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# INTERNATIONAL MONETARY FUND

## Minutes of Executive Board Meeting 93/154

10:00 a.m., November 5, 1993

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

| Executive Directors | Alternate Executive Directors |
|---|---|
| M. Al-Jasser | A. A. Al-Tuwaijri |
| M.-A. Autheman | |
| | J. A. Solheim |
| | J. Prader |
| | G. A. Heinen, Temporary |
| H. Fukui | S. Ishida, Temporary |
| | N. Prasad, Temporary |
| | K.-T. Hetrakul |
| | W. C. Keller, Temporary |
| A. Kafka | J. C. Jaramillo |
| | A. Chang Fong, Temporary |
| | A. Mozhin |
| | V. Y. Verjbitski, Temporary |
| | J. Papadakis |
| | E. Quattrociocche, Temporary |
| R. Marino | J. M. Burdiel, Temporary |
| | O. Kabbaj |
| | M. J. Mojarrad, Temporary |
| | B. S. Dlamini |
| D. Peretz | J. Dorrington |
| | O. Havrylyshyn |
| | J.-C. Obame, Temporary |
| | E. Wagenhoefer |
| | Y. Y. Mohammed |
| D. E. Smee | N. L. Laframboise, Temporary |
| | J. M. Abbott, Temporary |
| | J. B. Wire, Temporary |
| | M. W. Ryan, Temporary |
| | A. M. Tetangco, Jr. |
| | G. J. Mathews, Temporary |
| | S. C. McDougall, Temporary |
| | Wei B. |
| | Wang X., Temporary |
| A. G. Zoccali | A. F. Jiménez de Lucio |

L. Van Houtven, Secretary and Counsellor
S. L. Yeager, Assistant
R. I. Vera-Bunge, Assistant

Also Present

IBRD: S. H. Choi, Secretary's Department; K. B. Jordan, African Regional Office; J. B. Sokol, Latin America and the Caribbean Regional Office. External Relations Department: M. R. Kelly, Deputy Director. Legal Department: H. Cisse, P. De Boeck. Middle Eastern Department: P. Cashin, H. Ghesquiere, M. D. Knight, A. Salehizadeh, R. A. Valdivieso, J. F. Wilson. Policy Development and Review Department: T. Leddy, Deputy Director; R. Danielsen, L. D. Everaert, J. P. Pujol. Secretary's Department: E. Friis, G. Djeddaoui, R. S. Franklin. Treasurer's Department: W. J. Byrne, J. C. Corr, Z. Farhadian-Lorie. Western Hemisphere Department: M. E. Bongelino, A. J.-P. Feler, M. Hosen, C. M. Loser, L. Schmitz, G. Yadav. Office of the Managing Director: H. Wiesner, L. A. Wolfe. Advisors to Executive Directors: S. K. Fayyad, T. K. Gaspard, J. Jamnik, M. F. Melhem, R. Meron, R. Rainford, A. Törnqvist, J. W. van der Kaaij. Assistants to Executive Directors: S. Al-Huseini, R. N. A. Ally, T. Berrihun, A. Cathcart, D. Desruelle, M. Dzervite, S. S. Farid, L. Fontaine, A. Galicia, H. Golriz, N. P. Hahnemann, C. Imashev, T. Kanada, T.-M. Kudiwu, K. J. Langdon, C. F. Pillath, R. K. W. Powell, A. Sighvatsson, F. A. Sorokos, L. Tase, R. von Kleist, A. Wechsberg.

1. SUDAN - 1993 ARTICLE IV CONSULTATION

Executive Directors considered the staff report for the 1993 Article IV consultation with Sudan (SM/93/222, 10/14/93). They also had before them a statistical annex (SM/93/225, 10/25/93).

The staff representative from the Middle Eastern Department made the following statement:

> On November 3, the Sudanese authorities informed the staff of changes in the exchange regime since the staff report was issued on October 14.
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> Effective November 1, limitations were introduced on foreign currency holdings. Residents and nonresidents entering Sudan must declare their holdings of foreign currency and re-export them within three months or surrender them to the banking system either for deposit in a free foreign exchange account or for conversion into local currency.
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> Also effective November 1, the authorities officially introduced a dual exchange rate regime comprising a central bank rate and a commercial bank exchange rate. The central bank rate was set at LSd 215 per U.S. dollar, which compares with the unified rate of LSd 170 per U.S. dollar at the end of October, and the commercial bank rate was set at LSd 300 per U.S. dollar. The central bank rate applies to all exports and official receipts and payments. All other transactions are to take place at the commercial bank rate.
>
> The authorities characterized these recent measures as an attempt to curtail speculation in the illegal foreign exchange market for banknotes. The proposed draft decision included in the staff paper already makes reference to the existence of multiple currency practices and, based on the limited additional information available to the staff at this time, remains valid.

Mr. Dlamini made the following statement:

> As Directors may recall, at the Board meeting at which Sudan's voting rights were suspended, the authorities pledged to continue with policy reform and maintain the dialogue with the Fund in an effort to find solutions to their economic problems. The recent Article IV consultation reflects some evidence of this commitment. It shows that the authorities have not only been applying extraordinary efforts to keep the economy functioning, but have also expressed broad agreement with the staff on the general direction of the economic policies needed to ensure sustained growth in a stable macroeconomic environment. This is a window of opportunity that both the Fund and the authorities can

explore with the aim of further strengthening the adjustment effort.

The economy continued to register a high real growth rate, estimated at 7 percent in 1992/93. Contributing to this favorable outcome was the good performance of the agricultural and manufacturing sectors. The economy benefited from good weather conditions, the liberalization of commodity pricing, and the further opening up of the economy to the private sector.

On macroeconomic policy, the authorities endeavored to restore a more disciplined financial posture. Revenue performance showed considerable strengthening, reflecting a boost in receipts from import duties, public enterprise profits, excise duties, and other taxes. Cash expenditures were also contained within the projected targets. Consequently, the Government's net borrowing from the central bank was in line with the target set for the period.

The inflation rate, although lower than in the previous year, was higher than originally anticipated, reflecting shortages of essential imported commodities owing to the acute shortage of foreign exchange as well as speculative practices on the part of traders.

Pressures on the external sector continued to constrain reform efforts and weaken investment performance. The current account deficit showed further deterioration from 16.7 percent of GDP in 1991/92 to 21.9 percent in 1992/93. Disbursements of external loans and grants were much lower than expected, forcing the authorities to resort to further import compression and the use of export contracts as security for new commercial borrowings. Meanwhile, the country has remained one of Africa's most indebted nations with the external debt-service ratio, on commitment basis, standing at 254 percent. Faced with this desperate external sector position, actual repayments were limited to 18.7 percent of current export receipts leading to further accumulation of external arrears.

In formulating their economic policies for the 1993/94 fiscal year, the Sudanese authorities have indicated firm resolve to address the problem of financial imbalances in order to restore a more stable macroeconomic environment. Fiscal and monetary policies will be further restrained to slow down inflation and reduce pressures on the exchange rate. Steps will also be taken to sustain growth.

The authorities are determined to boost revenue receipts, through improved tax administration, the taxation of crude oil production, and the sale of government assets. Expenditure restraint will be achieved through the phasing out of petroleum subsidies, cuts in real wages and salaries, a reduction of defense outlays, and the restriction of eligibility for certain subsidies of a temporary nature.

Progress toward a liberalized financial system will be accelerated. The improvement of monetary statistics and the introduction of government securities bearing market rates of return would, however, require technical assistance from the international community.

The problems in the external sector remain difficult. Despite the constrains imposed by exogenous factors, the authorities remain committed in their efforts to seek a durable solution. Thus, significant adjustment to exchange rates to attract the critically needed foreign exchange resources and enhance external competitiveness of the economy has been carried out effective November 1, 1993. Henceforth the commercial rate will be largely market determined. The authorities are currently undertaking intense diplomatic negotiations to improve relations with the donor community as well as resolve the internal conflict in the south of the country.

Finally, based on the current Article IV consultation report, the basic elements for a much more comprehensive adjustment program seem to have emerged. It would be useful for the Fund to put these elements together in a positive manner and catalyze donor assistance.

Mr. Abbott made the following statement:

Coming right on the heels of the Board's early August decision to suspend Sudan's voting rights, the staff's recent consultations offered the authorities yet another opportunity to provide assurances that they intend to address their economic problems and improve their unacceptable level of cooperation with the Fund. Unfortunately, but not surprisingly, they did not chose to do so, and we cannot agree with Mr. Dlamini's opening statement that the basic elements of a more comprehensive adjustment program seem to have emerged. More unfortunately, by fueling inflation, cutting off access to external assistance, and generally driving the economy into the ground, the regressive and misguided autocratic policies being pursued by the authorities continue to extract a large and unnecessary human cost in Sudan that should not be overlooked.

It is clear from the staff's report that the authorities do not have a workable economic strategy to deal with their problems, much less an approach that the Fund could endorse. Instead, we see only further regressive moves on the policy front, as the authorities seem bent on undoing what little remains of the economic reforms put in place early in 1992. A partial litany of recent regressive measures includes reimposition of price controls on key consumer goods, expansion of the negative list for key imports, and expansion of subsidies for urban residents. After the authorities suggested to the Board in August that they could intensify efforts to narrow the gap between the official and parallel exchange markets, they apparently have instead introduced a dual official exchange rate system and banned foreign exchange holdings outside of the banking system.

The authorities apparently hope this patchwork of measures will permit them to scrape by with a severe compression of imports, continued remittances from abroad, and an ever larger accumulation of arrears. By doing so, they seem to think they can postpone the fundamental economic reform and adjustments needed in virtually every aspect of economic policy. Here again, we disagree with Mr. Dlamini's statement. There is little to indicate that the authorities have expressed broad agreement with the staff on the policies that will be needed. By our reading of the staff report and the information made available last night, among other disagreements, the authorities apparently have attributed inflation largely to "speculative" exchange rate movements and rejected the idea that a move toward a unified exchange rate is imperative in the near term. In addition, the staff obviously takes a dim view of official projections for 1993/94: for example, for real growth, the staff sees 2 percent versus 10 percent for the authorities; for end-year inflation, the staff sees 70-80 percent, compared to 45 percent for the authorities.

Before turning to specific policy issues that need to be addressed in the period ahead, let me first note that we found the alternative scenarios prepared by the staff to be quite helpful in pointing out the potential benefits of a comprehensive adjustment effort and the consequences of inaction. We fully agree with the staff's inescapable conclusion: a return to macroeconomic stability will be a long time coming even under the best scenario, and delaying the inevitable will only make the eventual adjustment that much more wrenching. To illustrate the real human costs noted at the outset, Table 4a on page 15 shows that under current policies, population growth will run at nearly triple the rate of real GDP growth, while per capita consumption will decline significantly. And this is in a country whose people, on a per capita basis, are already among the poorest in the world. Yet this does not have to be the outcome. The staff has outlined a number of sensible and obvious measures that, if implemented in a cohesive fashion, could offer the beginnings of a way out. As we can strongly endorse the staff's policy recommendations, I would just underscore a few points.

On fiscal policy, the FY 1993/94 budget represents a move in the right direction. However, the staff's pointed skepticism regarding many aspects of the official projections--beginning with a whopping 8 percent point differential in projected GDP growth figures for the coming year--is all the more worrisome when the starting point--a fiscal deficit of 20 percent of GDP in 1992/93--is taken into account. For the current year, only a very modest improvement to 16 percent is in the cards; on a cash basis--after accumulating large interest arrears--the authorities are still looking at a deficit of between 6 and 8 percent of GDP.

With revenues low relative to GDP, we support the authorities' intention to improve tax collection and introduce new taxes, but in view of the risks to the projections pointed out by the staff, additional revenue measures would appear to be in order. On the expenditure side, we note that the Government intends to pay only a fraction of its interest obligations and has slashed public investment; neither trend is sustainable. In other areas, we would agree fully with the need to reduce significantly and better target subsidies, and to restrain public sector wages. Other nonproductive expenditures need to be looked at as well, particularly in the area of military and security-related spending.

On the monetary side, the situation is a bit more encouraging, as the authorities seem to understand the consequences of their past actions and are prepared to limit credit growth. However, in view of the widely divergent inflation projections, and especially if the authorities see no latitude for further fiscal restraint, a substantially more ambitious credit target would appear to be in order. In any event, we share the staff's concern that monetary policy needs to be nailed down now and that unplanned credit growth needs to be resisted.

Clearly, the other key elements of the reform effort would need to take the form of a move to a unified and market-determined exchange rate regime and an associated effort to completely liberalize prices and eliminate trade restrictions for both imports and exports. Unfortunately, the authorities seem to see "speculative" activities in the parallel exchange market as the cause of their inflationary difficulties and seem intent on killing them off. In this regard, while the details of the exchange measures just put in place are sketchy, the additional distortions introduced by a multiple rate system and the ban on private foreign exchange holdings are not helpful.

Furthermore, while both exchange rates introduced this week appear to be somewhat more depreciated than the previous single official rate, there is no indication that these rates will be any more market-determined than the old official rate, or even that the authorities have addressed the downward stickiness, induced by the rate-setting mechanism, of the former official rate relative to the parallel rate. Finally, as a side note, it appears that the Government announced the foreign exchange measures in the local press on October 15 and implemented them, along with the dual exchange rate system, on November 1. However, the authorities apparently did not notify the staff of these developments until November 3. This episode, in our view, is not illustrative of a cooperative approach on the part of the authorities.

On the subject of Sudan's noncooperation and the future course of relations with the Fund, we fully agree that, as the staff suggests on page 18, implementation of a comprehensive adjustment effort in the very near term could provide the basis for a track record that could eventually permit resumption of relations with the Fund and a normalization of relations with the rest of the international financial community.

However, Sudan's policy record has been poor, and its recent payments record poorer still. Sudan has made only three payments this year--amounting to less than $1 million of the roughly $56 million needed annually to even stay current in its obligations--and has made no payments at all since our meeting on August 6. Of the $6 million Sudan promised to pay over its most recent fiscal year, it has paid less than half. As a result, Sudan's $1.6 billion in arrears poses an ever greater burden on all members of the Fund.

