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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 85/2

10:00 a.m., January 9, 1985

J. de Larosière, Chairman

Executive Directors	Alternate Executive Directors
A. Alfidja	
C. H. Dallara	
	H. G. Schneider
	X. Blandin
	M. B. Chatah, Temporary
	M. Sugita
	B. Goos
J. E. Ismael	
R. K. Joyce	
	H. A. Arias, Temporary
H. Lundstrom	
	A. S. Jayawardena
	A. Abdallah
F. L. Nebbia	B. Jensen
	J. E. Suraisry
	G. Ortiz
J. J. Polak	
A. R. G. Prowse	A. V. Romuâldez
G. Salehkhou	
	T. A. Clark
	N. Coumbis
Zhang Z.	Wang E.

L. Van Houtven, Secretary
R. S. Franklin, Assistant

Also Present

D. A. Dunn, IBRD. African Department: A. D. Ouattara, Director; G. E. Gondwe, Deputy Director; N. Abu-zobaa, N. Calika, F. d'A. Collings, A. Jbili, J. M. Jiménez, M. Sidibé, J. D. Simpson. Exchange and Trade Relations Department: W. A. Beveridge, Deputy Director; M. Nowak. External Relations Department: A. M. Abushadi. Fiscal Affairs Department: W. R. Mahler, Jr. Legal Department: Ph. Lachman, J. M. Ogoola. Personal Assistant to the Managing Director: S. P. Collins. Advisors to Executive Directors: L. K. Doe, D. Hammann, S. M. Hassan, A. Vasudevan. Assistants to Executive Directors: H. Alaoui-Abdallaoui, J. J. Dreizzen, G. Ercel, C. Flamant, G. D. Hodgson, Z. b. Ismail, J. M. Jones, A. K. Juusela, H. Kobayashi, M. Lundsager, R. Msadek, K. Murakami, E. Olsen, M. Rasyid, J. Reddy, D. J. Robinson, J. E. Rodríguez, C. A. Salinas, Shao Z., A. H. van Ee.

1. REPORT BY MANAGING DIRECTOR

The Chairman, reporting briefly on his recent visit to Paris, noted that he had delivered a speech on debt problems to a diverse group of French trade unionists, academicians, businessmen, bankers, and others; afterward, he had held discussions with French Treasury officials on Paris Club matters, reviewing a number of individual country situations.

2. EXECUTIVE DIRECTOR

The Chairman welcomed to the Executive Board Mr. Hans Lundstrom as Executive Director for the Nordic countries.

3. KENYA - REQUEST FOR STAND-BY ARRANGEMENT

The Executive Directors considered a request from Kenya for a stand-by arrangement in an amount equivalent to SDR 85.2 million (EBS/84/261, 12/12/84; and Sup. 1, 1/8/85).

Mr. David A. Dunn, IBRD, was present for the discussion.

The Chairman drew the attention of Executive Directors to the revised draft decision on Kenya's request (EBS/84/261, Sup. 1, 1/8/85) under which the stand-by arrangement would be approved in principle for a maximum of 30 days, with the arrangement to become effective on a finding by the Fund that satisfactory arrangements had been made to finance Kenya's balance of payments deficit expected in 1985.

Mr. Prowse requested clarification of the meaning of the two distinct dates mentioned in paragraph 3 of the decision. It was stated that the stand-by arrangement would become effective not later than 30 days from the date of the decision and on the date on which the Fund found that satisfactory arrangements had been made for the financing of the expected deficit in 1985. Was the intention that the stand-by arrangement would be suspended if the financing arrangements had not been completed within 30 days of the adoption of the decision?

The Deputy Director of the Exchange and Trade Relations Department recalled from an earlier general discussion on the approval in principle of extended and stand-by arrangements (EBM/84/155, 10/24/84) that Directors had endorsed the idea of setting a 30-day outer limit in normal circumstances; that limit had been applied in the Kenyan case because it covered both the period during which it was expected that negotiations on the Eurocurrency loan would be completed and, more important, it encompassed the date set for the donors' conference that it was hoped would make available additional amounts of concessional assistance. If, during the 30-day period, the staff was not in a position to state that satisfactory financing arrangements had been made, the stand-by arrangement would not be effective, and a new decision would have to be put to the Executive

Board. However, he was not in a position to say at present in what form the request might be put to the Board in those circumstances; it might be necessary, for example, to review the phasing of purchases and, perhaps, even the basic premise of the program. Of course, if adequate financing were to become available within the 30-day period, that information would be brought to the attention of the Executive Board together with a proposal, presented on a lapse of time basis, that the program be made effective.

