking sector is appropriate, and should be proceeded with as soon as possible.

The additional steps taken by the authorities to liberalize the exchange system early in June are in the right direction, as is the authorities' intention to move toward a more market-based system for determination of the exchange rate.

While the recent wide-ranging economic reforms and the further new policy undertakings could only lead to a correction of economic imbalances and the removal of structural bottlenecks that have characterized the Sudanese economy for quite some time now, we continue to remain troubled by the authorities' payments performance to the Fund.

Admittedly, the continuation of the weaknesses in the balance of payments for a number of years, due in part to poor export performance, and the diminution of external assistance, have put extreme pressure on external reserves and have led to a further buildup of external debt payments arrears. Indeed, we have some sympathy for the authorities in seeking to ensure a minimum flow of financing from other creditors for the purchase of essential commodities in order to keep the economy functioning at a minimum level. However, although we welcome the recent payment made by the authorities last Friday, we are distressed that Sudan's payments fall far short of its overdue obligations to the Fund. Furthermore, we view the planned increase in payments on a monthly basis to total at least $6 million in 1992/93 as unsatisfactory, as overdue obligations will still continue to rise if payments are limited to this amount--and this despite the relief provided by the termination of special charges in the General Resources Account for members with protracted arrears.

The staff has demonstrated in Scenario B, Table 2 of the staff report that a further strengthening of policies--particularly in respect of fiscal action and additional measures to improve the functioning of the exchange system--could go quite a way to strengthening the balance of payments and assisting in the accumulation of reserves. I would therefore want to stress the importance for the authorities of adopting these additional measures, not only for strengthening the external account and reestablishing good relations with other creditors, but also in order for Sudan's payments to attain a level sufficient to prevent overdue obligations from increasing further--which is essential in view of the possible rights accumulation program, and if the declaration of noncooperation with the Fund is to be lifted.

At present, we believe that an informal monitoring arrangement is appropriate in view of the authorities' efforts toward furthering the normalization of relations with the Fund. Furthermore, such an arrangement would offer the Sudanese authorities an opportunity to establish a track record of policy implementation and performance, and help to improve the credibility of the recently adopted measures. In addition, the technical assistance being sought by the authorities, aimed at strengthening the financial sector and the exchange system, is justifiable, if Sudan is to arrive at a comprehensive adjustment program, and if the momentum of reforms undertaken thus far is to be maintained.

A start has been made by the Sudanese authorities in laying the basis for a comprehensive reform program, and thus initiating the process of normalization of relations with the Fund. However, this is only a start, as the distinguished Ambassador has correctly pointed out. The true test of the authorities' commitment to lasting economic adjustment will only be apparent when the additional policy actions are carried forward and the increase in overdue obligations to the Fund is stemmed. I can support the proposed decisions.

Mr. Meron made the following statement:

Like others, we welcome this staff report for the Article IV consultation, which shows that the Sudanese authorities have had a change of heart with respect to Fund surveillance and their own cooperation with Fund staff. At the same time, the report shows to what extent the Sudanese economy has been shackled through years of interventionism and control. In fact, much of the institutional framework for the operation of a market economy--such as a properly functioning financial system--does not exist, and needs to be established.

We are pleased to note that following a second round of talks with the Sudanese authorities which took place in Washington earlier this month, the staff now believes that the "targeted borrowing requirement in the 1992/93 budget is realistic and attainable and ... is consistent with the authorities' goal of achieving a significant reduction in inflation during the period." We note, however, that, as in its earlier appraisal, the staff recommends that the government borrowing requirement be further reduced to 25 percent of opening money stock, as compared with the 37 percent contained in the budget.

However, there has been no sign of change regarding Sudan's resumption of payments of obligations falling due to the Fund. Payments made to the Fund since the last review are only a very small fraction of obligations falling due. The additional payment that the staff announced at the beginning of this meeting is disappointing, and falls short of what the authorities had indicated during the discussions with the staff. Moreover, in contrast with Sudan's payment record to the Fund, Sudan has remained current in its payments to the World Bank, and has been making substantial payments to other international financial institutions.

Nonetheless, given the new circumstances, we could go along with the draft decision, and we support in particular the proposal to renew technical assistance to Sudan--a decision that should signal to the Sudanese authorities that the Fund is taking them at their word.