As the staff has rightly pointed out to the authorities, procedures on compulsory withdrawal could be expected within six months of the decision to suspend a member's voting rights. With less than three months remaining until the next review of Sudan, the authorities have done nothing to reverse their record of noncooperation: payments have fallen far short of their own limited commitments, much less the level needed to stay current, and policy performance has been abysmal. While we continue to hope that the authorities will take steps to improve their cooperation with the Fund, we foresee a need to consider compulsory withdrawal in the very near future.

Mr. Autheman made the following statement:

This Article IV consultation discussion on Sudan is indeed out of the ordinary, given its unusual direct implication for Fund resources. I do not need to recall that Sudan represents by itself nearly 40 percent of all arrears due to the Fund and consequently poses a heavy burden.

Let me commend the staff for the quality of its comprehensive report, whose appraisal I fully support. It is obvious that a radical change in economic and financial policy will be needed in Sudan and that, without great efforts to resume payments to the Fund, Sudan will remain trapped in a vicious circle of economic regression and isolation.

Until now, regrettably we have received no indication of Sudan's readiness to make the slightest move that would authorize us to be more optimistic on future prospects of cooperation.

Sudan's policy performance remains disappointing. Despite a second consecutive year of rapid, weather-driven economic growth, high levels of inflation have been recorded while fiscal and external imbalances have continued to widen. To deal with the acute shortage of foreign exchange, the authorities have increasingly resorted to new restrictions and other ad hoc methods, as the November 1 decision on the exchange regime shows. In a number of areas, as rightly pointed out by the staff, policy setbacks occurred: in particular, the authorities have progressively moved away from the unified market-based exchange rate system that Sudan attempted to set up in February 1992, and I would mention that Sudan again contracted medium-term private nonconcessional loans, which could only add to its external difficulties.

Moreover, as regards payments to the Fund, the authorities did not act upon their reiterated commitment to continue making monthly payments of at least $300,000 to the Fund: in fact, since the Board's decision to suspend Sudan's voting rights, no payment has been received.

I am well aware that the dramatic dwindling of external assistance has created increasing constraints on economic policy. But the authorities' stance toward external creditors, in particular the Fund and the World Bank--the latter having been unable to maintain its disbursements and suspending them in September--can only worsen the situation.

I would have seen some hope in the recent adjustment in the exchange rate of the Sudanese pound if it had been part of a consistent strategy to re-establish relations between Sudan and the international community.

Could the staff tell us to what extent the depreciation has closed the gap between official and parallel market rates? I wonder whether the dual exchange rate system will not contribute to a further deterioration of the Sudanese position. Which rate will apply to workers' remittances, the only private inflow Sudan can presently expect to foster in order to improve its external position?

The adjustment of the exchange rate will not have positive consequences if it is not complemented by stricter fiscal and monetary policies.

As regards fiscal policy, I have noted that the Government's net borrowing from the banking system has been kept broadly in line with the 1992/93 targets, but this has been achieved only through further external arrears. Therefore, a substantial strengthening in the fiscal stance is of the utmost necessity, all the more so because budget revenue and expenditure targets are obviously unrealistic.

As regards monetary policy, the intention to slow down the growth of credit to the private sector and public enterprises is appropriate. The recent setting up of a reserve requirements system, besides the use of credit limits, might be a useful additional tool. But I have some doubts about the credibility of the announced objectives. Interest rates remain negative, the central bank continues to finance public deficit, and the devaluation of the currency would call for a stricter credit stance immediately.

Besides a more appropriate economic policy, an immediate resumption of payments to the Fund is clearly a prerequisite for a closer collaboration between Sudan and our institution. On the one hand, the level of the monthly payments should not be symbolic as compared to the interest charges falling due on the existing stock of arrears. On the other hand, I understand that it would be difficult to immediately reach the level required to stabilize the stock of arrears before a possible rights accumulation program. This chair fully supports the idea mentioned in the report of an upward payments scale that would provide the scope for a debt stabilization to be within reach in a reasonable lapse of time. I would be interested to hear the staff's opinion on an appropriate minimum level that could be called for. Such information could be conveyed to the Sudanese authorities. A positive answer on their behalf would be one of the last chances for Sudan to avoid cutting altogether its relationship with this institution.

Mrs. Wagenhoefer said that she was generally in agreement with both the staff and the previous two speakers regarding the analysis of Sudan's problems and the proposed therapy.

The figures carefully assembled by the Sudanese authorities were reminiscent of a "Potemkin village," pretty facades poorly concealing the sorry truth. Such an effect might have been amusing, except for the hardships that the people of Sudan had had to endure.

The staff was to be commended for having produced a well-balanced, concise, and interesting report under difficult conditions, Mrs. Wagenhoefer continued. The staff had highlighted some particularly questionable assumptions of the authorities and had rightfully voiced concerns about them. With some of the official figures appearing somewhat arbitrary, in areas like tax collection or credit growth, it was difficult to offer substantial comments on specific issues, although the bleak overall picture was worth another look.

Especially worrying was the fact that the exceptional growth performance of the last two years had been based almost entirely on favorable weather conditions and resulting good harvests, elements that were not within the authorities' control, Mrs. Wagenhoefer continued. Promotion of other areas of economic growth were, therefore, of great importance. The constraints and difficulties facing the authorities of developing countries were well known; however, even particularly challenging circumstances did not relieve governments of their responsibilities with respect to the needs and well-being of the population.

In closing, Mrs. Wagenhoefer quoted what she regarded as a particularly fitting passage from page 18 of the staff report: "Lack of prospects for an immediate resumption of foreign assistance, however, does not make a weakening of the adjustment strategy a viable course of action. On the contrary, stronger and more effective adjustment policies become all the more necessary in order to persuade the international community to increase its support for Sudan in the context of a comprehensive program designed to address Sudan's economic problems." She had found the staff projections comparing different policy scenarios especially useful in that regard, as they forcefully demonstrated the benefits of sound macroeconomic policies for Sudan. She fully endorsed the other sections of the staff appraisal and the proposed Board decision.

Mr. Quattrociocche made the following statement:

I share the sense of frustration expressed by previous speakers about Sudan's disappointing economic performance. My major concern comes from the substantial inadequacy of the Government's action in the exercise of fiscal restraint and in the pace of structural reform. Sudan's relations with the international financial community are at the most delicate stage in the history of the country, and this certainly adds to the already daunting task of the authorities. Still, I would have thought that they would take their increasingly difficult situation as a further sign of the urgent need to tackle the enormous problems facing their economy. Quite to the contrary, the staff report clearly describes how the stance of economic policies envisaged by the Government is alarmingly similar to past choices. Such a position on the part of the authorities makes one wonder about their willingness to implement the recommendations repeatedly made by the staff and by this Board, in the context of the assistance extended by this institution.

I am in complete agreement with the staff's appraisal of Sudan's economy, and I share its concerns with respect to the possible implications of the present economic policy setting. Comprehensive adjustment and reform efforts are badly needed, in order to elicit a favorable supply response and reduce macroeconomic imbalances. Rectification of the present economic policies is urgently needed in almost every field. I concur with the staff that unification of the exchange rates would be a useful starting point. A unified market exchange rate is of fundamental importance in the restructuring process of the economy. The persistence of a dual exchange market in Sudan impedes a better allocation of the extremely scarce foreign exchange resources and increases the burden falling on monetary and fiscal policies. The lack of flexibility shown by the Banker's Association in adjusting the exchange rate has left the authorities no choice but to introduce exchange restrictions, in order to keep the exchange rate at its present level. Rather, the focus should be on appropriate macroeconomic management, especially firm monetary control, in order to prevent the vicious circle of inflation and exchange rate depreciation.

Indeed, the effectiveness of monetary policy in fighting inflation is doubtful, given the still huge monetary financing of the budget deficit and the lack of monetary instruments bearing market-related rates of return. Only a reduction in the financing needs of the public sector will allow monetary policy to assume its role as an independent tool of macroeconomic management. In the present circumstances, the increased reliance on reserve requirements in order to tighten credit policy is almost unavoidable, but this, of course, hampers the development of a sound and competitive banking system. I tend to believe that the authorities' intention to slow down credit expansion to the private sector--which, by the way, may be the sector with the greatest potential to create new jobs--will not be enough. Under current policies, the rate of money growth may prove to be too high to meet the authorities' inflation objective, while at the same time may not satisfy the requirements of the private sector. Rather, positive real rates of remuneration should be firmly pursued in order to reallocate credit and achieve a pace of monetization consistent with the situation of the economy.

This is all the more important as the assumptions underlying the 1993/94 budget seem to be rather optimistic. In particular, the doubling of revenues envisaged by the Government is unlikely to be achieved, unless a decisive strengthening of tax enforcement and collection procedures is accomplished. Moreover, attainment of the fiscal objectives over the medium term will require a substantial increase in the revenue/GDP ratio from the current low level of about 9 percent. On the expenditure side, I share the concern of the staff that the dramatic reduction of nearly 10 percent in real terms can only materialize if capital expenditure is substantially cut. This is something that should be avoided, because infrastructure is badly needed in Sudan. Likewise, education and health should not be affected by budgetary cuts, while bold measures should be taken to reduce unproductive expenditures.

The medium-term prospects for Sudan are subject to a number of uncertainties, mainly related to the timing of external financing and the pace at which it will be resumed. Sudan's balance of payments fragility is clearly identified by its debt-service ratio, which is projected to be in the order of 285 percent of exports in the present fiscal year, and will remain well above 200 percent until the year 2000, under current policies. Without a doubt the staff is correct in pointing out that implementation of appropriate policies will be essential for an early resumption of assistance from multilateral and bilateral donors. I found the alternative scenario developed by the staff to be extremely useful in showing the magnitude of the improvement in Sudan's economic performance accruing from a strengthened adjustment effort. I hope the Sudanese authorities will not undervalue the necessity and urgency of coming to grips with the problems of their economy, and restoring normal relations with the international financial community.

I support the proposed decision.

Mr. Mojarrad made the following statement:

As Mr. Dlamini's helpful statement indicates, the 1993 Article IV consultation discussion with Sudan, immediately after the Board suspension of its voting rights, is evidence of the Sudanese authorities' readiness to maintain the dialogue with the Fund and their desire for an eventual normalization of relations. The authorities have also reaffirmed their commitment to the liberalization and reform program initiated in February 1992.

We are pleased to note that the authorities are making extensive efforts in improving relations with the donor community and moving toward a resolution of the conflict in the South. Notwithstanding the temporary interruptions in the progress of policy reforms owing to the fall in external assistance, growth performance during the last two years has been satisfactory, and success on the fiscal front has kept government net borrowing from the Bank of Sudan in line with the projected target in 1992/93. Nevertheless, the authorities are confronted with daunting economic problems, the most urgent of which is to alleviate pressures on the external sector and clear debt arrears. In this regard, the recent adjustment to exchange rates is a welcome step. As regards the prospects for 1993/94, we agree with the staff as well as the authorities that stabilization should be considered the first priority. The authorities are well advised to embark on a comprehensive adjustment and reform effort. It is encouraging to note that a number of steps, including cuts in real wages, containment of subsidies, and reduction of defense outlays have already been taken. The revenue target, though appearing overly ambitious, can be achieved given the revenue performance in the current year and the authorities' intention to further improve the tax collection system and procedures.

On the fiscal front, Sudan will need to reduce its budget deficit significantly. Cognizant of this, the authorities intend to reduce the deficit from 20 percent of GDP in 1992/93 to 12.5 percent of GDP in the next budget year, both through improved revenue collection and expenditure cuts. But these measures are obviously not enough. Crucially important are policies for liberalizing the restrictions on investment and further dismantling price controls and adjustment of the rates of return. The latter policy measure is important not only in view of the mobilization of domestic savings, but also owing to its critical role in improving resource allocation. In our view, there is no inconsistency between a market-determined rate of return and requirements of Islamic banking. In this regard, we would like to endorse the staff's useful suggestion for issuance of government bonds having market-related returns.

Needless to say, without the private sector's active participation, domestic resources could only be partially mobilized. Therefore, the authorities are encouraged to speed up the privatization process. Recent initiatives, including mergers of several state banks for eventual privatization, as well as sales of two cotton ginning factories and a public mining corporation, are steps in the right direction.

An area of concern is the high rate of inflation. While some progress has been made in reducing price pressures in recent months, the year-to-year increase in inflation is still rather high, and there is the risk that inflationary pressures may even rise as the market-determined exchange rate depreciates. Thus, the monetary authorities would need to persevere with a policy of restraint.

On the medium-term policies, the staff convincingly emphasizes that the program has to be proportionate to the magnitude of imbalances, and therefore has proposed a tougher scenario, which in the staff's view embodies a partial adjustment and limited reform efforts. While we generally agree that the present corrective policies can be fostered at least in some areas, we are of the view that care should be taken in deciding how much austerity is manageable, given the political and economic realities of the country. Recent experiences in several former centrally planned countries have left no doubt that when there are severe imbalances, vigorous adjustment policies would make social strain inevitable. In the case of Sudan, the staff is making these recommendations in the absence of an increased flow of capital from abroad.

The result of scenario B indicates that, under the most ambitious reform measure assumption, this country can and should be afforded generous debt relief similar to that enjoyed by other countries because of the large projected current account deficit over the medium term. The authorities have demonstrated their commitment to the implementation of adjustment program and deserve timely encouragement and financial support to sustain the measures already taken and to enhance their efforts for further adjustments. We are of the view that an early resumption of financial assistance would pave the way for the implementation of scenario B and, therefore, for the full settlement of arrears to the Fund.

With these remarks, we support the proposed decision and wish the authorities well in performing their daunting task of stabilization.

The staff representative from the Middle Eastern Department replied, in response to Mr. Autheman's question on the parallel exchange markets, that unofficial press reports placed the parallel exchange rate at between LSd350-370 per U.S. dollar, while the two official rates were at LSd300 and LSD215 per U.S. dollar. In addition to informing the staff of the new rates, the authorities had indicated to the staff that commercial banks would be permitted to determine the commercial bank rate. Of course, the effectiveness of that rate would depend on the extent of the gap between the official and parallel rates.