The Chairman noted that the Kenyan case was consistent with the guidelines for approval in principle of stand-by and extended arrangements: the approach had nothing to do with the design of the program or the actions to be taken by the authorities but was prompted only by uncertainty with respect to the financeability of the program, particularly the amount of the financing that might be yielded by the early February donors' conference. For staff and management to have sought full approval for the Kenyan program at the current meeting would have been both imprudent--because the Board would not have been assured of the program's financing--and tactically unsound, since approval might have weakened the position of the Kenyan authorities at the donors' conference.

It must be clearly understood, particularly by the donor countries, that Kenya needed the sort of financial assistance that was consistent with its debt profile and its general debt position, the Chairman remarked. In the circumstances, the good prospects for a Eurocurrency loan to Kenya should not lead to complacency among those who felt that longer-term concessional assistance was required. Put more bluntly, even if the Eurocurrency loan negotiations were completed, he would still want to wait for the outcome of the donors' conference before making a judgment about whether the program was financeable.

Mr. Abdallah made the following statement:

> The present request of my authorities for a stand-by arrangement comes only a few months after the successful implementation of the program agreed with the Fund in March 1983 and supported by an 18-month stand-by arrangement. The request articulates the strong desire of the Kenyan Government to continue working closely with the Fund in seeking solutions to the country's economic problems. My authorities believe that the adjustment process must be continued in order to maintain a viable balance of payments position and establish the basis for sustained economic growth. The importance of the latter cannot be overemphasized, given the high rate of population growth in Kenya.
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> Except for 1984, when the economy had been severely affected by the drought, performance of the economy in the past few years has been most encouraging. On the domestic front, the budget deficit declined from 9.5 percent of GDP in 1981 to 4.6 percent in 1984, while inflation, as measured by the consumer price

index declined from more than 20 percent to 10 percent during the same period. Monetary policy was supportive of the authorities' efforts to contain aggregate demand and promote a more efficient allocation of resources. Interest rates were increased, and the Central Bank strengthened its surveillance over the financial system. In the real sector, remunerative prices have helped to increase agricultural production, allowing for increased exports and the buildup of a strategic grain reserve in 1982 and 1983. The latter has been a crucial factor in ameliorating the impact of the drought in 1984, which has been described as one of the worst in the country's history.

Substantial progress has also been made in reducing imbalances in the external sector of the economy. In addition to achieving a marked reduction in the current account deficit to a level which is considered sustainable over the medium term, the overall balance of payments recorded surpluses in both 1983 and 1984, leading to a rise in reserves from the equivalent of 1.4 months of imports in 1981 to 3.2 months of imports by the end of 1984. These developments reflected the convergence of several factors, including a pickup in international demand and, in particular, the implementation of a flexible exchange rate policy aimed at ensuring remunerative returns to all producers. The increase in supply of foreign exchange has helped to facilitate the liberalization of Kenya's import regime and the external payments system.

The recent drought has made the adjustment process more difficult for Kenya, with the budget and the balance of payments coming under pressure largely because of the need to provide relief to affected areas throughout the country through higher importation of cereals. However, the 1985 program has been designed to cope with this temporary emergency, while fostering the longer-term goals of maintaining fiscal equilibrium and a viable external payments position.

The implementation of prudent fiscal policies is central to the current program, the objective being to keep the budget deficit within manageable limits. Although allowance has been made for drought relief, which has contributed to a small rise in current expenditure, the budget on the whole indicates restraint in most expenditure categories. For instance, no general salary increase was granted to the civil service in 1983/84 fiscal year, and none is envisaged for 1984/85, while efforts are being made to contain the growth in the size of the civil service. Meanwhile, new tax measures have been introduced to help offset the projected increase in expenditure. In all, the budget deficit is expected to rise from the equivalent of 4.6 percent of GDP in 1983/84 to 5.1 percent of GDP in 1984/85. However, if the efforts being made by the authorities to attract additional foreign grants and loans materialize as expected, the deficit will be smaller than projected, along with the need for domestic financing. Thus, even though the program projects the expansion of total domestic credit equivalent to 16.2 percent of the initial stock of money, actual growth is expected to be lower. If expenditure to counter the effect of the drought is removed, the budget deficit would have declined from 4.6 percent of GDP in 1983/84 to 4.1 percent of GDP in 1984/85, indicating that fiscal policy continues to be restrictive and that the underlying trend toward a sustainable budget deficit is being maintained.

The efforts that are under way to improve the performance of public corporations remain crucial to the stability of the Government's financial position. The activities of these corporations are now being monitored more closely by the Investment Division of the Ministry of Finance. The basic objective is to ensure fuller accountability, cost effectiveness, and general viability of the public entities. Expenditure plans of major public enterprises should be integrated into the forward budget of the Central Government in the next fiscal year, a move which should improve the planning process.