The staff representative from the Middle Eastern Department stated that the staff had had discussions with the World Bank on the particular circumstances of Sudan's making of payments to the Bank but not to the Fund. The staff had benefited considerably from the Bank's support, both in its discussions and in its missions to Khartoum. A broad policy framework had been laid down for the Fund and the Bank in handling each other's arrears cases, and it had been his understanding that the Bank had not breached them. The Bank had made no new commitments to Sudan over the previous few years, with the exception--in consultation with the Fund, and as reported to the Fund Board--of one drought recovery project that had been agreed in the summer of 1991, at the height of the food crisis. Moreover, the Bank had reiterated to the authorities the vital importance, both for Sudan and for its relationship with the Bank, of moving forward in resolving its arrears to the Fund. The Bank had downscaled its resident representative office in Khartoum partly in reaction to Sudan's arrears situation. It was expected that the Bank would appoint a new resident representative to Khartoum once the monitoring arrangement with the Fund had been agreed.

Mr. Knight commented that he recalled that the provisions on Bank/Fund collaboration specified particular actions that one of the institutions should take if a country's financial obligations to the other institution were not discharged.

The staff representative from the Policy Development and Review Department stated that the Fund staff had received the complete cooperation of the Bank staff in the case of Sudan. The Bank continued to make disbursements in the case of Sudan because the legal documentation underlying the relevant loans did not permit the Bank to suspend disbursements unless certain conditions related to overdues to the Bank were to occur, or related to nonperformance of project implementation and adherence to Bank procedures. The disbursements in question had all been for investment-type loans or projects, and not for policy-based lending. The Bank had also scaled back its operations in Sudan in reflection of the Fund's adoption of further remedial measures, by withdrawing its resident representative and making no new loan commitments except for humanitarian assistance. In his view, the Bank had acted fully in accordance with the principles of Bank/Fund collaboration.

The staff representative from the World Bank stated that Sudan was a member in good standing with the World Bank. Sudan's project implementation had improved, so the Bank had continued to disburse against previous obligations. The Bank staff had worked closely with the Fund during the period of Sudan's arrears to the Fund, and the necessity of resuming a cooperative relationship with the Fund had been a major element of the Bank's dialogue with the Government. The Bank would consider a monitoring arrangement agreed between Sudan and the Fund as a satisfactory macroeconomic basis for resuming some new investment lending, most likely in the agriculture sector.

Ambassador Abdallah stated that the relatively small amount of the payments that Sudan could make to the Fund was not an indication that the authorities disregarded the importance of payments to the Fund. The authorities recognized that the payments represented only a token amount, but the situation in Sudan simply did not permit payments that were higher. To make a commitment to do any more would be to make a promise that the authorities knew they would not be able to keep.

Most of the policies that had been put in place were intended to encourage production in, and the productivity of, the agriculture sector, which was the key sector in Sudan, the Ambassador pointed out. The result had been an encouraging rate of growth in the agriculture sector in the previous year. It had been essential to extend short-term credits to the sector in order to pay for the investments needed to increase agricultural production and thereby, exports and foreign earnings. The Government had therefore been unable to meet all of its arrears.

Even if Sudan stopped paying the estimated $26 million due to the World Bank, the African Development Bank, and the OPEC Fund for International Development in fiscal year 1992/93, and paid it to the Fund, not only would Sudan still remain far behind in meeting its obligations, but it would be unable to finance the agricultural inputs and other imports that were key to a minimum level of economic viability, the Ambassador stressed. Moreover, aside from the organizations he had just mentioned, Sudan was receiving no external financial assistance. The authorities believed that their only course at present was to pour investment into the agriculture sector, in the hopes of stimulating agricultural production and growth in the rest of the economy as well.

If Sudan's exports--and thus its foreign receipts--increased, and if some external assistance were forthcoming, then the authorities would be committed to increasing their payments to the Fund, the Ambassador stated. The likelihood of that occurring should be known later in the year. The authorities were willing to repay the Fund, but they depended upon the ingenuity and imagination of the Fund's staff, working together with them, to help them resolve the serious problems that confronted the country. In that connection, he wished to thank the staff for its diligent and outstanding efforts on Sudan's behalf. The authorities would work closely and cooperatively with the staff with a view to meeting the targets agreed under the monitored arrangement.