With respect to the question Mr. Autheman had raised on Sudan's payments to the Fund, the staff representative noted that, over the past year, the staff had made it clear to the authorities that, for a rights accumulation program to be initiated, Sudan would need to stabilize its arrears. On an annual basis, they would need to pay about SDR 40 million, or about SDR 3.5 million per month. During discussions in 1993, the staff had discussed a specific time frame of six to eight months for reaching that objective. During the Article IV consultation, using different scenarios, the staff had tried to indicate to the authorities that SDR 40 million could be reached on an annual basis, even without a significant resumption of external assistance. In particular, the second scenario illustrated how workers' remittances and exports could generate the foreign exchange required to meet the targeted level of arrears payments.

Mr. Dorrington made the following statement:

First, like some of the earlier speakers, I wish to commend the staff for producing a very clear, measured, and balanced report on Sudan. I also agree with Mr. Autheman's comments on the burden Sudan is placing on other Fund members, especially those other low-income countries that are trying hard to solve their problems. More generally, I agree with everything that has been said by Mr. Abbott and the three speakers who followed him.

Sudan, despite its geographical location, has considerable productive scope. In agriculture, for example, favorable weather conditions can lead to good harvests capable of generating exportable services. The longer-term prospects could therefore be for significant improvements in the low standard of living. But to realize these prospects requires a suitable adjustment program. The strategy outlined by the staff is the right one, and I urge the authorities to adopt it.

The contrast between the two scenarios in the paper underlines a point that this chair has made before, namely, that failure to adopt the kind of economic policies that could be endorsed by the Fund will not reduce the economic pain to be suffered by the Sudanese people. On the contrary, it will increase it.

I have one or two specific issues I would like to raise. First, the Sudanese authorities have, as the report notes, introduced pervasive price subsidies. We spend a great deal of time around this table urging countries to permit realistic prices and to address the related welfare aspects through well-directed social safety nets. Today is no exception. These subsidies go hand in hand with the extensive price controls. Subsidies cannot be the answer to inflation; they merely transform high prices into longer queues for scarce commodities, and I agree with the staff that use of such controls only attacks the symptoms of inflation and does not address its causes.

On the exchange rate system, the measures introduced last month, which involved the devaluation of the Sudanese pound and more recent devaluations, do not go anywhere near far enough. I endorse the staff's view that the full adjustment of the exchange rate and a move to a unified, freer exchange rate system is urgent.

The measures introduced recently also include further exchange restrictions. This is not merely a failure to adopt Fund advice, but clearly a move in the opposite direction, manifested in the loss of faith in the domestic currency and the shortage of foreign exchange.

In an anecdotal report from Khartoum, I learn that the duty free shops at the airport will not accept Sudanese pounds but will accept U.S. dollars. In practice, they also deal in the currency that keeps its value in terms of U.S. dollars, the so-called Disney dollars, which look somewhat similar to U.S. dollars, except they carry the picture of Mickey Mouse. Indeed, I understand that elsewhere in Khartoum there are places where Disney dollars are more acceptable than Sudanese pounds. I repeat this anecdote not because it is amusing, but because it illustrates the seriousness of the economic situation, a situation which I believe can only be improved by following the staff advice. Regrettably, there is no sign of that.

Since Sudan was last discussed at the Board in August, there have been no payments to the Fund in respect of outstanding arrears. That information, coupled with the information in the staff report being discussed today and the exchange restrictions recently introduced, leave me regretfully to conclude that no evidence has yet emerged that the Sudanese authorities have resumed cooperation with the Fund. I urge them to do so very soon. I support the proposed decision.

Mr. Jiménez de Lucio made the following statement:

Like previous speakers, we regret that the Sudanese authorities have not taken advantage of the Article IV consultation to translate into reality their stated intention to continue with policy reform and to cooperate with the Fund to develop a comprehensive program to address Sudan's severe economic and financial imbalances. We also regret that no additional payments to the Fund have been made since the country's voting rights were suspended in early August.

We commend the staff for its frank assessment of the outlook for the Sudanese economy. The large difference between the two scenarios presented by the staff in the report--one embodying the current policy stance and the other the authorities' declared economic objectives--clearly demonstrates that current adjustment efforts are insufficient and inadequate to reach the authorities' macroeconomic goals, and that there is a strong likelihood of a further significant deterioration of the economy during the coming year. A meaningful discussion of an adjustment program that could be endorsed by the Fund does not seem possible at this time.

Experience shows that the economic policies presently being pursued are both unsustainable and detrimental to the future welfare of Sudan's population. We urge the authorities to reconsider their economic reform strategy and adopt corrective measures immediately. Only by introducing credible exchange rate, fiscal, and monetary policies will the authorities be able to stabilize the economy, restore donor confidence, and lay the foundations for sustained growth. The Fund should, in any event, stand ready to assist the Sudanese authorities in their adjustment efforts.

In closing, we reiterate our call to the Sudanese authorities for an immediate and unequivocal resumption of active cooperation with the Fund.

Ms. Laframboise made the following statement:

We view the recent history of relations between Sudan and the Fund as very unfortunate and would sincerely like to see Sudan take the steps necessary to achieve balanced sustainable growth and to restore active cooperation with the Fund. However, we observe with some distress that Sudan's economy is currently following its own unruly course without appropriate guidance from its authorities. We fully support the staff's appraisal and the views of earlier speakers.

We do note progress in certain areas such as strong GDP growth and a prudent expansion of credit to the Government; however, the outcome in other areas and the recent policy initiatives regarding the exchange regime do not provide us with much confidence in Sudan's future. We have no doubt about the staff's assertion that depreciation of the currency is a result of high inflation and not its cause. In the same "chicken and egg" context, we can appreciate that the difficulty of implementing adjustment policies is compounded by insufficient flows of foreign assistance. However, the only way to bring foreign assistance back and to encourage private capital flows is to build the confidence of investors and the international community by demonstrating a commitment to stabilization and reform.

We only wish to urge the authorities to adhere to a comprehensive adjustment program in order to develop a consistent record of policy performance. The logic of this approach is clearly illustrated by the staff's two sets of medium-term macroeconomic projections.

Mr. Wei made the following statement:

At the outset, I would like to emphasize three points before discussing the details of the consultation report for Sudan. First, the recent Article IV consultation itself has demonstrated the authorities' willingness to cooperate with the Fund. Second, the authorities have continued to implement their adjustment policies and have taken a number of reform measures in the areas of liberalization of commodity pricing and enhancement of the role of the private sector. This was highlighted in Mr. Dlamini's very helpful opening statement and also recognized in the staff paper. Third, the authorities have been making adjustment efforts in an extremely difficult environment, particularly in the face of the serious shortfall of external assistance. With these remarks in mind, we are in broad agreement with the staff appraisal, and thus I will limit myself to a few observations.

With respect to inflation and macroeconomic policy, the measures to liberalize pricing, coupled with the currency depreciation and excessive bank credit to the private sector, have contributed to the disappointing inflation performance--persisting at 80 percent of the yearly average. In my view, the gains from continued economic growth will ultimately be eroded if inflation persists at this high level. In this regard, I welcome the target to reduce the rate to 45 percent by June 1994. Consistent with this goal, I appreciate the authorities' recognition of the primary need to further strengthen fiscal discipline. In addition, the Government's borrowing from the banking system, which has also exacerbated the inflation problem, should be sharply reduced and strictly limited to the target.

On the external front, faced with a marked decline of private inflows and official capital transfers, Sudan's balance of payments position has weakened and remains extremely vulnerable. This has led to the restoration of two exchange rates and, consequently, the authorities have had to resort to import restrictions. We share the staff's concern that the reform of the foreign exchange system has fallen short of the authorities' original intentions, resulting in a real appreciation of the currency. The authorities should be encouraged to press ahead courageously with market-oriented policy reforms and exchange rate unification, which I concur with the staff should be the top priority on their policy and reform agenda.

Finally, I welcome the authorities' reaffirmation of their commitment to carry out the reform policies and strongly encourage them to initiate further policy measures to improve relations with the donor community. In this respect, the authorities are urged to adopt a comprehensive adjustment program with the aim of increasing Sudan's ability to repay its overdue obligations to the Fund.

With these remarks, I support the proposed decision and take this opportunity to urge the authorities to persevere with reform efforts and to do their best to improve their payments to the Fund so that the arrears can be settled as early as possible.

Mr. Verjbitski made the following statement:

As previous speakers have made most of the points that I was going to make on Sudan's difficult economic adjustment effort, I shall limit myself to commenting briefly on several issues of special concern to my authorities.

As we previously stated, this chair views the Article IV consultation as an important opportunity for revitalizing the dialogue between the Fund and the Sudanese authorities regarding the necessary actions and policy measures, that could pave the way toward eventual normalization of Sudan's relations with the Fund.

Taking into account Sudan's continued reliance on foreign sources of financing of its overall budget deficits, and given the size of Sudan's external arrears--equivalent to about 250 percent of external current account receipts--and the virtual drying up of foreign donor support last year, this chair remains convinced that a rights accumulation program is the only viable option for Sudan to improve its relations with the Fund and the international financial community in general. I agree with the staff that enhanced adjustment policies are fully warranted in Sudan as a basis for possible resumption of active cooperation with the Fund.

In this context, I am sympathetic to the view expressed by Mr. Dlamini that the Sudanese authorities' broad agreement with the staff on the general direction of their economic policies creates a window of opportunity for strengthening the adjustment effort. Still, it is regrettable that so far this broad agreement has not been fully translated into action by the authorities.

The authorities' price liberalization effort, initiated in February 1992, has recently gone off track. Especially worrisome in this regard are the measures announced by the authorities last July that provide for increased price subsidies and the setting up of price councils to enforce fixed prices for a range of commodities through referrals to the judicial system.

The new mechanism for determining the official exchange rate of the Sudanese pound has proved to be ineffective, which has led once again to its large overvaluation in relation to the parallel market rate. The authorities' measures on introduction of a dual exchange rate, described in today's statement by the staff representative, appear to represent another step in the wrong direction, despite the implied currency depreciation. This confirms that the authorities prefer to continue relying on trade and exchange restrictions in dealing with Sudan's balance of payments problems instead of further liberalizing the external sector.

Unfortunately, such steps do not create an adequate basis for concluding a rights accumulation program with the Fund. Therefore, I would like to urge the authorities to review their policy stance on these issues because they are key to any market-oriented reform. Reunification of the exchange rate system in Sudan would be an important step in that direction and could improve the Bank of Sudan's ability to make debt-service payments and to acquire foreign exchange.

As I broadly agree with the thrust of the staff appraisal of Sudan's monetary and fiscal policies, and with the relevant policy recommendations, I would just like to specifically point out two things. First, I share the staff's view that the authorities' 1993/94 budget projections are overly optimistic and require substantial downward revision of the revenue estimates. Second, Sudan's monetary policy is undermined by highly negative real interest rates on deposits, which inhibit savings and remain a major factor of instability.

With these comments, I can support the proposed decision.

Mr. Ishida made the following statement:

I am in a broad agreement with the staff's appraisal.

As many Directors recalled, last July the authorities expressed their intention to resume a schedule of monthly payments of at least $0.3 million to the Fund over the 12-month period from July 1993. I understood at the time that, while the amount of the payment would be small in comparison with future obligations falling due, the payments would have been evidence of the authorities' willingness to resume normal relations with the Fund.

It is therefore extremely disappointing to hear from the staff that the authorities have not made any payments at all to the Fund since the last Board meeting. Certainly the authorities have had severe difficulties as a result of shortfalls in foreign exchange because of the virtual elimination of foreign assistance. Nonetheless, as this chair has repeatedly stressed, it is important that the authorities pay as much as possible on a regular basis to the Fund, even if the amount is very small, and that they recognize the preferred creditor status of the Fund. Without the minimum payments and recognition of the Fund's preferred creditor status, it is almost impossible for Sudan to resume normal relations with the Fund.

Let me turn to the policy issues. The major problems of the economy are the high inflation and the shortfall in foreign exchange. In order to reduce the rate of inflation, the authorities have reversed the price deregulation policy of early 1992 and are now considering adopting a policy of direct price controls, which would include the enforcement of fixed prices for essential commodities, and the strengthening of the government distribution system. In addition, the authorities have not completed the unification of the foreign exchange markets.

It is obvious that these measures will not help in any way to solve the problems in the long run. The authorities should give priority to the resumption of normal relations with the international financial community; to do this, they need to improve their capacity to repay their debt to creditors by strengthening exports and reducing imports. There is no other way, therefore, than to gradually adjust the exchange rate to a market-based level, and promptly and steadily contract the credit supply so as to curb inflation as soon as possible.

Mr. Mohammed made the following statement:

Faced with a deteriorating economic situation for several years, the authorities began in February 1992 to liberalize and reform the Sudanese economy. The exchange rate was unified, allowing the Sudanese pound to depreciate substantially, and the exchange and trade systems were liberalized. The authorities also lifted price controls for all goods, except a few basic commodities and services, and they opened the economy to private investment. These were welcome steps indeed, but as events demonstrated, they were insufficient for a sustainable turnaround in economic conditions. Large fiscal imbalances persisted and were financed by continued large monetary expansion. This led to persistent high inflation and severe pressures on the balance of payments, and, of course, more arrears accumulation. As a reaction to the high inflation, the authorities effectively discontinued the exchange rate unification, imposed new trade restrictions, and reversed several price liberalization measures. The parallel exchange rate continued to depreciate with the rise in inflation, but the official rate remained sticky, leading to continued tightening in the foreign exchange situation and a rationing of foreign currency for imports.

The staff report points to the need for the adoption of a stronger and more comprehensive strategy for Sudan to begin to move along a path of sustainable economic recovery. The cornerstone of such a strategy should be strong demand management, which would control the short-run inflationary effect--understandably a concern of the authorities--of implementing a market-determined unified exchange rate.