Monetary policy will remain restrictive in the current year, reflecting the Government's concern about inflation as well as the need to reduce pressure on the balance of payments. However, efforts are being made to channel credit to productive sectors of the economy. The Government is committed to maintaining interest rates at positive levels and, currently, real interest rates range from 2 percent to 5 percent.

Kenya's balance of payments is expected to come under pressure in 1985, reflecting the rise in imports necessitated by the drought and the softening of the international market for tea and coffee, whose prices are expected to fall by 16 percent and 9 percent, respectively. Exports of refined oil are also expected to decline, partly as a result of increased domestic demand arising from reduced hydroelectric capacity and partly from reduced economic activity in the neighboring countries. Because of the higher food imports and some reduction in exports, the current account deficit of the balance of payments is projected at 5.6 percent of GDP in 1985. However, the outlook for the medium term is encouraging, with the deficit projected to decline to around 3.5 percent of GDP in 1989. The authorities intend to finance the deficits by long-term private capital inflows to ensure that Kenya's debt service is kept within manageable proportions.

For some years now the authorities have been managing the exchange rate in a flexible manner. This policy will continue, together with import liberalization which is stipulated in the program.

> It is clear that the Kenyan authorities are committed to the adjustment process and are doing everything necessary to ensure the attainment of sustained growth and a viable balance of payments position. The economic policies of the past two years have left the economy much stronger and better able to cope with the reversal in economic activity precipitated by the drought. The noticeable progress which has been made has strengthened the resolve of the authorities to persevere with tough stabilization policies whose impact has touched every segment of society. Kenya, through its policy of HARAMBEE (meaning pulling together), has demonstrated that it can cope with natural misfortunes and rebound from them. It has also demonstrated that it can put international assistance to constructive use and run its affairs in a cooperative and open manner. It continues to require further assistance from both bilateral sources and international agencies such as the Fund and the World Bank. The authorities strongly hope that the needed assistance will be forthcoming in the required magnitude and at the right time for the foreseeable future.

Mr. Ismael commended the Kenyan authorities for having successfully implemented the 18-month program that had expired in September 1984. All the performance criteria under that program had been met and the overall objectives had been achieved; indeed, performance in certain areas--particularly the balance of payments--had far exceeded expectations. The achievements of the authorities reflected their deep commitment to the program and their willingness to take additional measures as warranted.

His chair fully supported the proposed request for a new stand-by arrangement, which was justified on the basis of Kenya's balance of payments need, its record of adjustment under the previous program, and the adjustments envisaged in the proposed program, Mr. Ismael said. Provision had been made for an increase in the size of the budget deficit from 4.6 percent of GDP in 1984 to 5.1 percent of GDP in 1985. That increase had been necessitated by the drought, which was expected to have a negative impact on government revenues and would require increased outlays for relief and rehabilitation. In setting program targets for the future, the Fund should continue to take due account of emergency situations facing member countries and would grant the authorities additional time to bring about needed adjustments.

Another element of fiscal performance was related to the balance between the operating and capital components of the budget, Mr. Ismael continued. In the past, the burden of fiscal adjustment had fallen too heavily on the capital budget, such that the share of capital expenditures in the budget had declined from more than 10 percent of GDP in 1980/81 to 7.8 percent of GDP in 1983/84. Recognizing that it would be difficult sharply to increase the capital program in 1985, he felt nonetheless that it would be important in subsequent years for the authorities to be more aggressive in implementing the new Five-Year Development Plan, which had received a favorable review from the World Bank. In implementing the capital program, the authorities might be well advised to avoid projects that had a high import content, unless those happened to be high priority projects that were supported in large part by concessional financing from foreign sources.

A third aspect of the public finances deserving of comment was related to the operations of the state enterprises and their implications for the government budget, Mr. Ismael noted. The number and size of the parastatal institutions, and their potential for destabilizing government finances, could not be underestimated. The staff had explained the difficulties encountered in controlling the parastatals, and it was clear that the management of those enterprises seemed to be seriously hampered by a shortage of technical and managerial skills. Perhaps technical assistance from the Fund would be helpful.

Remarking on the financing of the fiscal deficit, Mr. Ismael observed that a very high proportion--nearly 80 percent--of the total budget deficit in Kenya was financed by commercial bank and foreign borrowing. While such financing might be warranted to some extent by the emergency situation in the country, he hoped that greater attention would be paid in future to the mobilization of domestic financial resources.