The authorities would take the critical comments that Directors had made very seriously, and they realized that those comments were meant to be constructive, the Ambassador concluded. He would like to urge the Fund to share its findings on the economic progress and prospects for Sudan with its sister organizations in the international financial community and with prospective donors, and in that connection, he would welcome any public disclosure or endorsement. The fact that Sudan had not been cooperating with the Fund in the past had been communicated to the Governors and to the international community at that time; now that Sudan had reoriented its policies and was taking steps to cooperate with the Fund, he hoped that those facts would likewise be communicated to the international community. Moreover, such a public endorsement would help those in the Government who were leading the drastic and unprecedented actions that were the first steps in a process of effecting a positive reorientation of the economy and the re-establishment of fruitful and mutually beneficial relations with the international financial community.

Mr. Monyake stated that he wished to thank speakers for recognizing the many positive achievements of the Sudanese authorities, and for having provided encouragement to them to persevere on the long and arduous road of economic reorientation. In a case like that of Sudan, taking into account the earlier bleak economic prospects and the long hiatus in performance and economic management, there was a great benefit--especially from the psychological point of view--in stressing the positive aspects of what had been achieved, even though it was clear that much more remained to be done. The Sudan had made commendable progress even in the absence of outside assistance.

He hoped that management and staff would work toward finding a solution to the problems of Sudan's arrears, given the reasons the Ambassador had outlined so eloquently as to why Sudan had not found itself in a position to pay, Mr. Monyake observed. Perhaps special consideration could be given to a program or mechanism under which Sudan might be able to make substantive payments to the Fund in the near future, including, inter alia, through meaningful external financial flows to Sudan.

He would suggest that paragraph 2 of the draft decision on overdue financial obligations be amended so as to omit the words "...and prompt...," as it was clear from the staff's analysis that prompt payment, albeit desirable, was impossible in Sudan's circumstances, Mr. Monyake concluded. He would also go along with Mr. Finaish's proposed amendment. Finally, he hoped that the Fund would not move in the direction of becoming the debt collector for the debts of other institutions. If the World Bank were to be asked to collect debt due to the Fund, the next step would be for the World Bank to ask the Fund to collect debt due to the World Bank; he believed that there was a danger in such reciprocity.

Mr. Knight stated that his understanding was that the agreement on Bank/Fund collaboration provided for the collection of debts owed one organization by the other organization--in fact, reciprocal debt collection.

The Acting Chairman made the following summing up:

Executive Directors welcomed the wide range of economic and financial measures adopted by the Sudanese authorities since the last consultation. It was noted that the emphasis of the recent reforms was on liberalizing the economy and enhancing the role of the private sector, and thus marked a much-needed reorientation of policies. Notwithstanding the positive character of the recent measures, Directors believed that those actions had to be viewed in the context of the enormous adjustment challenges confronting the authorities. From that perspective, it was stressed that firm and sustained implementation of the recent reforms, combined with a broadening and strengthening of the adjustment strategy over a number of years, would be essential for restoring confidence, redressing the very large domestic and external imbalances, and building a basis for an eventual normalization of Sudan's relations with the Fund. At the same time, Directors expressed disappointment with Sudan's poor record of payments to the Fund.

For the immediate future, Directors saw a compelling need for strong and supportive financial policies as a means of underpinning the recent introduction of economy-wide market pricing, the liberalization of the exchange and trade regime, and the movement toward a more market-determined and realistic exchange rate. In that regard, Directors recognized that the budget had become more transparent and that a significant improvement in the underlying fiscal position had been achieved. Nevertheless, inflation was likely to remain high. Hence, Directors urged Sudan to take additional measures to strengthen fiscal revenues and contain expenditures--including, in the view of some speakers, cuts in the unsustainably high level of military outlays--and to tighten control over other current expenditures. Directors stressed the importance of reducing the Government's prospective borrowing requirement in order to achieve a more rapid improvement in price performance.

Directors also emphasized the importance of the authorities' plans to introduce government securities carrying realistic rates of return as a supplementary means financing the budget deficit and to signal the Government's commitment to increased rates of return and charge. More realistic rates of return and charge to reflect the underlying inflation rates were seen as taking on greater urgency in view of the lifting of controls and restrictions on most current and capital transactions, and given the need for Sudan to attract and retain capital.