As Sudan's adjustment effort regains momentum, it is hoped that financial assistance from the international community would be forthcoming and, in due course, private resources would also be attracted. Thus, it is hoped that conditions will be created for the restoration of active cooperation with the Fund.

With these remarks I agree with the proposed decision and wish the authorities well in dealing with this difficult situation.

Mr. Heinen made the following statement:

Sudan's economic situation remains very precarious. Since the last Article IV consultation, the expectations for a turnaround stemming from the February 1992 reorientation of policies have not materialized: on the contrary, during 1993 the Sudanese authorities, citing a serious balance of payments problem, suspended their arrears payments to the Fund, which led in turn to the suspension of Sudan's voting rights last August.

Although Sudan's productive capacity, certainly aided by favorable weather, expanded for the third consecutive year, the staff report very clearly depicts the fundamental structural problems that need to be resolved before the country's economic development can resume. As we fully agree with the thrust of the staff paper, we only wish to highlight two main points: the underlying causes of the present situation and the scope of fiscal policy.

The analyses of the Sudanese authorities and the staff diverge on the causes and effects of the country's economic woes. While the authorities view the lack of foreign assistance and the presence of speculative elements in the currency markets as the main causes of the country's weak economic base and the rapid depreciation of the pound, the staff sees them instead as consequences of mistaken policy decisions. Even though it is arguably difficult to determine precisely which is cause and which is effect, as their relation is reciprocal, we fully agree with the staff that the primary goal of the authorities should be to implement confidence-creating measures. These include introducing a unified market-determined exchange rate and a tightening of financial policies to foster price stability and improve the real rate of return on deposits. The latter would go far to encourage domestic savings, attract outside remittances, and eventually provide a basis for the gradual resumption of donor support.

On the fiscal front, the authorities' estimates concerning the expansion of their revenue base and the real cuts in cash expenditures strike us as extremely optimistic, if not unrealistic. The staff points out that the revenue assumptions depend largely on sustained import volumes and continued favorable climatic conditions, both of which are subject to considerable uncertainty. The planned redirection of expenditures from the national wage and defense bills toward domestically financed development projects is certainly laudable, but may not be feasible for Sudan. For example, how do the authorities expect to maintain the fragile social consensus while holding 1993/94 salary increases far below the inflation level? How can they cut defense expenditures when the civil war in the South is far from being resolved? In the latter respect, has there been any attempt so far to quantify the financial burden of this conflict on the Sudanese economy generally, or to determine exactly what would be gained from its early settlement? The staff's comments on these issues would be appreciated.

Mr. Tetangco made the following statement:

The Fund's exposure of more than SDR 1 billion to Sudan and the country's recent suspension heighten the importance of this Article IV consultation discussion. Primary among our concerns is how the Fund can increase the probability of repayment of arrears in a timely fashion. With Sudan having lost much international support, I agree with the staff that their primary goal needs to be the achievement of financial stabilization and implementation of a sound economic program. Undoubtedly this is a daunting task, especially without external assistance. However, it is clear there is no alternative if the Sudanese economy is to extract itself from its current difficult position, and if relations with the Fund and other countries and agencies are to be normalized.

Listening to Mrs. Wagenhoefer's quotation of the staff's statement that stronger adjustment policies are all the more necessary given the lack of international support reminds me of a Roman historian, Titus Livius, who once said, "In difficult situations when hope seems feeble, the boldest plans are safest."

I agree with much of the staff appraisal as well as its policy recommendations. In particular I join it in urging Sudanese authorities to move rapidly toward unification of the exchange rate and to work to contain the fiscal problems. Less reliance on optimistic forecasts would also be prudent, given current uncertainties and the agricultural sector's vulnerability to climatic changes. A calm political atmosphere is clearly an important prerequisite for early progress, and it is our hope that progress in resolving internal conflict becomes a lasting improvement.

I support the proposed decision.

Mr. Keller made the following statement:

At the time of our last discussions in early August, the Sudanese Minister of Finance, then in charge, assured this Board personally of his country's commitment to fully cooperate with the Fund. Some speakers then argued that Sudan should be given more time to prove its good intentions. The occasion to provide the proof of commitment in line with the intentions was supposed to be the Article IV consultation. On the basis of the staff report in front of us, I must say that it is hard to see any sign of improved cooperation and renewed dialogue on economic policy issues with the Fund. Rather, there are once more new promises for reform, but contrary actions, as well as excuses for a weakening of the policy stance, so that one could doubt whether the seriousness of the situation is really well understood.

Moreover, prior to our discussions in August, the authorities made minor payments, intended as a sign that they also took seriously the problem of overdue financial obligations with the Fund, and made an effort to resume the payments. One is stunned to learn that a few weeks later the staff was told by the same authorities that the virtual drying up of foreign assistance is the reason that precludes them from making any further payments. I do not think that this is the way to enhance credibility with the Fund.

Against this background, I would like to make two comments. First, the staff is fully right in stressing the paramount importance, when assessing Sudan's economic problems, of confidence in the adjustment efforts of the Sudanese authorities, and confidence in their commitment and ability to formulate a coherent economic policy in the face of civil wars and repression.

Second, in these circumstances and considering the nature of Sudan's very entrenched debt problems and its protracted arrears situation not only with the Fund but also with other donors, it is difficult to see how foreign assistance could presently be justified. In this context, it should be noted clearly that foreign assistance is not an entitlement but has to be won through achievements. In the particular case of Sudan, I think that blaming a shortfall in performance on the fall of foreign assistance does not help at all, and is particularly unwelcome.

It is difficult to conclude on a more positive note than by bringing to the attention of the Sudanese authorities that, in principle, it is never too late to start strengthening adjustment efforts substantially in a positive and cooperative way with the Fund. While the economic and social costs of delayed action increase rapidly, time is quickly running out for them to take advantage of the window of opportunity for economic reform and improved relations with the international financial community that Mr. Dlamini has identified in his opening statement. The Sudanese authorities have their future in their own hands.

I can support the proposed decision.

Mr. Solheim made the following statement:

I am in full agreement with the staff appraisal. At this stage, I will therefore comment on only a few issues.

The Sudanese economy is in a very difficult situation, and the economic policy stance of the authorities seems to be in serious disarray. A major problem is that the 1992 reform of the foreign exchange system has fallen short of the authorities' original intentions, and the official exchange rate has thus failed to adjust fully in line with market developments. The hesitancy of the authorities to depreciate their currency in line with market conditions has also contributed to the strained relations with the international financial community.

The real appreciation of the Sudanese currency, amounting to 60 percent since the attempted unification of the exchange rate in February 1992, clearly illustrates this point. We urge the authorities to revert to their initial policy of a unified exchange rate and accept the necessary market implications. It is essential that the shortage of foreign exchange start to be redressed, thus enhancing the incentives for private capital inflows. This should also contribute to progress toward stabilization of arrears to external creditors, and allow for a normalization of Sudan's relations with the international financial community. While I understand the authorities' concern about the inflationary implications of currency depreciation, it will have to be addressed through consistent and comprehensive implementation of accompanying macroeconomic and structural adjustment policies.

I share the staff's concern about the realism of the authorities' budget estimate, on both the revenue and expenditure sides. In particular, I concur that the gasoline subsidy is the most obvious candidate for early elimination. Additional fiscal action and monetary restraint is called for, although this may prove difficult to implement fully if more foreign assistance is not forthcoming. Thus, without both strong economic policy measures and gradual resumption of donor support, the Sudanese economy seems trapped in a vicious circle.

The Sudanese authorities should be left in no doubt that only a consistent domestic adjustment and stabilization policy program on their part can unlock donor assistance. While I welcome the authorities' desire for normalization of relations with the Fund and their readiness to maintain a dialogue, the staff report does not give many glimmers of hope for Sudan's future economic development. It is absolutely essential that the authorities establish a track record of policy cooperation in the time ahead, and thus undertake a substantial strengthening, and reorientation, of the reform and adjustment efforts.

Finally, I support the proposed decision.

Mr. Burdiel made the following statement:

This is indeed a very special Article IV consultation, after the suspension of Sudan's voting rights by this Executive Board on August 6, and the suspension of World Bank disbursements, effective September 16. The staff itself is "conscious of the severe constraints on the conduct of economic policy imposed by the fall in foreign assistance," and the "lack of prospects for an immediate resumption of that foreign assistance." Foreign assistance has indeed virtually dried up at a time when the external debt stock is estimated to amount to approximately $17 billion--more than three times Sudan's GDP--with external payments arrears of $12 billion, including the $1.6 billion of arrears to the Fund.

Under these circumstances, it is necessary to reinvigorate the adjustment effort with a view to creating the favorable conditions to restore active cooperation with the Fund. It is not discouraging to hear that the authorities, in discussions with the staff, "reaffirmed their desire for an eventual normalization of relations and their readiness to maintain the dialogue." However, the authorities' declared commitment to a market-oriented economy led by the private sector should be backed by facts. As indicated by the staff, a key element to judge the authorities' commitment would be the introduction of a unified market-determined exchange rate, supported by tight credit conditions and a firm fiscal policy stance.

When this Board discussed the suspension of Sudan's voting rights, this chair supported the interpretation of the authorities' statement as a sincere desire to resume active cooperation with the Fund. The time has come to demonstrate it with policy corrections. We expect steady policy implementations for an early introduction of a unified market-determined exchange rate, allowing restoration of active cooperation with the Fund and the Bank to catalyze--as expressed by Mr. Dlamini in his opening statement--the much-needed financial assistance from the international community.

Mr. Obame said that he was reassured by Mr. Dlamini's statement, which noted that the authorities, during the Article IV consultation, had indicated their interest in maintaining a dialogue with the Fund to address the current macroeconomic imbalances facing their country. Sudan's economic and financial situation was extremely difficult and would remain so over the medium term if the authorities did not implement a strong adjustment program. Therefore, he hoped that the emerging adjustment process would be pursued and strengthened in order to cooperate actively with the Fund.

He agreed with previous speakers that, without external assistance, the country's problems would be difficult to resolve, Mr. Obame continued. It was up to the authorities to agree to the conditions of that assistance, which he hoped would soon be forthcoming.

The Chairman noted that, as evident from experience, correct economic policies generally led to external support. However, the Executive Board did not appear to be convinced that the Sudanese authorities had made sufficient changes to warrant such support.

The staff representative from the Middle Eastern Department observed that military expenditures, as represented in the fiscal accounts, measured between 2 percent and 3 percent of GDP. The staff had discussed the figure with the authorities, who maintained that it was a comprehensive one. Outside estimates were slightly higher--4-5 percent of GDP. The achievement of peace would have an impact at the budgetary level, as considerable resources could be freed for rebuilding of infrastructure. The continuing conflict in the South also indirectly affected the economy, as it was among the obstacles to a resumption of foreign assistance. Another indirect effect in the medium term was the lack of private sector reflows and capital formation. Hence, both directly and indirectly, the conflict had a considerable impact on the economy.

Mr. Dlamini remarked that both the authorities and the staff had shown pragmatism in their consideration of the economic conditions in the Sudan.

The Chairman made the following summing up:

Executive Directors praised and gave their endorsement to the appraisal contained in the staff report for the 1993 consultation with Sudan. Despite two consecutive years of good weather-driven rapid growth, Directors observed that there had been no corresponding improvement in economic policies and that the large imbalances in the economy had been reflected in very high rates of monetary expansion and inflation. In addition, Directors observed that Sudan continued to face extreme pressures in its external accounts manifested by declining export receipts, remittances, and other inflows that severely limited the economy's import capacity. The exchange rate remained under pressure and external arrears continued to mount.

Directors regretted that a competitive foreign exchange market had not been introduced by the authorities and that pressures on the exchange rate had been met by a reversal of policy reforms. Directors stressed the urgent need for action in reforming the foreign exchange and trade systems and eliminating remaining price controls. They remarked on the recent significant depreciation of the Sudanese pound in the official and parallel markets, and they reaffirmed the need for the authorities to unify the exchange rate and support it by tight credit and fiscal policies, with a view to curbing inflationary pressures. In the absence of such actions, the recent limited progress in Sudan's economic performance could be placed in jeopardy.

Directors emphasized the need to reduce the budget deficit substantially through a combination of revenue increases and current expenditure cuts, while safeguarding, as much as possible, essential public investments. They considered that tight monetary and fiscal policies were crucial to arrest Sudan's vicious cycle of inflation and devaluation. Positive real rates of return in the financial sector were also necessary to increase domestic savings and investment and to channel such savings into their most productive uses. Directors also urged the authorities to contain the rapid expansion in domestic credit creation, which fueled inflationary pressures and eroded the competitiveness of Sudan's exports by contributing to a large appreciation of its real effective exchange rate.

Directors emphasized the enormous cost to Sudan's already very poor population of the continuation of inward-looking policies and the piecemeal approach to economic management. They also observed that the Sudanese authorities were unduly optimistic with regard to the 1994 outlook for growth, inflation, the fiscal position, and the external balance. All speakers, therefore, urged Sudan to adopt and implement a comprehensive and outward-looking adjustment and reform plan, as has been outlined to them by the staff.

Directors noted with disappointment the failure of Sudan to make payments on arrears to the Fund, even at the very minimal level proposed by the authorities themselves. Also, several speakers observed that the size of Sudan's arrears to the Fund placed an unfair burden on other low-income countries. Directors also noted that Sudan's failure to meet its overdue financial obligations under the Articles of Agreement had resulted in the suspension of its voting rights as of August 9, 1993, and they expressed the hope that Sudan would speedily act to fulfill its obligations to the Fund. Noting also the effects of reduced foreign assistance on Sudan's task of adjustment and stabilization, Directors stressed that sustained and strong policies were essential to convince donors of Sudan's commitment to adjustment and, indeed, to restore its active cooperation with the Fund.

It is expected that the next Article IV consultation with Sudan will be held on the standard 12-month cycle.

The Executive Board then took the following decision:

Decision Concluding Article XIV Consultation

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 1993 Article XIV consultation with Sudan, in the light of the 1993 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/93/222, 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, a bilateral payments agreement with a Fund member, and limitation on the availability of foreign exchange for invisibles other than foreign travel, 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 urges the authorities to eliminate the above-stated restrictions and multiple currency practices and to eliminate the restrictive features of the bilateral payments agreement as soon as possible.