There had been no cost of living adjustment in the public sector since 1981, while the private sector had been allowed to increase wages up to 75 percent of the rise in the cost of living, Mr. Ismael remarked. He would appreciate an indication from the staff of the extent to which the 75 percent indexation was actually practiced in the private sector. Also, what had happened in recent years to the wage differential and to labor mobility as between the private and public sectors?

The authorities should move quickly to meet the financing gap of SDR 93 million projected for 1985 and on which the implementation of the proposed program heavily depended, Mr. Ismail said. Given the substantial deterioration in the current account and in the overall balance expected in 1985 because of the emergency situation in Kenya, the staff might have been too optimistic about Kenya's medium-term balance of payments prospects; he himself would have been more cautious, for a number of reasons. In making projections for 1986-89, the staff had assumed an import volume growth of 2 percent per year, which was rather low by comparison with historical growth rates for imports and in light of the import liberalization initiatives introduced by the authorities. Also, if the balance of payments was not strengthened by more vigorous implementation of an export development program, the medium-term outlook would not be very promising. In view of those uncertainties, the authorities should perhaps adopt a contingency plan to deal with their external problems in case weather conditions failed to return to normal in the year ahead and import growth exceeded expectations.

Finally, Mr. Ismael noted from Table 11 of the staff paper that the real effective exchange rate had appreciated in the first ten months of 1984. Table 2 showed an estimate of a 5 percent depreciation in the rate for 1984 as a whole. What was the explanation of that rather large discrepancy? In any event, there seemed to be a case for reviewing the appropriateness of the exchange rate on the basis of the actual figures for the first ten months of 1984; the staff should be looking into that matter in due course.

Mr. Joyce stated that he too had been impressed by the accomplishments of the Kenyan authorities under the previous program. It was clear that, if not for the severe drought conditions experienced throughout East Africa, Kenya might be well on the way toward solid economic growth in all areas of its economy and the achievement of a sustainable balance of payments position. The performance criteria under the previous program had been met by comfortable margins, and signs of strong recovery had begun to appear in the real economy by late 1983, as both the agricultural and industrial sectors had responded to stronger macroeconomic policies, changes in relative prices, and the liberalization of the trading system. Unfortunately, the severe drought in Kenya during 1984 had greatly offset those positive developments, despite additional adjustment actions taken by the authorities. In many respects, the proposed stand-by arrangement--which deserved in his view the full support of the Board--was representative of strong crisis management aimed at meeting the immediate needs of the Kenyan people while still preventing the achievements of the previous stand-by arrangement from slipping away. Nonetheless, the current emphasis should be on the immediate needs of the people.

The decision to increase consumer prices for agricultural goods in order to strengthen the financial position of the National Cereals and Produce Board was a courageous step, Mr. Joyce noted. While the medium-term strategy for adjustment set ambitious, but not unrealistic, goals for restoring growth, reducing inflation, and effecting further cuts in the size of the fiscal and current account deficits, the margin for maneuver was limited; the authorities would need to take even more stringent measures if the drought conditions were to persist in 1985. Also, as was the case elsewhere in Africa, population growth in Kenya must be brought under better control if future economic gains were to be translated into improvements in per capita living standards.

An increase in the projected budgetary deficit was warranted in the circumstances of Kenya, Mr. Joyce said. Moreover in 1984/85, there would be a reordering of expenditure priorities, and efforts would be made by the authorities to further strengthen the revenue base. Measures had been taken to shift the tax burden from import duties to other forms of taxation, such as sales taxes. The increased sales tax on luxury items and tax increases on air travel and cigarettes seemed fully justified in current circumstances. As for expenditures, the increases related to the drought were understandable, and development outlays should not be reduced, since the new development plan was already constrained by a shortage of local funding. Efforts to contain wage expenditure and to draw up a register of civil servants should help to eliminate waste in government; however, since drought-related expenditures accounted for only one half of the increase in current expenditures, greater efforts to contain other expenditures should be made. The other side of the increase in current expenditures was related in part to weaknesses in the management of the public enterprises, an area not being appropriately dealt with under the proposed stand-by arrangement. So long as the authorities failed to gain firm control over the parastatals, of which there were many in Kenya, the fiscal position would remain at risk. Perhaps additional technical assistance in that area from either the Fund or the World Bank would be helpful.

Efforts had been made to limit the recourse to bank financing of the budget deficit, especially since such a limitation could create more room within the credit ceilings for funding of private sector activities, Mr. Joyce commented. The projections for credit expansion and net bank financing to the Government, however, should be regarded as ceilings. He joined the staff in urging the authorities to seek out concessional assistance for financing the fiscal deficit and to continue their prudent monetary policy stance.