There was a broad consensus among speakers that the recent encouraging policy reorientation should be broadened and strengthened to become a comprehensive and mutually reinforcing set of policies developed in a medium-term context and implemented in a sustained manner. This would involve, inter alia, the abolition of remaining internal controls and features of a command economy. Fiscal policy would need to play a key role in reducing inflationary pressures and easing the external constraints, and would need to involve a significant cutback in the role of the government sector. The financial sector was in urgent need of reform to facilitate efficient financial intermediation and to make it possible for the authorities to conduct an effective monetary policy.

Directors considered that Sudan's payments performance continued to be poor. Moreover, present prospects regarding payments to the Fund over the coming 12 months implied that payments would continue to fall well short of obligations falling due. Accordingly, most speakers urged Sudan to increase its proposed payments to the Fund to a level sufficient to prevent overdue obligations from increasing further; it was stressed that the latter would constitute an essential element of a possible rights accumulation program.

Directors welcomed the intention of the staff to move expeditiously to set up, in consultation with the Sudanese authorities, a framework for monitoring informally Sudan's macroeconomic policies and payments performance vis-à-vis the Fund in the first half of Sudan's current fiscal year (July-December 1992). Such an arrangement was seen as offering Sudan the opportunity to begin establishing a track record of policy implementation and payments performance, while allowing the time necessary to put in place the structural and institutional reforms needed to form part of a comprehensive medium-term-oriented program that could pave the way to a possible rights accumulation program, as well as to the resumption of external assistance at higher levels. Directors considered that the provision of technical assistance by the Fund to Sudan in support of the authorities' adjustment efforts would be both appropriate and supportive of an eventual regularization of Sudan's relations with the Fund. It was expected that the next Article IV consultation with Sudan would be held on the standard 12-month cycle.

The Executive Directors took the following decision:

1. The Fund takes this decision relating to Sudan's exchange measures subject to Article VIII, Sections 2(a) and 3, and in concluding the 1992 Article XIV consultation with Sudan, in the light of the 1992 Article IV consultation with Sudan conducted under Decision No. 5392-(77/63), adopted April 29, 1977, as amended (Surveillance over Exchange Rate Policies).

2. Sudan maintains a restriction on payments and transfers for current international transactions as described in SM/92/130, in accordance with Article XIV, Section 2. In addition, Sudan retains restrictions on payments and transfers for current international transactions, including those evidenced by external payments arrears and bilateral payments agreements, that are subject to Fund approval under Article VIII, Section 2(a), as well as multiple currency practices subject to approval under Article VIII, Section 3.

3. The Fund welcomes the unification of Sudan's official and commercial bank exchange markets. The Fund urges the authorities to eliminate the above-stated restrictions and multiple currency practices and to terminate the bilateral payments agreement with a Fund member, as soon as possible.

Decision No. 10104-(92/100), adopted
August 3, 1992

The Executive Directors then considered the proposed decision on the overdue financial obligations.

Mr. Goos stated that, with respect to the suggestion from Mr. Monyake to remove the reference in the second paragraph of the proposed decision to the prompt payment of arrears to the Fund by Sudan, he would hesitate to weaken the message regarding repaying the Fund, even though--in Sudan's case--such prompt repayment was unlikely.

Mrs. Krosby said that she agreed with Mr. Goos. Moreover, in order to highlight the positive, it was sometimes necessary to mention the negative--which was what the formulation of that paragraph as proposed by the staff had done, in her view. The reference to the need to repay the Fund promptly should therefore be retained.

Mr. Wright and Mr. Végh said that they agreed with Mrs. Krosby and Mr. Goos.

Mr. Végh said that, on a related issue, he believed that the Fund should not provide any public indication of its support for the authorities' measures and policies, without at the same time remarking on the insufficiency of Sudan's payments performance and the question of the Fund's preferred creditor status. Therefore, he would support instead making public the Acting Chairman's summing up and the texts of the Board decisions.

Mr. Mirakhor, supporting the proposal put forward by Mr. Finaish to amend the third paragraph of the decision to note that the implementation of further adjustment measures could form the basis for a rights accumulation program, stated that that idea was already incorporated in the Acting Chairman's summing up, and that it was indeed the consensus of the Board. It constituted one of the most important elements of the staff's recommendations, and it would serve as an encouragement to the policymakers in Sudan to follow up with their plans to strengthen their strategy and policy stance.