Decision No. 10506 (93/154), adopted
November 5, 1993

2. BARBADOS - 1993 ARTICLE IV CONSULTATION

Executive Directors considered the staff report for the 1993 Article IV consultation with Barbados (SM/93/168, 7/29/93). They also had before them a statistical annex (SM/93/176, 8/12/93).

The staff representative from the Western Hemisphere Department made the following statement:

> During October 5-15, 1993 a mission visited Bridgetown to initiate discussions on a program that could be monitored under the procedure of enhanced surveillance. The mission found that in recent months Barbados has made significant progress with structural reforms, whereas performance under the financial program for fiscal year 1993/94 has been mixed. The authorities are making certain policy corrections to strengthen Barbados external position in the remainder of 1993/94 and are working on defining further their policies for 1994/95.
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> This week Barbados accepted the obligations of Article VIII.
>
> In the area of tax and trade reforms, a uniform value-added tax (VAT) rate has been defined, except for the hotel industry where a decision is still pending, and technical assistance for the implementation of the value-added tax will be provided by the Inter-American Development (IDB) Bank over the next 18 months. The replacement of most import quotas with import duty surcharges was approved by Parliament in July 1993 and will become effective this month.
>
> In September 1993, management of the privately owned sugar sector was taken over by a firm of international experts appointed by the Government; this involved, as a prior step, the leasing of both the assets of the sugar factories and the management rights of the heavily indebted plantations to a government-owned trust company. At the same time, the nonperforming debts of the sugar industry--equivalent to 5.7 percent of GDP--were purchased with government bonds by the trust company from the insolvent government-owned Barbados National Bank (BNB). In addition to the above-mentioned debt swap, the Government also relieved the Barbados National Bank from all its nonperforming loans that were guaranteed by the Government--equivalent to 2.0 percent of GDP. The interest cost of these debt operations has been incorporated into the central government budget. Last month the authorities agreed with an IDB mission on a restructuring scheme for the BNB that would aim at its eventual liquidation or privatization. Furthermore, work is proceeding with technical assistance from the World Bank on proposals for amending the severance pay scheme and restructuring the public enterprise sector and public expenditure.

Prospects for raising US$14 million of divestment revenue--included in the 1993/94 budget--improved last month when the cabinet authorized the sale of the Arawak cement plant and of 85 percent of the government shares in the Heywoods Hotel and Resort. Also, the authorities believe that negotiations on the divestment of the country's two oil companies are sufficiently advanced to conclude their sale before end-1993/94. Furthermore, the transport company CARICARGO--which was jointly owned with the Government of Trinidad and Tobago--was liquidated in October and the Government of Trinidad and Tobago reimbursed the Barbados National Bank for delinquent debts of BDS$33 million owed by CARICARGO equivalent to US$16 million.

Preliminary information for the first half of 1993/94 suggests that a moderate recovery is under way after three years of economic contraction, and employment has been increasing, in particular in manufacturing and financial and business services. Private investment, mostly in tourism facilities and in the retail sector, offset a shortfall in central government investment. At the same time, inflation has decelerated faster than expected and the 12-month increase in consumer prices at end-1993/94 is likely to be around 3 1/2 percent, below the initial projection of 4 1/2 percent. The mission found broad public support for the incomes policy that was defined in the tripartite agreement of August 1993. The social partners have begun to collaborate on the application of the guidelines, which call for a two-year freeze of basic wages--through March 1995--and bonus payments on the basis of measured productivity increases or profit-sharing arrangements.

While the economy performed in line with projections in the first quarter of 1993/94, in the subsequent quarter--ended September 1993--the Central Bank lost US$36 million in international reserves, compared with a projected seasonal decline of US$6 million. This loss is attributable in part to the attempt of the Central Bank to engineer a decline in interest rates. The private sector responded by shifting deposits out of the banking system to higher-yielding deposits with trading and manufacturing companies, which used these funds mostly for restocking and other investments. At the same time, commercial banks continued to meet private sector credit demand by running down their excess liquidity. These developments contributed to a faster than expected rise in imports. In addition, in the second quarter of 1993/94 tourism earnings were weaker than projected as growth in tourist arrivals slowed--compared with the first quarter of the fiscal year--and hotels offered steep price discounts. Furthermore, delays in the start-up of certain government projects kept foreign financing below projections.

Through the first half of 1993/94 the overall position of the consolidated public sector was better than projected--with a surplus of BDS$12.5 million compared with the planned equilibrium--mainly because of larger social security contributions reflecting higher formal employment and more timely payment. The Central Government had accumulated a margin of BDS$7 million in the first quarter--compared with the objective--but lost most of it in the second quarter, as collection of taxes on profits, income, and property was below projections.

The authorities recently took steps to tighten financial policies in order to begin to recover the reserve loss noted above. The main emphasis is on slowing credit expansion and improving incentives for financial savings. The Central Bank intends to intensify open market sales, and last week it announced an increase in the anchor interest rate--the mandatory minimum rate on savings deposits--from 4 percent to 5 percent. In addition, the authorities have decided to introduce some cuts in government current expenditures and to strengthen the administration of direct taxes, where collection has weakened recently. On this basis, in 1993/94 the central government deficit would be contained at 0.3 percent of GDP--compared with a deficit of 0.5 percent of GDP envisaged earlier--and the overall public sector is anticipated to achieve a surplus of 1.3 percent of GDP--compared with a surplus of 0.8 percent of GDP.

The authorities believe that the projected growth of real GDP of 1 3/4 percent for 1993/94 is still achievable. In the light of developments and with the measures referred to above, the authorities expect the balance of payments to show a surplus of US$9 million in 1993/94, compared with an initial target of US$19 million.

The authorities expect to complete soon the preparatory work for policies in 1994/95, and plan subsequently to resume discussions with the staff on the terms for enhanced surveillance.

Mr. Smee made the following statement:

The report of the staff on the Article IV consultation with Barbados reflects the continuing commitment of my Barbadian authorities to ensure orderly growth on the basis of stable fiscal and monetary conditions, complemented by a comprehensive program of structural reforms. The staff also reports the intention of my authorities to request in the near future the application of the procedures of enhanced surveillance, and the Barbados Government is looking forward to the presentation of a program to the Board for this purpose.

The adjustment efforts pursued by Barbados in recent times, with the support of the Fund through the stand-by arrangement which ended in May this year, and through the program that the authorities have been pursuing subsequently, are basically aimed at restoring and maintaining the tradition of sound economic performance for which Barbados is known. Practically all observers of Barbadian conditions would endorse the observation in the staff report that Barbados, over the years, has achieved a relatively high per capita income under conditions of low inflation, low external indebtedness, and a solid social and economic infrastructure.

In seeking to maintain this tradition, my Barbadian authorities recognize that problems of competitiveness of their economy emerged during the course of the 1980s, and it is known that the external position deteriorated over the period 1989-91.

The response of the authorities in September 1991, when liquid foreign reserves were down to 1 1/3 weeks of imports, reflected their commitment and determination to take the necessary steps to reverse the emerging problems. Strong measures were taken at that time to reduce the fiscal deficit substantially--from 7.5 percent of GDP in 1990/91 to 0.3 percent of GDP in 1991/92, improving further to reach a surplus of 1.4 percent of GDP in 1992/93--and monetary policy was considerably tightened.

My Barbadian authorities feel gratified that in the 16-month stand-by arrangement that ended in May 1993, the quantitative targets for the five quarters covered by the arrangement were all met with comfortable margins, except for the target in the fifth and last quarter for the Central Government's overall deficit. This outstanding performance reflected the commitment of the authorities during the stand-by arrangement to be resolute in pursuing the strong measures required to stabilize the economy and lay the foundation for a resumption of soundly based growth.

The authorities regret that the final review under the stand-by arrangement was not concluded because of the slower than expected implementation of structural reforms. However, my authorities would wish to draw attention to two considerations. The first is that even though there were slippages in implementation of some structural measures during the stand-by agreement that ended in May 1993, there was solid progress in other areas of reform. In particular, the reform of direct taxation was introduced, aimed, among other things, at simplification of the tax system, reduction of the tax burden, and broadening of the tax base; and action was taken, in cooperation with Barbados' Caribbean Common Market partners, to reform customs tariffs by introducing fewer and lower rates.

The second consideration is that even those reforms that had experienced slippages have nevertheless been the subject of serious attention, both during the stand-by agreement and subsequently. There has clearly been movement toward implementation of the overall program of divestment and rationalization of public enterprises. The Barbados Flour Mill was divested in May 1992, and agreement has been reached with Trinidad and Tobago, joint owner with Barbados of the air freight operation CARICARGO, on action to liquidate the company. Preparations and negotiations for divestment are proceeding in connection with other enterprises such as Heywoods Hotel and Resort, Arawak cement plant, National Oil Corporation, and the National Petroleum Company.

During the Article IV consultation in May, my Barbadian authorities were pleased to discuss and reach agreement with the staff on a revised timetable for action in 1993/94 on these and other areas. These included plans to reform indirect taxation, principally through the introduction of a value-added tax regime; the execution of a comprehensive expenditure analysis with a view to restructuring central government expenditure over the medium term; measures to strengthen performance of public enterprises; development of a comprehensive tourism strategy; and streamlining of the operational modalities of an incomes policy. The record to date shows significant progress in most of these areas as illustrated in the statement by the staff.

Conscious of the important role that fiscal and monetary policy will have to play in the short and medium term in anchoring their continuing adjustment effort, my Barbadian authorities have responded to recent indications of renewed decline in international reserves and falling levels of deposits in the banking system by raising, with effect from November 1, 1993, the minimum prescribed interest rate on savings deposits from 4 percent to 5 percent. They also have decided to make some cuts in central government expenditure.

My authorities accept the observation in the Article IV consultation report that the continuing challenge for Barbados as it goes through 1993/94 will be to encourage economic activity while maintaining financial stability and to strike a balance between increased activity, on the one hand, and "protecting the still vulnerable external position," on the other.

The current outlook following the corrective measures that have been and are being taken is that projected real GDP growth for 1993/94 remains at about 1 3/4 percent; the external position will recover sufficiently for net international reserves to improve by BD$19 million--as against the BD$38.4 million originally projected--the expected end-year inflation of about 3.5 percent will be lower than the original projection, and will put Barbados' inflation rate at about the same general level of inflation being experienced by its principal trading partners among the major industrial countries; and the overall public sector is expected to do better than originally projected and achieve a surplus of 1.5 percent of GDP, incorporating a central government deficit of 0.3 percent of GDP.

In the expectation of a satisfactory outcome for 1993/94, my Barbadian authorities are advanced in their preparations for early resumption of discussions with the staff on a program that would be subject to the procedures of enhanced surveillance.

Miss Chang Fong made the following statement:

We note that, owing to slippages in the implementation of structural reforms and financial policies, Barbados' final review under the stand-by arrangement was not completed, and the stand-by arrangement expired on May 31, 1993 with an undrawn balance of SDR 9.2 million. That notwithstanding, the Barbados authorities feel capable of making up lost ground and have indicated their intention to seek agreement on a program that could be monitored under the procedures for enhanced surveillance.

As a bilateral partner of Barbados, we have noted that Barbados has over the years demonstrated prudent financial management and has enjoyed steady economic growth with low inflation until very recently. The staff's recent statement notes that the Barbadian authorities have taken the opportunity in the current budget period to accelerate the structural reforms and to consolidate the fiscal gains made in the previous two years. It would appear from the staff's recent update that, while the results have been mixed, the outlook remains promising.

Since the end of fiscal year 1990/1991, real GNP has contracted by 8.3 percent and unemployment had increased from 17.1 to 23.4 percent. It certainly makes the medium term look more optimistic that the authorities have succeeded in forging social acceptance for the incomes policy, which involves a two-year basic wage freeze with future wage increases tied to productivity improvements. Given the authorities' fixed exchange rate policy and the concerns about cost competitiveness, the incomes policy should begin to provide the necessary flexibility to compete with some of Barbados's regional neighbors who have benefited from exchange rate adjustments.

In 1992/93, public sector operations achieved a surplus of 1.4 percent of GDP which was equivalent to the surplus of the public enterprises. Even excluding these enterprises, the Central Government did improve its outturn from a deficit of 0.9 percent of GDP in 1991/92 to a virtual balance in 1992/93, owing mainly to cuts in capital expenditures and public service employment. We agree with the authorities' intention to restore, over the medium term, the previous level of capital expenditures, which are important for future economic growth. However, this will clearly require more substantial cuts in current expenditure, as the proposed tax reform--necessary in part to facilitate administration but, as important, to encourage a renewal of private sector activity--is expected to result in an initial fall in the tax revenue.

On the public enterprises, we welcome the resolution of the long-outstanding matter of the restructuring of the sugar industry and the assumption of its cumulated debts by the issuance of government bonds. We understand that, in fact, these are debts mainly of the privately owned sugar plantations but assumed by the Government in the wider public interest. These bonds have, however, increased the long-term liabilities of the Government. While deferring the immediate need for settlement, the current claims on the government budget for servicing the debt will increase. The sale of CARICARGO, the air freight company, may redress some of this additional expenditure. The removal of these significant bad loans from the Barbados National Bank can also improve the prospects for the bank to continue as a going concern.

The elimination of the fiscal deficit in the past year acted as a brake on credit expansion. Barbados' situation was further assisted by the apparent depressed demand for credit from the private sector, as evidenced by the surplus liquidity of the commercial banking system and the fall in deposit rates. Lending rates did not follow suit. Thus, gross international reserves improved from one week of imports to 2.7 months at the end of 1992/93. Subsequently, in the current fiscal year 1993/94, lending rates fell under pressure, private sector demand for credit revived, and Barbados suffered a loss of US$36 million in international reserves as of September 1993. The recent staff statement indicates that corrective action has since been taken.