The authorities intended to continue a flexible exchange rate policy and to press toward greater import liberalization, Mr. Joyce remarked; similar approaches in the past had served Kenya well. He had some concerns about the relationship between the proposed program and the prospects for assistance from the World Bank. In Attachment V of EBS/84/261, it was stated that the World Bank was not currently contemplating the negotiation of a third structural adjustment loan and that "the Bank remains dissatisfied at the degree to which Kenya met the commitments included under the program." It was further stated that "implementation was also affected by...the preoccupation of the authorities with short-term stabilization efforts." He wanted to be reassured that a situation had not arisen in Kenya whereby, because the country was carrying out the recommendations of the Fund with respect to stabilization problems, it was in turn running into difficulties in obtaining World Bank financing.

For the medium term, there seemed to be grounds for some optimism, Mr. Joyce commented. The outlook for export prices was uncertain, major problems existed with respect to the parastatals, and the drought was not yet over, but the Kenyan authorities had demonstrated a commitment to do what was necessary to pursue their declared objectives and an ability to implement agreed programs. Moreover, Kenya's medium-term debt service projections were reasonably favorable by comparison with those of most other African countries, and the ceilings on new debt within the program were appropriate. A proper comprehensive marketing development strategy would help to strengthen the balance of payments, and the authorities could make some progress toward that end in the near future. Perhaps that matter could be looked at on the occasion of the next review.

In giving his strong support to the proposed stand-by arrangement, Mr. Joyce agreed that the program should be approved only in principle until appropriate financing arrangements had been made. In that respect, any commercial financing that might be arranged could be replaced to the extent possible by concessional resources from donors, since that was the only way to ensure that the future debt servicing outlook for Kenya would improve.

Mr. Dallara indicated that Kenya's balance of payments need and its performance under the previous stand-by arrangement led him to support the request for a new arrangement. Fiscal policies in Kenya had been comprehensive and well managed under the past two stand-by arrangements. The budget deficit--including grants--had fallen from 9.5 percent of GDP in 1981 to 4.6 percent of GDP in 1984. The deficit was expected to increase somewhat in 1985 due to drought-related expenditures; however, he presumed that the authorities would act as they had in the past and take the corrective measures necessary to prevent too great an adverse impact by the drought on both revenues and expenditures. Additional drought-related expenditures aside, the present budget continued to be conservative, with other current expenditures decreasing and plans for no general wage increase in the civil service for the third consecutive year. Moreover, the authorities had economized on development expenditures by postponing nonpriority projects. At the same time, revenue measures appeared to be aimed at containing demand for various consumer goods while providing revenue for the Central Government.

Monetary policies were broadly appropriate and supportive of fiscal policy, Mr. Dallara considered. He welcomed the commitment of the Government to limit its recourse to nonbank financing, a move that would provide greater room for credit expansion to the private sector. In that regard, he would appreciate a breakdown of credit expansion to the private sector from the banking system; in the year ended September 1984, credit to the public enterprises had grown 63 percent, while credit to the private sector had increased by only 8 percent. Given inflation of about 10 percent, the implication was for no real growth in the private sector. Real interest rates seemed sufficiently positive, given the sharp decline in inflation in the recent past; however, the authorities should be prepared to make further adjustments in interest rates if that should prove necessary to preserve incentives for savings.

Price adjustments in the productive sector, including the exchange rate changes that had taken place, had led to increases in agricultural output until 1984, Mr. Dallara noted. Producer and consumer prices had been increased again in the fall of 1984, apparently preserving the profitability of food production. He welcomed the flexibility of the authorities in that area and encouraged further price adjustments, which were necessary to the achievement of the authorities' internal and external objectives.

The authorities had maintained a prudent debt profile, Mr. Dallara said. Indeed, Kenya was one of the few developing countries to eschew debt rescheduling. Even assuming some increase in debt on commercial terms, the staff was projecting in Table 10 that the debt service burden would fall from 29 percent of exports of goods and services in 1985 to around 20 percent--a manageable relationship--by the end of the decade.

He had some serious reservations about the pace of adjustment under the program in the areas of the exchange rate, trade liberalization, and the public sector enterprises, Mr. Dallara continued. The Fund had been making recommendations for change on those fronts for some time, and it was discouraging to note that little improvement had been registered during a period of continuing Fund support. He had been particularly discouraged to read on page 22 of EBS/84/261 that the plan to "better control the public enterprises" had suffered some important delays. Because of their size and number, the parastatals significantly affected economic activity in Kenya, and the evidence suggested that the effects were not helpful always to the country's overall economic prospects. The new delays were mainly legislative impediments to a speedy rationalization of the parastatals, including possible privatization of the public sector. While some changes had recently been made in the area of centralized control over marketing of agricultural inputs and output, it was difficult to assess the effect of those changes. In the circumstances, it was imperative that the pace of divestiture and rationalization of the public sector enterprises be quickened and support be generated in the Parliament for speeding up the legislative process. While he understood that some foreign investors might have concerns about the change in the status of certain of the public sector enterprises, those investors would reduce government control.