Mr. Wright commented that accepting Mr. Finaish's proposed amendment might run the risk of raising unjustifiably the authorities' expectations. However, he could support Mr. Finaish's suggestion if the sentence were to read instead: "[t]he Fund also welcomes the authorities' intention to implement, in consultation with the staff, further adjustment measures in the near future with a view to the adoption of a comprehensive adjustment program which, if strictly adhered to, and with greatly improved payments performance, could form the basis for a rights accumulation program."

Mr. Prader said that he could support Mr. Wright's compromise proposal, provided that the sentence referred to the necessary improvement in the payments record.

Mr. Mirakhor said that it appeared to him that qualifying the sentence in the way that Mr. Wright had proposed was redundant. The sentence already laid particular stress on the fact that the adoption of a comprehensive adjustment program would need to be implemented in close consultation with the staff.

Mr. Wright observed that the prerequisite for a rights accumulation program clearly went beyond the adoption of a comprehensive adjustment program; rather, it included improved payments performance, which should therefore be reflected in the wording of the decision.

Mrs. Krosby said that she agreed with Mr. Wright.

Mr. Finaish remarked that he would prefer that his proposal stand as it was, mainly for the reasons stated by Mr. Mirakhor. Moreover, it might be noted that his formulation stated that a comprehensive adjustment program could--could, not would--form the basis for a rights accumulation program. He believed that that would take care of Mr. Wright's concerns. In his view, the formulation was appropriately cautious already.

Mr. Goos suggested that Mr. Wright shorten his amendment, so as to refer only to the need for strict adherence to the program, which could then form the basis for a rights accumulation program. It was clear from the preceding paragraph of the decision that the authorities should increase their payments to the Fund in order to qualify for a rights accumulation program.

Mr. Fridriksson, Mrs. Krosby, and Mr. Wright said that they could support Mr. Goos's proposal.

The Executive Directors then approved the following decision:

1. The Fund has reviewed further the matter of Sudan's overdue financial obligations to the Fund in the light of the facts and developments described in EBS/92/120 (7/27/92).

2. The Fund notes the recent payments to the Fund by Sudan and regrets that these payments remain small in relation to obligations falling due and that the amount of Sudan's overdue financial obligations to the Fund has therefore continued to increase. The continuing nonobservance by Sudan of its financial obligations to the Fund places a financial burden upon other members and reduces the financial resources needed to help others. The Fund urges Sudan to make full and prompt settlement of the overdue financial obligations to the Fund. The Fund stresses that settlement of the overdue financial obligations to the Fund should be given the highest priority. The Fund notes the commitment of the Sudanese authorities to increase their payments to the Fund. In this context, the Fund emphasizes that payments to the Fund in amounts that would be sufficient to prevent the overdue obligations of Sudan from increasing further would be an essential element of a rights accumulation program for Sudan.

3. The Fund welcomes the recent reorientation of economic policies in Sudan, including the economic measures adopted by the Sudanese authorities since the last review. The Fund also welcomes the authorities' intention to implement, in consultation with the staff, further adjustment measures in the near future with a view to the adoption of a comprehensive adjustment program, which, if strictly adhered to, could form the basis for a rights accumulation program. The Fund is prepared to assist the authorities in this endeavor, and considers the provision of technical assistance to Sudan in support of efforts to formulate and

implement a comprehensive adjustment program to be appropriate. The Fund staff will monitor informally the authorities' program for the period July-December 1992.

4. The Fund will review the matter of Sudan's overdue financial obligations to the Fund again not later than four months from the date of this decision, in the light of actions taken by Sudan in the meantime in settling its arrears to the Fund and in adopting and implementing a comprehensive adjustment program.

Decision No. 10105-(92/100), adopted
August 3, 1992

The Acting Chairman said that Executive Directors needed to consider whether or not to recommend that the Managing Director send a letter to Governors and other institutions outlining the state of the relationship between Sudan and the Fund, indicating that the Board welcomed the recent policy measures, encouraging the authorities to continue with their policy reforms, and informing the authorities that the Board supported Fund technical assistance for Sudan and the development of a program for the informal monitoring of Sudan's performance during the rest of the year. The text of his summing up of the discussion could be sent as well, to provide background.

Mr. Shimizu stated that the Board's sense of disappointment regarding the level of Sudan's payments to the Fund needed to be incorporated in any such letter as well.