The recent staff paper also points to favorable developments in several areas in the last six months--growth, employment, and private investment. There was clearly some cost to these favorable results, including a loss of international reserves as discussed earlier. The dilemma that faces the authorities is, therefore, to find the so far elusive appropriate mix of policies that would enable a sustainable external balance while maintaining growth.

We agree with the staff on the importance of improving the tourism sector, as it is a major contributor to the economy and to employment. It becomes more critical as the competition among, and additions to, Caribbean tourist destinations increases. The major requirement seems to be the upgrading of the existing hotel plant. The proposed structural reforms--such as lower tariffs and lower taxes on hotel industry inputs--will be helpful in removing the disincentives to private sector willingness to rehabilitate the hotel industry.

Moves to liberalize interest rates should serve to improve the incentives for increasing financial savings. Gross national savings in relation to GNP have been rising, albeit slowly, over the last five years, and it will be necessary for the private sector to generate the necessary investment if growth and employment are to be maintained.

Barbados' intention to seek enhanced surveillance is indicative of its wish to access credit from multilateral institutions in support of policy reforms and also to access moderate amounts from commercial sources, which is consistent with Barbados' long history of conservative debt management. We feel that there is a basis for a successful conclusion to the discussions on a relevant program. Much of the staff's medium-term projections are favorable and are premised on the maintenance of structural reforms, tight monetary and fiscal policies, and, most important, continued wage restraint. The continuing social support for the adjustment program no doubt depends upon tangible benefits coming to light, in particular increased economic growth and lower unemployment.

Mr. Dorrington made the following statement:

Perhaps I should say first that I agree with everything that is in the staff appraisal and everything that Miss Chang Fong has just said.

It seems to be a tradition in this Board to describe opening statements as "helpful." The two we received in connection with Barbados' Article IV consultation are certainly that. More important, they are encouraging. The staff report left me feeling uncomfortable with the pace of Barbados' structural reforms. The staff's helpful statement, reporting significant progress with structural reforms, removed some of that discomfort. Nevertheless, macroeconomic performance, which had previously been excellent, has recently been more mixed. This underlines my basic reaction to the papers in front of us--the Barbadian authorities have a strong commitment to doing all the right things, but they seem unable to do them all right at the same time.

Of the new information in the staff statement, I am delighted, in particular, that the long-awaited contract for management of the sugar sector has been concluded. It has been clear for some time that the Barbadian authorities were aware of the severe problems in the sugar industries and were committed to solving them. While the necessary steps should have been taken earlier, the Barbadian authorities nonetheless are to be commended for finding a solution that enables the industry to remain privately owned. I am glad that they resisted any temptation to take the far easier route of nationalization.

In the past, the Barbadian authorities have made great strides in improving the tax system based on the principles of simplicity and base broadening, and steps are now being taken toward the introduction of a value-added tax. I would encourage the Barbadian authorities not to underestimate the work involved in getting the new VAT up and running; we have seen elsewhere that it often takes longer than expected, and the timetable the authorities have set themselves looks optimistic. Certainly no time can be wasted if this timetable is to be adhered to.

Another area where planning ahead will be necessary, where there have been slippages in timetables in the past but some good news recently, is the divestiture program. I urge the authorities to maintain a steady flow of enterprises coming to the market.

Before moving on to what remains to be done, I want explicitly to welcome two other measures: the end of most import quotas and the acceptance of Article VIII status.

Of course, much remains to be done. I fully agree with the staff's assessment that restructuring public expenditure is a priority. I also share the staff's view that this restructuring should focus on making room for necessary capital expenditure by cutting back current expenditure, especially the wage bill. I note that the economy has benefited from a de facto freeze in private wages. The authorities propose to institutionalize wage restraint through an incomes policy. This may be the only effective way of containing wage settlements in the short run, and that is certainly essential. But there is surely something very wrong with the labor market when such measures are necessary, i.e., when measured unemployment is over 20 percent. Thus, I hope that the authorities will accompany legislation with a thorough analysis of the reasons behind the labor market problems and then tackle these causes. I would welcome staff comments on this. In this respect, I note the staff report's assessment that significant improvements in competitiveness only occurred where there were changes in the way labor was used, including increases in part-time working.

Labor costs are especially crucial in determining the competitiveness of Barbados' tourist industry, as the staff's statistical annex points out. In turn, an increase in tourist arrivals is the key determinant of the growth forecasts. While the staff report seems quite confident about the projected expansion in tourism, the analysis in the statistical annex is less sanguine. Barbados' share of tourist arrivals in the Caribbean has fallen steadily over the past few years, and I hope the Barbadian authorities will lose no time in implementing a strategy to restore their island's position in the Caribbean tourist market.

The statistical annex also identifies the exchange rate as a contributor to Barbados' decline in competitiveness. I have some sympathy with the argument that breaking the established link with the U.S. dollar would increase financial instability. From the balance of payments figures, and more informally from looking at a package holiday brochure last night, the extent of any misalignment does not appear to be too great to be solved by differential changes in domestic costs and prices. I do not therefore propose to argue for devaluation. But this reinforces the need to take steps to contain domestic costs--especially labor.

Turning explicitly to future arrangements with the Fund, it is clear to me that enhanced surveillance is the right approach for Barbados. Progress already made means that Barbados probably no longer has a balance of payments need for a further Fund program in the conventional sense. But Barbados certainly does need policies capable of support under the upper credit tranches, and it needs the monitoring, etc., that would be provided under a stand-by arrangement. A continuing close relationship between the Fund and the Barbadian authorities should have benefits both in defining the economic program and in helping to keep it on track.

Furthermore, this will be necessary to give the needed confidence to potential creditors. Indeed, to serve this purpose it is essential that the enhanced surveillance process be as rigorous and transparent at all stages as an upper credit tranche arrangement. Anything less would undermine the whole process of enhanced surveillance, and this would be to the detriment of Barbados, and of a number of other members in similar circumstances in this regard. Only when the Barbadian authorities are able to agree and to start to implement a set of policies that passes this test should we move into enhanced surveillance. Meanwhile, some form of informal monitoring and consultation with the staff should pave the way.

I have been impressed by the commitment of the authorities and, given the size of the country, I recognize the limits on implementation capacity. It is essential that the best use be made of that limited capacity and that priorities be set and followed. I hope that the authorities will work with the staff to produce a letter of intent that is both ambitious and realistic. I hope, and indeed expect, that it will not be too many months before we see that document, and I look forward to it.

Mr. Matthews made the following statement:

The authorities are to be congratulated on the program of economic reforms that has been introduced over the last few years. A key focus of these reforms has been the impressive consolidation of fiscal policy, resulting in a turnaround in the budget deficit of over 7 percentage points of GDP. The authorities' commitment to this reform was shown in the past year when, in the face of an unexpected shortfall in revenue, the authorities prevented an adverse effect on the deficit by further reducing government spending. The beneficial effects of this action have been widespread. Not least among these was that the Central Bank was allowed to loosen monetary policy--though this loosening seems to have been taken somewhat too far--and to move away from direct credit ceilings.

At first glance, one could argue that the fiscal reforms already introduced and those planned for the remainder of 1993/94 would provide a sound fiscal base for the medium term. However, to date, a large part of the fiscal effort has been achieved through lower development expenditure--something that cannot be maintained over the medium term. We would therefore agree with the staff that further consolidation will be required, particularly in limiting recurrent expenditures, if the authorities' plans to increase development expenditure and to reduce some elements of taxation are not to result in a large blow-out in the fiscal deficit.

Central to the economic problems that have recently faced Barbados and a key to its economic future is the issue of competitiveness. The authorities clearly recognize lack of competitiveness as a problem and their efforts thus far to overcome this problem have been commendable. An important part of this effort has been the government-sponsored freeze on wages growth. History has shown us that wage freezes often do not provide a lasting solution to competitiveness problems because the thawing process can result in "catch-up" claims and wage-price spirals. However, there is some reason to be optimistic in this case. First, there appears to have been quite widespread recognition in the community that improvements in competitiveness are needed. Second, the current system does allow for wage increases if they are linked to productivity and profitability, thereby providing an avenue for real wage increases and reducing concerns over wage breakouts.

While these features might suggest that the current wage system should be maintained, it is important not to underestimate the role that needs to be played by the Government. This role includes ensuring that the necessary institutions, such as the Productivity Board and the Severance Fund, are functioning properly. The Government must also be seen to be setting the right example. In this regard, it was of concern to read that the Government had granted wage increases for civil servants well beyond what could have been expected on the basis of productivity improvements. I can understand that this may have been a reversal of the nominal wage cut taken by civil servants in 1991, but the commitment of the community to the wage guideline may have been damaged. I would appreciate the staff's views on this point.

But the wage system alone cannot solve all of the competitiveness problems in Barbados. Structural reform also has a very important part to play. It was somewhat disappointing then that the failure to conclude the final review of the stand-by arrangement came about partly because of slippages in the implementation of structural reform. The positive statements made by Mr. Smee regarding the strong commitment of his authorities to continued structural reform auger well for the quick implementation of outstanding measures.

Even with real wage restraint and accelerated structural reform, the road to improved competitiveness will be a long one, as can be seen clearly in the thorough analysis of the tourism sector provided in the background paper. The tourism-weighted real effective exchange rate appreciated by over 30 percent between 1980 and 1992, a loss that will take many years to claw back. With the need to overcome this large loss of competitiveness now quite urgent, I agree with the staff that the authorities should give further serious consideration to a nominal depreciation of the exchange rate. To be sure, such a strategy would place strains on the consensual incomes policy, but the current strategy will also put strains on incomes policy because restraint will be needed for many years. If a nominal depreciation continues to be eschewed by the authorities, it is likely that they will continue to come up against the balance of payments constraint whenever they try to stimulate growth, as the most recent episode has shown. If matched with appropriate economic policies, a nominal depreciation could make the adjustment path shorter and provide scope for early reductions in what is now very high unemployment. Perhaps this is an issue that could be discussed with the authorities in the context of enhanced surveillance.

Mr. Wire made the following statement:

Barbados has made a very commendable effort over the past two years to restore macroeconomic stability. As noted by previous speakers, implementation of strong fiscal adjustment measures, monetary tightening, and wage restraint have led to a substantial improvement in long-term economic prospects. The payoffs of sticking with a tough adjustment plan are becoming evident. The recovery appears to be under way, with modest growth, improved price stability, and a somewhat stronger external position in store for this fiscal year.

Nonetheless, Barbados still has some way to go to improve its external viability. The authorities seem to recognize the need to improve competitiveness throughout the economy and to reduce the high level of unemployment. A number of measures they have implemented or are contemplating in this regard will be useful. However, this process will clearly be a long-term proposition.

As we broadly agree with the comments and concerns of the previous speakers, I have just a few points to make. On the structural side, the renewed commitment to structural reform is commendable. We particularly welcome indications that preparations for privatization of a number of enterprises are moving forward, but there is a real need to bring these deals to closure as soon as possible. We also welcome the progress in restructuring the sugar industry.

With regard to incomes policy, the new wage pact agreed upon in August represents helpful additional restraint, and we look forward to its full implementation.

On the monetary side, the recent reserve losses point to a need to fully liberalize interest rates and to continue the process of financial sector reform.

Still, as other speakers have noted, it is not completely clear to us that continued tight financial policies, a tightened incomes policy, and an array of other measures envisioned by the authorities will be sufficient to bring about desired and necessary improvements in competitiveness in the time frame desired by the authorities. In this regard, we share the concerns expressed by the staff and by Mr. Matthews. Clearly, the approach adopted by the authorities deserves some time to work, but it also may be useful to have contingency measures in hand. The main element of contingency measures would obviously need to be strengthened internal adjustment. In this regard, we agree with the comments made by the staff and other speakers.

However, it also appears to us that there is some scope for exchange rate adjustment, because competitiveness developments are not particularly encouraging, as Mr. Matthews has noted. The staff reports real effective appreciation of some 8 percent from the outset of the adjustment effort through March 1993; compared to a sample of neighbors competing for tourists, real appreciation has been even larger. There does seem to be some agreement that the external position remains weak; though recent export performance has been buoyant, tourism performance has lagged. Reserves fell substantially in the July-September quarter and need to be rebuilt. Unemployment remains quite high at around 25 percent of the work force. The downside risks of exchange rate adjustment seem limited, particularly as inflation has come down to 3.5 percent--below initial projections--and the fiscal position remains fairly strong. In any case, let me reiterate that we would see this as a complementary measure to strengthened internal adjustment should the authorities' current projections not prove to be materializing on the timetable that they envision.

With regard to the authorities' interest in enhanced surveillance, this may be a case where it would be appropriate for the Board to consider an appropriately quantified and rigorous arrangement, in line with the January 1993 guidelines approved by the Board. The lack of progress on structural issues that derailed the stand-by arrangement is being addressed, and, as already noted, financial policies have been broadly appropriate. Like Mr. Dorrington, we do not see the need for a Fund program, but we do see catalytic benefits that may result. I agree with the staff that the authorities would need to present a strong and detailed plan for the coming fiscal year, in line with the probable timing of a possible enhanced surveillance arrangement. We look forward to hearing the outcome of the staff's discussions with the authorities on this.

Finally, we welcome the recent move to Article VIII status.

Mr. Wang made the following statement:

The authorities are to be commended for the headway made in adjusting the economy. With the notable adjustment efforts envisaged in the Fund-supported program, especially in the fiscal area, impressive progress has been made in achieving a public sector surplus and lowering the underlying inflation to 3 percent. Equally commendable is the remarkable achievement in maintaining a favorable balance of payments position. Notwithstanding this progress, it is worrisome that real GDP growth has continued to shrink and unemployment has accelerated, largely on account of the authorities' intense demand management policy. Structural reform has also witnessed some slippages.

In our view, the Barbadian economy is now at a critical juncture. The major imbalances in the economy have been corrected, laying a sound foundation for sustained growth in the short and medium term. The authorities should be encouraged to embark on a renewed adjustment and stabilization program to further consolidate their adjustment gains and bring about a sustainable and balanced growth. At this crucial stage, the formidable challenge facing the authorities is to revitalize the contracted growth, while tackling the structural impediments through broadening and deepening programmed reforms in a decisive fashion. In this regard, it is encouraging to know from the staff's statement that a moderate growth recovery is gaining momentum and that progress with structural reform is under way.