Also the pace of import liberalization in Kenya did not appear to have been adequate in the circumstances, Mr. Dallara commented. Appendix I provided some useful information, although it was difficult to see what the numbers in the text and the table implied for the protection of domestic industry. He would be interested in hearing staff views regarding the effects of the reported increased freedom to import on the efficiency of the Kenyan economy and on direct competition with imports. He would also be interested in knowing whether stepping up the pace of import liberalization was likely to generate additional incentives for rationalization of the public enterprise sector. While some progress had been made toward import liberalization, the matter seemed to be one of continuing concern, despite the fact that it had been given particular emphasis in the previous Fund stand-by arrangement and in an earlier structural adjustment loan program with the World Bank.

Also of concern was the matter of exchange rate policy in Kenya, Mr. Dallara commented. Although the real effective exchange rate had fallen since 1978, the net change since September 1983 had been an appreciation of the shilling, and he had serious doubts that the trend had been appropriate. Moreover, the relationship between import liberalization and the exchange rate changes should be reviewed, especially since the maintenance of trade controls seemed to support the current exchange rate. The current rate was not far from what it had been in the mid-1970s, when trade controls had been even more extensive. More extensive exchange rate adjustments would have permitted a faster pace of trade liberalization, which would have been helpful to both domestic activity and to the medium-term balance of payments prospects. Greater emphasis should have been placed on exchange rate adjustment at the beginning of the proposed program in order to send the price signals to stimulate production and diversification in nontraditional exports, thus providing the framework for more rapid import liberalization. As it stood at present, exchange rate policy would apparently not be scrutinized until the midterm review in late spring, which might be too late to have much impact on the current program.

A more general concern was related to the matter of Fund/Bank collaboration in the Kenyan case, which in his view had been somewhat less than ideal, Mr. Dallara said. He was not blaming either the Fund or the Bank staff in their relations with one another or in their relations with the Kenyans; however, the Bank's lack of participation in the current effort to assist Kenya with its drought-related difficulties was a clear indication that the authorities had not been prepared to make the policy adjustments that the World Bank would find acceptable. In ordinary circumstances, that "failure" on the part of the authorities would not give rise to particular concern in the Fund, especially since the Kenyans had been remarkably successful in following the policy advice of the Fund over the years. However, Kenya would not be able to reach a sustainable balance of payments position--where it would no longer need to rely on Fund financing--without more rapid structural adjustment; therefore, he was worried about the failure of the Kenyan authorities fully to meet the World Bank's expectations. The amount of information that had been provided to the Executive Board regarding World Bank relations with Kenya--including any differences of opinion that might exist between the two institutions regarding either the analysis of the problems facing Kenya or the most appropriate policy responses to them--had not been entirely sufficient. Indeed, Attachment V of EBS/84/261 left much to be desired in the provision of straightforward information about the real nature of the differences of view between the World Bank and the Kenyan authorities and about how relevant those differences were to the Fund.

Mr. Clark, noting the successful implementation of the previous stand-by arrangement, considered that a priority matter for the next phase of adjustment should be to tackle the structural problems from which the Kenyan economy continued to suffer. In the past six months, Kenya's circumstances had changed sharply for the worse, mainly because of the severe drought. Structural reform, of course, remained a pressing concern; in addition, however, there was at present also an urgent need to contain the pressures on government spending, the balance of payments, and the rate of inflation, which the drought and the associated reduction in economic activity had brought about. In general, therefore, he could endorse the staff's assessment that policy in present circumstances must be aimed at dealing with the consequences of the drought while reinforcing and extending the progress already made in adjusting the fundamentals of the economy. The proposed stand-by arrangement seemed an appropriate step toward that end, and he could support the proposed decision, although he had a number of comments on economic policy.

On the fiscal side, while several components of government expenditure had naturally been increased by the drought, it was possible that, even without the drought, expenditure targets might have come under pressure, Mr. Clark continued. For example, civil service pay had not increased since 1981, which was a welcome restraint; but one had to ask how far it was reasonable to expect such restraint to continue, given the rise in prices and the decline in living standards that had taken place over the past three years. Also, for financing the deficit--currently projected at 5.1 percent of GDP--there seemed to be an implicit reliance on a much higher proportion of foreign grants than in the past, if the projected increase was in fact materializing.