The Acting Chairman said that the fact that Sudan's payments remained inadequate would have to be included.

Mr. Filosa said that sending such a letter would be consistent with the practice that had been followed of warning the Governors when the policy implementation and payments performance of a member had been unsatisfactory. It was important that Governors be kept informed of recent progress. He could not support the making of a public statement by the Fund on that matter, however. He recalled that, at the time of the discussion of the wording for declarations of noncooperation, the Fund's General Counsel had stressed that the Fund could not make public statements about the quality of a country's policies; indeed, there was no such wording in any declaration of noncooperation. Therefore, a public statement to the effect that a member's policies had improved was plainly inappropriate as well. Moreover, the public might well wonder why the Fund was making such a public statement without simultaneously withdrawing the declaration of noncooperation.

Mr. Wright stated that he agreed with Mr. Filosa. A public statement would have an inherent risk of raising expectations that were unwarranted, especially given the nuances and technicalities that--while possible to include in a letter to Governors--would necessarily be lost in a public communication. Moreover, the Fund's intention was to send an encouraging signal to the authorities, and there was not much additional value to be gained from a more public pronouncement, in his view.

Mr. Mirakhor said that, as the Ambassador had noted, a public statement from the Fund endorsing the economic policy stance of the Government would encourage the catalyzing of political support inside the country for additional measures. He recalled that, in the cases of other countries, the Fund had endorsed the policy stance of the Government, but had noted that further measures would need to be taken, in a standard press release. He therefore did not believe that the Board would be contravening its usual procedures if it were to handle the case of Sudan in the same way.

Mr. Filosa said that he was unaware of any public statements by the Fund on the conclusion of Article IV consultations. Such a statement at the current juncture would be difficult to interpret. The important issue was whether or not, by way of a letter from the Fund to Governors and international financial institutions, the authorities would receive encouragement from their major creditors. A dangerous course would be set were the Fund to begin to make public statements with the object of encouraging political support in its member countries.

Mr. Wright commented that he recognized and understood the importance of mobilizing support within Sudan for the necessary economic measures. Were the Fund's letter to the authorities and to Governors to be made public within Sudan by the authorities, that objective might be achieved without requiring the Fund itself to take a public stance.

The Acting Chairman said there did not appear to be a consensus in favor of a formal public statement from the Fund. On an informal basis, however, the Fund's External Relations Department might, in response to questions raised by the press, note that the Board would review again the matter of Sudan's arrears to the Fund, and that the Fund had observed positive developments in policy implementation in Sudan in the recent past. That would not constitute a formal public statement, but it might provide important background information.

The Executive Directors concluded their discussion on Sudan.

2. REPORT BY MANAGING DIRECTOR

The Managing Director stated that, over the preceding two weeks, he had visited a number of countries, and he wished to inform Directors of the discussions he had had with the authorities.

In Fez, Morocco, he had participated, along with the President of the World Bank, in the Tidewater Meeting, an informal meeting of heads of international agencies on development issues organized by the Development Aid Committee of the OECD, the Managing Director said. The key topic of discussion had been how to be effective in maintaining international assistance while making a major effort in the Eastern European countries and the republics of the former Soviet Union. He and the President of the World Bank had informed the other agencies about the work being done in both regions by the Fund and the Bank.

He had been received by His Majesty King Hassan, the Managing Director continued. The King had reiterated his determination, and that of his Government, to keep the Fund-supported program on track. He had reaffirmed his commitment to the convertibility of the dirham and the full liberalization of the economy by the end of 1992.

He had then traveled to Nouakchott, Mauritania, on July 14, 1992, shortly after the first democratic elections in the country, the Managing Director said. The President had restated his commitment to sound economic policies and his determination to embark on a program of economic adjustment with the Fund's support. The President had hoped that the negotiations with the Fund on a program could be completed as soon as possible, and not later than September 1992. As only an agreement on the exchange rate had remained to be achieved, it had appeared that the negotiations could be completed fairly quickly. However, statistical information requested by the staff to monitor the situation following the discussions in mid-April 1992 was as yet unavailable, and it was therefore difficult to assess the program, which had been affected by recent developments. He had confirmed to the President that a Fund technical team would arrive in Nouakchott in July or August 1992 to help assemble and reconcile the necessary statistical data, thus paving the way for an early resumption of negotiations, which he hoped could be completed during the 1992 Annual Meeting. After meeting the President and the Prime Minister, he had met with the leaders of the opposition, with whom he had had a constructive dialogue.