Broadly speaking, I agree with the thrust of the staff appraisal and appreciate the updated information; thus I will confine myself to the following brief remarks.

The improvement of financial stability will play a central role in promoting Barbados' external competitiveness, which is critical to the export-oriented and private sector-led growth strategy. In this regard, a tight fiscal policy should be implemented until the fiscal position improves substantially; this would reduce inflation, facilitate rationalization of interest rates, and alleviate balance of payments pressures. To create room for a healthy and sustainable growth in the medium term, the top priority of fiscal policy should be to overhaul and reconstruct the expenditure structure, including a cut in current spending. In addition, much effort needs to be devoted to the reinforcement of revenue collection, with particular emphasis on strengthening and reforming the tax system. This underscores the necessity and urgency of accelerating other envisaged structural reforms, including the delayed divestment program.

With respect to the exchange rate policy, we note with concern that the external account remains fragile mainly on account of its critical dependence on the tourist sector. Given the limited diversification of its exports, and in view of the increased competitiveness from neighboring countries, maintaining a viable balance of payments position would primarily hinge on the strength of domestic reforms and adjustment efforts. In this connection, we encourage and welcome the authorities' commitment to pursue a tight fiscal and monetary policy stance and a prudent external borrowing policy. However, according to the staff, the real effective exchange rate appreciated by 8 percent through March 1993, which could further erode external competitiveness. While I concur with the authorities' concern over the possible adverse impact on inflation pressures, the financial system destabilization, and incomes policy, fine-tuning the exchange rate with a view to carefully maintaining a flexible and responsive exchange rate policy should not be ruled out as a means of improving Barbados external competitiveness. As this point was mentioned by the previous speakers, the staff's view on the appropriateness of devaluation by some margin would be appreciated.

Like previous speakers, we are also concerned about the renewed decline in international reserves and the falling level of deposits in the banking system. However, it is encouraging to note from Mr. Smee's very helpful statement that the authorities have raised the minimum interest rate from 4 percent to 5 percent. I am wondering whether this measure is sufficient to address the issue or whether the staff have recommended any other measures.

Finally, we highly commend the authorities' willingness to have their economic program monitored through the Fund's enhanced surveillance procedures, which we hope the World Bank and Inter-American Development Bank can support. To this end, it is of vital importance that the authorities remain committed to the programmed adjustment and reform policies and stand ready to take the necessary measures in order to ensure the achievement of the medium-term adjustment strategy objectives.

With these remarks, I support the proposed decision and wish the authorities well in their endeavors.

The staff representative from the Western Hemisphere Department said that it was useful to put wage developments into a historical context. During the 1980s, wage increases in Barbados had been clearly too rapid; however, in 1991, during the financial crisis, disposable income had dropped sharply as a result of revenue measures, such as tax increases and increases in public service tariffs. At the time, there had been the temptation to make up for that drop in disposable income by increasing wages in the private sector. Instead, the Government had issued a wage guideline, and, although it had not been formally endorsed by the social partners, it had been tolerated to a degree. From 1991 until recently, there had been a de facto wage freeze as most wage contracts remained pending. The few settlements that took place were, to a large extent, limited to bonuses related to productivity increases. The exceptions to the freeze of basic wages were contracts with foreign-owned companies in which there had been small wage increases, but only in the order of 2-4 percentage points. Therefore, calculating the weighted effect of wage settlements during that period, the resulting increase in wages was very small.

A major breakthrough in wage bargaining had been the recent agreement between social partners on incomes policy, and they were pleased that the National Productivity Board had been restructured, the staff representative continued. The Board would now have equal participation by labor and employers, and would have the technical assistance of labor consultants provided by the World Bank. During the mission of May-June 1993, the staff had spoken with the social partners, who had confirmed that the so-called incomes protocol would be implemented within the next two years.

Unemployment was high in Barbados, the staff representative added, and the unions believed that it should be resolved not only through wage policy, but also with the appropriate training for the growth sectors. The unions had become involved in the instructional area, and employers had also indicated their interest in participating. Everyone agreed that the severance pay scheme was a hindrance to labor flexibility, and the scheme was being reformed, with World Bank technical assistance. A cabinet proposal on that reform was expected in early 1994.

The rollback of the wage cut in the public sector would not affect the private sector, the staff representative considered; the private sector viewed the reinstatement of civil servant wages as only fair because private sector wages had not been reduced at the time when civil servants had accepted a wage cut.

The staff believed that an increase in the mandatory minimum interest rate on savings deposits from 4 to 5 percent was one measure among several to resolve the monetary situation, the staff representative remarked. The Government planned to sell a number of treasury bills to restrict the commercial banks' ability to provide credit, and, because the bills would have attractive yields, even banks without excess reserves would wish to buy the bills and would invite deposits to fund their purchases. As a consequence, deposit building would no longer be discouraged. In the past, commercial banks had discouraged deposits by dropping those deposit rates that were not controlled to very low levels, because bank management felt constrained on the asset side by an agreement with the Central Bank that the prime rate not exceed 8 percent. It was clear that the whole interest rate structure, including the prime rate, had to be raised, and that that constraint was no longer relevant. More flexibility on the lending rate side, in combination with open market operations, would solve the recent monetary problem.

Mr. Smee remarked that the message to be derived from the Board discussion was the need for improved competitiveness; the staff report had identified it as the key to the future success of the Barbadian economy, including an increase in employment and growth. Directors had recognized that the authorities had made a considerable effort in the macroeconomic sphere, in particular with respect to structural changes, notwithstanding a few problems that had occurred. The Government had reiterated its commitment to structural reforms, and much progress had been made recently in that area. Anyone who read Appendix II of the staff report would be impressed by the depth and breadth of both the structural reforms that had already been implemented and those the Government had committed itself to implement in the future.

A fallback position for any country, in terms of improving competitiveness, was depreciating the exchange rate, Mr. Smee continued, but, as the staff report noted, Barbados had had an exchange rate fixed to the U.S. dollar since mid-1975, and it was obviously deeply committed to undertaking the necessary domestic reform to validate that rate. The authorities admitted that a loss in competitiveness had occurred, and they were fully committed to improving it through a more costly domestic route in terms of employment and output than through a nominal depreciation. They feared that a depreciation would be extremely destabilizing after so many years with a fixed exchange rate. Many of the country's costs were import costs, which, of course, would rise with a depreciation. Furthermore, the Government, because of its commitment to the exchange rate and the validating policies associated with it, would suffer a substantial loss in political credibility if a depreciation were required.

Nevertheless, the recent success at the macroeconomic level and the commitment to structural reform indicated that real progress was being made, Mr. Smee remarked. He hoped that the progress would continue with the assistance of an enhanced surveillance arrangement that had appropriate conditionality to catalyze other multilateral official funds, and the assistance of a modest amount of commercial financing. The enhanced surveillance arrangement would permit the Government to continue to receive policy advice from the Fund beyond that received from a normal Article IV consultation. Indeed, he and his authorities looked forward to returning to the Board in the near future with a successful application for an enhanced surveillance arrangement.

The Acting Chairman made the following summing up:

Executive Directors were in general agreement with the thrust of the staff appraisal. They commended the authorities for the decisive actions taken since September 1991, which had helped to achieve a major turnaround in Barbados' economic situation. Directors noted that the tightening of financial policies, together with a restrained incomes policy, had brought about a deceleration in underlying inflation, an improvement in the external situation, and strengthened confidence in the currency.

Directors acknowledged that the Government had to tighten financial policies more than originally envisaged in 1992/93 in the face of major shortfalls in tourism earnings and foreign financing, and this tightening of policies had contributed to the sluggishness of domestic demand. Directors encouraged Barbados to avoid further slippages in the divestment program and in the implementation of structural reforms, which had resulted in shortfalls in support from multilateral lending institutions in 1992/93.

Directors noted that the resumption of growth over the medium term depended on the strengthening of investment and savings, wage restraint, and the expeditious implementation of structural reforms in order to improve cost competitiveness.

Directors emphasized that the restructuring of government expenditure, with its emphasis on downsizing current outlays, was essential in order to make room for an adequate level of public investment while ensuring a satisfactory fiscal balance over the medium term. They welcomed the restructuring and reduction in taxation as steps toward improving competitiveness, and they urged the timely implementation of the proposed value-added tax. Directors endorsed the recent reforms in the sugar sector and in the Barbados National Bank. They added that a cautious monetary policy stance was needed to protect the external position.

In this context, Directors voiced concern over the recent fall in foreign reserves, which was related in part to a faster than expected expansion in private sector credit while domestic financial savings had weakened. Directors welcomed the authorities' steps to tighten financial policies and emphasized that the evolution of key monetary variables needed to be monitored closely.

With respect to wage policy, it was considered essential that the principle of basing pay awards on established productivity increases be adhered to. Directors stressed, therefore, the importance of fully implementing the tripartite agreement on incomes policy and eliminating labor market rigidities. Indeed, it was noted that the need to have an incomes policy, at a time of high unemployment, stressed the importance of reducing the labor market rigidities.

Directors noted that Barbados' balance of payments remained fragile and that underscored the need to strengthen competitiveness. Thus, Directors emphasized the need for the authorities to maintain sound fiscal, credit, and incomes policies and continue structural reforms. Some Directors indicated in this context that contingency plans needed to be kept in readiness to bolster domestic increases and adjust exchange rate policy if necessary. Directors encouraged the authorities to define a program for 1994/95 that could provide the basis for a request for Fund monitoring under the enhanced surveillance procedures, while also attracting support from the multilateral lending institutions.

The decision of Barbados to accept the obligations of Article VIII was noted, and the authorities were commended for maintaining an exchange system free of restrictions on the making of payments and transfers for current international transactions.

It is expected that the next Article IV consultation with Barbados will be held on the standard 12-month cycle.

3. ANNUAL MEETINGS - REVIEW

Executive Directors considered the Secretary's background note on Annual Meetings arrangements (EBD/93/171, 10/29/93).

Mr. Kafka made the following statement:

A few questions might be raised on the subject of Annual Meetings arrangements.

The problem of the need for annual, rather than biennial, meetings has again been mentioned. This question was discussed in 1974, and while there was some sympathy in the Fund's Executive Board for holding biennial meetings, the idea was rejected by the World Bank Directors on the grounds that they needed annual meetings in order to facilitate the sale of bonds. But there is a real problem here, as one could see from the embarrassing emptiness of this year's plenary sessions.

The need for semiannual meetings of the Interim and Development Committees could be raised, and--in fact--there is a plan to have a working group on the future of the Development Committee. What does this mean for the Interim Committee? Should its meetings be held on the basis of need only, or perhaps once a year--at the time of the Annual Meetings--with additional meetings on the basis of need? It could be argued that meetings where no decisions are taken detract from, rather than contribute to, the value of the Committee. The statute of the Development Committee speaks of one or more meetings a year; that of the Interim Committee, of three to four meetings a year. Thus we have already corrected our initial enthusiasm for more frequent Committee meetings.

As to the organization of Interim Committee meetings, should we attempt to have more focused meetings in the morning as well as in the afternoon, for example, by selecting main speakers on specific issues, although each member could submit a statement for the record?

While country-related meetings at the time of the Annual Meetings are useful, I wonder whether there is a genuine need for the simultaneous presence of staff from many departments. Even then, should there be a limit on the number of staff? On a recent occasion involving a meeting with a country in my constituency, I counted 3 country representatives and 12 Fund staff.

At this year's meetings, a spouse lunch was arranged on September 27 distinct from that for Governors' spouses, which took place earlier. As usual, Executive Directors' and Alternates' spouses were also invited to this luncheon, but, distinct from the invariable practice followed until this year, they were advised that their invitation was contingent on there being room available for them. We have never heard of anyone being invited on a contingent basis to anything, except where the contingency was connected with the weather. If it was not possible to accommodate everyone who might be interested, surely a different means of limiting attendance could have been found. I am sure there will be no repetition of this gaffe.

Mr. Wire made the following statement:

There appears to be a good deal of dissatisfaction with current Annual Meetings arrangements. As the background note points out, low attendance at all but the opening plenary session creates an unfortunate public impression. More than that, it raises questions as to whether the substantial time, effort, and money spent on these meetings currently is producing commensurate returns. I should note that the Annual Meetings have not been singled out for this sort of scrutiny. Dissatisfaction has also been expressed by heads of state in recent years with the way the summit meetings of the Group of Seven industrial countries have grown into overblown events that have detracted from their original purpose.

There is nothing in the Fund's Articles of Agreement that compels the convening of an Annual Meeting, although the By-Laws require that regular meetings take place, and there is the presumption that such meetings should take place on an annual basis. While it may be somewhat tempting to ask whether these meetings need to be held at all, we are inclined toward the view that they do serve a useful purpose--while recognizing the clear need for their improvement. The meetings establish a rhythm of high-level political attention to international economic issues as well as institutional concerns that is important and useful. Along those same lines, they provide a unique opportunity for interaction among a variety of participants in the international financial community that appears to be valued. Many of these benefits are intangible, but nonetheless valuable. Whether the meetings need to take place every year is perhaps an open question, but it does seem important that they take place on a regular basis.

That being said, the question then becomes how to make the meetings more effective. Cost containment is a clear concern. The costs associated with various social events receive a good deal of attention, as they should, but other items loom much larger. Chief among these are travel and per diem costs. We understand that about one half of Annual Meetings expenses comprise such spending. When meetings are held in Washington, these costs include the travel and per diem expenses of Governors and Alternate Governors paid for by the Fund and the Bank. When meetings are held abroad, there are additional costs associated with moving staff and management to the meetings' site, although we understand that some of these costs may be picked up by host governments. In any event, this is a large budget item to which some modifications could produce substantial savings. Greater emphasis on attendance by Joint Governors is one possible solution. Elimination of first-class travel is another.

On the issue of holding meetings abroad, it is our impression that these meetings are significantly more costly--notwithstanding the fact that certain expenses are offset by host countries. This practice clearly warrants close examination.