He was not clear why the performance criteria for credit expansion appeared loose, Mr. Clark said. Credit growth was projected at 18 percent in 1985, about twice the rate of inflation. There had been persistent undershooting of such targets, and he recognized that a substantial external outflow was expected; however, he wondered whether some capital flows, and indeed some components of the current account, were not sensitive to domestic credit conditions and whether, therefore, the targets might not have been more tightly drawn. Also somewhat unclear was the list of precisely which institutions were covered by the domestic credit aggregate. Some emphasis had been given in the staff paper to the role of nonbank financial intermediaries, and he would be grateful for an indication of the extent to which their credit was included. On the institutional aspects of financial policy, he understood that the Fund staff had recently completed a report on the financial system in Kenya and had come to a number of conclusions--for example, the effect of the present interest rate structure. How were the Kenyan authorities proposing to respond to that report?

On external policy, four points were deserving of note, Mr. Clark considered. First, much of the improvement in the balance of payments seemed to have reflected strong growth in agricultural exports, especially of tea. Even without the difficulties caused by the drought, the favorable trend in export revenues could have been expected to continue over the medium term, and there was a risk of large financing gaps. Projections for future growth in imports, other than emergency food imports, were rather modest, despite a substantial liberalization of the import licensing regime and relatively rapid domestic credit growth. Third, the recent exceptional increase in grain imports and other effects of the drought on trade seemed to strengthen the case for a compensatory financing facility drawing. How did matters stand currently with respect to a possible request and how large a drawing might be in prospect? Fourth, the prospective financing gap for 1985 had led the staff to put before the

Board a conditional decision on Kenya's request for a stand-by arrangement that required the necessary financing to be assembled within 30 days. There seemed to be two main sources in prospect for that financing: further support from donors and commercial borrowing. In respect of the former, he had noted plans for a donors' meeting in early February; as for the latter, he joined others in questioning whether commercial borrowing was appropriate in Kenya's current circumstances. Still, he would be interested in hearing further details from Mr. Abdallah about the status of discussions between the Kenyan authorities and the commercial banks.

Improving the supply capacity of the economy was crucial to Kenya's medium- and long-term prospects, Mr. Clark reiterated. There had been little or no progress toward a third structural adjustment loan from the World Bank. The Bank had expressed reservations on the way in which the previous two structural adjustment loans had been implemented, and there was a rather different tone in the papers on Kenya by the Bank and by the Fund.

Finally, like Mr. Dallara, he would be interested in a status report on Kenya's relations with the World Bank, Mr. Clark commented. Longer-term issues might not be given high priority; however, without progress toward structural adjustment in the parastatal enterprises and more rapid trade liberalization, the return to a path of medium-term growth would be difficult. In sum, the Kenyan authorities had adopted appropriate and effective policies that, under the previous stand-by arrangement, had succeeded in bringing about major improvements in the economy. The current need was to preserve those successes and to cope with the temporary disruptions caused by the drought while continuing to strengthen the underlying supply capacity of the economy.

Mr. Goos said he regretted that the progress achieved in 1984 toward a sustainable balance of payments position and a general improvement in economic conditions had been interrupted by a severe drought. As it was, several key economic variables were expected to deteriorate in 1985 to levels that were close to those shown for 1982, a year of severe constraints in foreign exchange availability. While the program needed to make allowances for the financial requirements resulting from the drought, a strong adjustment effort was nonetheless envisaged. With continued adjustment, prospects were good for maintaining the underlying economic improvements already registered and for returning to a viable external payments position in the medium term. Such an outcome would be particularly desirable in view of Kenya's indebtedness to the Fund resulting from successive Fund arrangements in recent years.

Kenya's record of adjustment under the previous arrangement and the measures introduced under the current program were impressive, Mr. Goos continued. In particular, adjusting producer prices to realistic levels together with a flexible exchange rate policy and import liberalization measures, explained the economic improvements registered since 1982. Nonetheless, the authorities would be reviewing the import liberalization measures because they were concerned that the present practice might have led to overstocking. It would certainly be unfortunate if the process of import liberalization were to be reversed on the basis of that review; a more efficient approach to the overstocking problem might lie in an increase in interest rates, a matter to which the staff itself had attached importance.

The degree of restraint in the area of wage policy in the past several years had been commendable, Mr. Goos considered. However, he joined others in wondering whether further restraint might not impair the efficiency of the public sector; indeed, the restraint thus far already might have contributed to difficulties in hiring qualified personnel.