He had accepted the invitations of several of the heads of state of countries in the franc zone to visit their countries, the Managing Director went on. He had taken that occasion to share with them the particular concerns he had had about the prospects of their economies and adverse developments affecting Fund-supported programs in a number of those countries, in spite of the authorities' meritorious adjustment efforts. Among those adverse developments were the dramatic decline in the prices of, and uncertain prospects for, agricultural primary commodities, the severe deterioration in the terms of trade, and the significant appreciation of the French franc against the U.S. dollar--the currency in which those countries' commodity exports were frequently denominated. He had taken the opportunity to remind his hosts of the views of the Executive Board regarding the economic strategy for their countries, as reflected in the Board review of CFA franc arrangements at Seminar 90/6 (11/5/90) and in Board discussions of individual country reports. He had drawn their attention to the consequences for the economic stability and prospects of their countries of the recent adverse developments, and he had stressed that those developments called for strengthening the adjustment effort in terms of, inter alia, public wages, the size of government, and farm prices.

He had recommended that a pragmatic approach to the maintenance of competitiveness be taken, as the existence of the franc zone was not tied to the fixity of the exchange rate, and the zone's reinforcement could require external monetary adjustment at a given moment, the Managing Director went on. The key features of an alternative strategy--implying a change of the exchange rate--would not imply that adjustment efforts should be lessened, but rather that those efforts might be more gradual, more effective, and more convincing for markets and foreign investors. Some common adjustment instruments could be implemented, as needed, without disrupting the basic standing principles of monetary integration that were common to all members of the zone. He had emphasized that the credibility of the adjustment efforts was the Fund's chief concern, and that those efforts must lead to sustained growth and external viability in the medium term.

His discussions with the heads of state had been particularly timely, as they had preceded the meeting of the leaders of the West African Monetary Union (WAMU) together with representatives of the BEAC, on July 29, 1992, to consider, inter alia, a report on competitiveness and the respective merits of internal and external adjustment, the Managing Director recalled. In that context, he had had informal discussions on July 15 with the President of Senegal, on July 16-17 with the President of Cote d'Ivoire, on July 17 with the President of Burkina Faso--currently the Chairman of the Council of Heads of State of the WAMU--on July 24 with the President of Cameroon, and on July 27 with the Presidents of Gabon and the Central African Republic--the latter of whom chaired the Central African Monetary Union.

The WAMU meeting in July had taken place in the context of intense speculation on the content of the agenda and on a possible devaluation of the CFA franc, the Managing Director concluded. The French authorities had been informed, at the highest level, of the conclusions of the meeting on July 31, 1992. The participants had decided to maintain the existing parity of the CFA franc relative to the French franc; they had indicated their willingness to reinforce their structural adjustment policies with the support of the Fund and the World Bank, and to deepen their regional integration through several specific measures. The Fund management took note of the communiqué and the recent developments, and welcomed the determination to strengthen adjustment policies and to move forward on the road to regional integration. The Fund would stand ready to start immediate discussions with the countries concerned as soon as they were made known to the Fund. The early announcement of strong adjustment measures, approved by the Fund, could be particularly desirable in calming speculation and reversing capital outflows. In such a context, immediate and strong monetary measures would be indispensable as an unquestionable first signal of determination to implement fully what had been decided.

The Executive Directors took note of the Managing Director's report.

DECISION TAKEN SINCE PREVIOUS BOARD MEETING

The following decision was adopted by the Executive Board without meeting in the period between EBM/92/99 (7/31/92) and EBM/92/100 (8/3/92).

3. ESTONIA - REPRESENTATIVE RATE FOR ESTONIAN KROON

The Fund finds, after consultation with the authorities of Estonia, that the representative exchange rate for the kroon against the U.S. dollar, under Rule O-2(b)(ii), is the rate obtained on the basis of the fixed relationship of the kroon to the deutsche mark and the representative exchange rate for the deutsche mark. (EBD/92/166, 7/28/92)

Decision No. 10106-(92/100) G/S, adopted
July 31, 1992

APPROVED: March 23, 1993

LEO VAN HOUTVEN
Secretary