We would agree that the intention to hold the opening and plenary sessions of the Madrid Annual Meetings at different venues could serve as a useful guide for future meetings in Washington. Scaling back meeting halls to better match attendance is sensible and could result in budget savings, although the latter point is dependent on a variety of factors.

More discussion of these and other issues is needed and will require additional background information. It has already been agreed at the World Bank that a thorough review of the meetings, including costs, is needed. We look forward to such a review. Given the collaborative nature of the meetings, such a review would benefit from close cooperation between the two institutions--both in the preparation of documentation as well as its consideration. Among its other challenges, the background papers will need to take into account the different budget treatments employed by the Fund and the Bank in recognizing various expenses.

Advances in communications technology might be employed usefully to both enhance the quality of the meetings as well as lower their costs. This topic appears to be an area worthy of coverage in future papers.

Mr. Peretz made the following statement:

I fully agree with Mr. Wire's comments about the excessive attendance and formality of Group of Seven meetings, but that is not for us to discuss today. But it is a matter on which my own Prime Minister has been running an initiative for some time.

Experience with this year's Annual Meetings--the fourth I have attended--confirmed my view that the time has come to take a new look at the format of the meetings.

Dealing with the Interim and Development Committees first, we note that the review of the Development Committee's role and function is under way, probably overdue, and very welcome. On the Interim Committee, the format of the meetings seems to be relatively satisfactory, although more thought could be given to how we use the afternoon session or, indeed, to whether an afternoon session is always needed.

As to the Annual Meetings, I agree with Mr. Kafka and Mr. Wire that the format has become increasingly unsatisfactory. The sight of Governor after Governor addressing a vast empty meeting hall is not a happy one; it is not very polite to Governors, either. At the same time, many of those who wish to hear a particular Governor's address are choosing to do so on closed-circuit television rather than going to the meeting hall itself. This is partly owing to the queues for elevators in the hotel, but it is also a reflection of the availability of new technology. Moreover, the whole process of moving all our offices to the Sheraton Washington for 2 1/2 days also seems to be a thoroughly unsatisfactory one.

I would like to suggest that we consider changes along the following lines: that for the meetings held in Washington, we cease using the Sheraton Washington altogether and that we find a venue nearby to headquarters that is large enough for the opening ceremonies--which are attended and which include speeches by the Chairman of the Boards of Governors as well as the heads of institutions. One possibility would be to use the Fund's Atrium or nearby Constitution Hall for that purpose. Thereafter, we should adjourn the Annual Meetings to a room in the Fund or in the World Bank, perhaps the Meeting Hall used for the Interim Committee, and limit member countries to two seats each so that there would be seating for 400, and arrange for speeches to be transmitted on closed-circuit television throughout the Fund and the Bank. Governors and their staff could be accommodated in

Executive Directors' offices. For large constituencies, it would be necessary to find some additional office space in the headquarters buildings, which might mean some staff temporarily vacating their offices for two days.

We also ought to consider other possible cost-reducing measures, including reducing the number of Governors and Alternate Governors of the Fund and the Bank and the MIGA who qualify to have their travel and per diem costs paid, perhaps by limiting the number of persons reimbursed per country; and reducing the number of social events.

As the Annual Meetings are held jointly with the World Bank, I strongly urge that if we reconsider their format, we do so in consultation with our Bank colleagues. I know that at the request of World Bank Directors, the Bank's Secretary's Department is preparing a paper on options for change. I would like to suggest that the Board ask our Secretary and his staff to participate in this effort and make it a joint review paper, which this Board could then discuss as well as the Bank Board.

I hope we might think again about the possibility of levying a charge on commercial bankers and other nonofficial attendees. At the moment, bankers who come for the meetings have to pay premia of up to $200 a night in addition to the regular hotel charge; this is a measure of the demand to attend these meetings. This economic rent is being collected by Washington hotels at the moment; I think that we should try to collect some of it for ourselves.

Mr. Fukui made the following statement:

On the venue for the plenary sessions, the background note indicates that in Madrid, the opening session and subsequent plenary sessions will be held at separate venues and indicates that this arrangement may be continued after 1994. I support this proposal in view of the low level of attendance at all except the opening session, which has been of particular concern in recent years, and the unfortunate public impression that has been created. Moreover, if the opening session is held at a different venue, it will enable us to consider other hotels as the main venue after 1997, especially as the quality of the services of the Sheraton Washington Hotel is below our expectations in many respects.

As to the site of the Annual Meetings, I understand that some Executive Directors consider that the traditional practice of holding the meetings outside Washington, D.C. every third year should be abolished after 1997 mainly because of cost considerations. I believe that while cost factors are important, other factors should also be taken into account. For example, a host country can expect its prestige to rise in the financial community; this enhanced prestige increases its credibility and, thus, there is some return to the international financial community. I presume that in the future, a number of countries will wish to be chosen as the site of the Annual Meetings. Therefore, at this stage I do not want to rule out the possibility for potential candidates to host an Annual Meeting. At the same time, I would emphasize that more needs to be done to reduce costs, for example, by reducing the number of Fund staff sent to meetings held abroad.

Regarding the other issues for discussion, I believe that a quantitative analysis by the staff is indispensable for a discussion on reducing costs, including by reducing the size of delegations. Therefore, I would suggest that the Fund should consider the procedure that has been agreed in the Bank--namely, that a committee of the whole undertake a review of various aspects of the meetings on the basis of background material prepared by the staff.

Mr. Autheman made the following statement:

I share many of the views that have already been expressed and will focus on some points.

I do not question the need for Annual Meetings. In fact, my Finance Minister and Central Bank Governor do not feel the need to reconsider this issue. They have not noticed a change in views on this matter among many of their colleagues at the Annual Meetings. And I do not question the need for a twice-yearly meeting of the Interim Committee. I also do not question the principle of periodically holding Annual Meetings abroad. I agree with Mr. Fukui that if we were to reconsider this practice, all possibilities and not only the practice of holding meetings abroad should be open to review.

There is a need to find a solution for the sick body that the Development Committee has become. We hope that the small committee that has been established will put forward a proposal for dramatic changes, but we think that the Managing Director of the Fund and the President of the World Bank should consider making their own proposals for improving this Committee. We are not satisfied with the present evolution toward an academic forum, and there is a risk that attendance may decline further.

I strongly support the principle of changing the organization of the Annual Meetings. We regret that so many Governors speak before a sparse audience; we need to change that. The only way to improve attendance is by restricting it, thereby creating an incentive to attend. But we also have to take into account the availability of closed-circuit television. In this regard, we hope that the Madrid meetings will offer us an experiment and a precedent.

I agree with the staff's proposal to distinguish the opening session from the rest of the annual discussion. Obviously, the opening session has to remain a plenary session, with a large attendance. But, for the rest of the annual discussion, we should make use of existing closed-circuit television coverage. I would take exception to the view that we should make provisions for broad attendance during the rest of the discussion. We all know that many countries do not make use of the present seating capacity, so I think that we should instead fit the size of the room to the expected attendance.

I support the idea of reopening the issue of charging attendance fees. Our purpose is not to make a profit--we do not have the same goals as hotel owners--but rather, at the least, to recover expenses.

The Chairman said that he appreciated the preliminary arrangements under consideration for the Madrid meetings precisely because they provided for a large plenary at the opening session and for a smaller plenary to accommodate subsequent sessions, which should create a compact audience for Ministers addressing the meetings. He hoped that the restricted character of the annual discussion would have the effect on attendance that Mr. Autheman anticipated.

Ms. McDougall made the following statement:

Our observations from the most recent Annual Meetings leave us favorably disposed toward a thorough review of arrangements, including costs. The World Bank is already moving toward such a review, and we would advise that the Fund, as co-host to the Annual Meetings, consider a similar exercise in cooperation with the Bank.

We would like to see some specific ideas investigated in any review. Mr. Wire and Mr. Peretz have already posed some worthwhile suggestions for reducing transportation and entertainment expenses, which represent a significant proportion of total costs. Other ideas we would support include reassessing the practice of holding Annual Meetings abroad, looking at the possibility of holding meetings every two years rather than annually, and looking at the frequency of Interim and Development Committee meetings. The departure of members of many delegations following the Interim Committee meeting or the opening session of the Annual Meetings might also indicate the need to reconsider the length of the meetings.

The Secretary's note confirms that many of our concerns are shared by others. For those who sat through plenary sessions with more chairs than people for company, the contrast between the number of delegates eligible to attend the plenary and those actually present was remarkable. Rather than reprimanding delegates for their absence, we take this as a loud signal that the plenary is not the delegates' primary focus. Our observations have been that the more important business of the Annual Meetings has become the bilateral meetings held with staff, other delegates, and visitors from financial institutions.

A number of members of this constituency appreciate the opportunity to present their views at the plenary. However, we would support the idea of shifting the plenary from a large meeting hall following the opening session, not only in Madrid but also here in Washington. Finding a suitable venue in Washington needs to be a priority, and we would suggest that a feasibility study be carried out on the possibility of more intensive use of the meeting hall here at the Fund, as well as other options suggested by Mr. Peretz. Basing activities at headquarters would also have the advantage of avoiding the shifting of offices, lock, stock, and barrel from the Fund to the Sheraton Washington Hotel. As a result, pressure would be reduced on secretarial staff who are required to be at headquarters for the Interim and Development Committees meetings. It would also lessen the security problems that this constituency faced and would put an end to the "to-ing and fro-ing" between the two locations. An early and timely decision on this matter would prevent committing ourselves to further long-term contracts with the Sheraton Washington Hotel.

Our difficulty with use of the Sheraton Washington stems partly from poor attendance at plenary sessions but also the dissatisfaction of a number of delegates from our constituency with the quality of service at the Sheraton Washington. The particular problems we faced included rooms not being ready on time, converted bedrooms not working well as offices, difficult access owing to heavy use of elevators, and rooms with leaking plumbing and dirty furniture, in addition to problems with security. Moreover, catering service fell well short of the prices being demanded.

As Bretton Woods approaches its fiftieth anniversary, an in-depth review of the aims of and arrangements for Annual Meetings would be timely.

Mr. Smee made the following statement:

The Annual Meetings are important for this institution, and we want them to be as useful as possible. But the Annual Meetings themselves have become a familiar ritual that are exclusive rather than inclusive of the responsibilities and role of the Fund. By that, I mean they have become a hollow exercise in a large, empty hall.

The opening ceremonies are fine. They could even be moved to some large, impressive hall in Washington rather than the Sheraton Washington. The Governors' speeches could then be given in the main meeting room here at the Fund, with no pretense that Governors and delegations will be there or want to be there at any one time, if ever. In this regard, perhaps the Secretary could elaborate on why all Governors, special invitees, staff, press and guests must be taken account of in the seating arrangements.

Madrid should be the last Annual Meeting held outside Washington, not only because a large amount of money would be saved, but also because meetings outside Washington appear to be much less conducive to the conduct of business.

I note from the Secretary's memorandum that the World Bank is reviewing various aspects of the meetings, including a review of costs. Could the Secretary inform us of the Fund's links to this review? After all, these are joint meetings, and we do not want to be handed a fait accompli at some future date. Should we undertake a more formal review ourselves?

On the Interim Committee, I return to the idea of moving at least the afternoon session into the Executive Board Room. What is worse: our ignoring that the Interim Committee has become a gathering of high-powered people talking past each other or our pretending that all the hundreds of hangers-on and observers behind the 24 members are really adding anything to or getting anything out of the ritual? How can a meeting be interactive if there are 200-300 people in the room? I predict that if the meetings continue as they are, we will be down to one Interim Committee meeting a year within two to three years, and none by the end of the decade.

The lunch is not meant to be a communiqué drafting session. At the last meeting, the drafting on the ESAF was done with words that were chosen to sound innocuous to unsuspecting Ministers but were ripe with meaning for the cognoscenti of Fundspeak. Then, we were told afterwards, "no changes, your Minister has agreed."

Decisions, tough decisions, can be made over lunch, but no communiqué drafting. I have been instructed to say that I must inquire formally before the next lunch if communiqué drafting is to be done. If so, a Canadian official, rather than the Member, will attend. If that becomes widespread, I also predict that soon, the lunch will go the way of the dinner.

Mr. Autheman said that in reaction to Mr. Smee's last comments, he wished to record an objection: he would not wish to see any bureaucratic censorship of the conduct of the Interim Committee's meetings.

The Executive Directors agreed to continue their discussion in the afternoon.

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/93/153 (11/3/93) and EBM/93/154 (11/5/93).

4. DOMINICAN REPUBLIC - EXCHANGE SYSTEM

The approval for retention by the Dominican Republic of the exchange restrictions evidenced by external payments arrears, granted under Executive Board Decision No. 10411-(93/96), adopted July 9, 1993, is extended until completion of the next midterm review of the stand-by arrangement or February 28, 1994, whichever is earlier. (EBD/93/172, 10/29/93)

Decision No. 10507-(93/154), adopted
November 4, 1992

5. PANAMA - ARTICLE IV CONSULTATION - POSTPONEMENT

Notwithstanding the period of three months specified in Procedure II of the document entitled "Surveillance over Exchange Rate Policies" attached to Decision No. 5392-(77/63), adopted April 29, 1977, as amended, the Executive Board extends the period for completing the next Article IV consultation with Panama to December 20, 1993. (EBD/93/172, 10/29/93)

Decision No. 10508-(93/154), adopted
November 4, 1993

6. ACCESS TO FUND ARCHIVES

The Executive Board approves the proposal relating to the use of material in the Fund archives as set forth in EBD/93/173 (11/1/93).

Adopted November 4, 1993

7. APPROVAL OF MINUTES

The minutes of Executive Board Meetings 93/45, 93/46, 93/48, and 93/49 are approved.

8. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors as set forth in EBAM/93/190 (11/2/93) and EBAM/93/192 (11/3/93) and by an Advisor to Executive Director as set forth in EBAM/93/190 (11/2/93) is approved.

APPROVED: August 18, 1994

LEO VAN HOUTVEN
Secretary