Despite the problems he had mentioned, it was apparent that the overall policy stance was having a beneficial effect on a number of areas of the economy, including agricultural production and exports, Mr. Goos remarked. The policies pursued had indeed placed the country in a relatively comfortable position to weather the impact of the recent drought, and he heartily endorsed the authorities' intention to continue with those policies under the proposed arrangement. Of course, there remained areas requiring additional attention--in particular, the urgent need to improve financial control of the public enterprises. Despite a long period of successive Fund arrangements with Kenya and continuous World Bank involvement in that country, the authorities had begun only recently to monitor the activities of the public enterprises more closely. Given the major role that those enterprises played in the economy and the considerable drain they represented on the budget, such monitoring was more than timely. He wondered to what extent the World Bank in its favorable assessment of the new Five-Year Development Plan had taken into account the unsatisfactory situation of the public enterprises. Also, Attachment V to EBS/84/261 stated that "the Bank remains dissatisfied at the degree to which Kenya met the commitments included in the program"; that statement had implications for Fund/Bank cooperation in Kenya and for structural adjustment.

An "in principle" approval of the proposed stand-by arrangement was appropriate in view of the remaining external financing gap, Mr. Goos continued. However, the arrangement should become effective only when the financing had been secured. While the envisaged Eurocurrency loan would not add much to Kenya's outstanding indebtedness, would the loan be consistent with the objective of improving the country's debt servicing capacity? In the circumstances, the authorities would be able to substitute other more appropriate financing for the Eurocurrency loan. Finally, to what extent would the envisaged compensatory financing facility drawing contribute to the closing of the financing gap expected in 1985?

Mr. Schneider noted that substantial progress had been made under the previous stand-by arrangement and that the program had been successfully implemented. Unfortunately, Kenya had been faced in 1984 with a major drought that had had a severe impact on normal economic activities. With the proposed stand-by arrangement, the authorities were appropriately aiming at remedial measures while seeking to sustain the internal and external stability achieved thus far. Implementing the measures designed to achieve those ends should leave Kenya in a position to cope with its present emergency situation and to move forward with the structural reform of the economy, particularly in the areas of the budget, development planning, and import liberalization. In the joint collaboration between the Fund and the World Bank, agreement had not yet been reached on a new structural adjustment program. The Bank was dissatisfied with the commitments made under the past two structural adjustment loans and with the disagreements between the Kenyan authorities and the World Bank staff during the negotiations for the third structural adjustment loan. Those developments were particularly disappointing since the economy already was suffering from a number of structural deficiencies, including rapid population growth. Population growth for several years had been higher than or equal to real GDP growth, and the authorities should take steps to correct the situation since it meant that per capita income was falling or stagnant.

Because of the present emergency, the authorities must exercise caution in pushing for further adjustments in the underlying budget deficit, Mr. Schneider continued. It was important to bring about a better allocation of resources in the public sector and to improve financial controls in the public enterprises. The authorities had made commendable progress on the external front, achieving balance of payments surpluses in 1983 and 1984 and moving toward a sustainable position in the medium term. A temporary deficit was expected in 1985 as a result of the drought; however, if the drought were to persist in 1985, the authorities would need to design a new economic strategy to cope with the situation, a strategy that must take into account Kenya's debt service ratio. In conclusion, he could support the revised proposed decision.

Mr. Prowse stated that he too could support the proposed program and revised draft decision. The financing gap should be met by donors rather than through commercial borrowing. While the debt service position of Kenya was not as difficult as that experienced by some other developing countries, it was not so comfortable that complacency was warranted. The projections for Kenya's financing were nearly equal to the net position vis-à-vis the Fund over the period; coincidence should not lead uninformed people to think that the donors' conference was being called upon to finance Kenya's repayments to the Fund.

The proposed program was unusual in that it provided for a substantial increase in the current account deficit, Mr. Prowse continued. In that respect, the program was a reflection of the flexibility of the staff and management of the Fund in responding to the particular circumstances of Kenya. It was apparent that the increase in the deficit was expected to be a short-term phenomenon based on additional spending to meet the immediate needs of those suffering from the drought; however, if the drought were to persist beyond 1985 or if other adverse circumstances were to develop, contingency plans would be needed. In any event, a current account deficit of the size currently projected should not be allowed to continue beyond the program period. He had not seen sufficient analysis in the staff paper to support the assessment that a current account deficit equivalent to about 3.5 percent of GDP through the medium term was viable; moreover, the staff was justifying its figure on the basis of its projections for capital inflows equivalent to 3.5 percent of GDP over the period. While the current account deficit might be financeable with inflows of that magnitude, it did not necessarily make the deficit appropriate, particularly given the size of the debt service ratio.

The viability of the current account could not be discussed in isolation from exchange rate policy in Kenya, Mr. Prowse remarked. The staff report showed clearly the relationship between the nominal exchange rate and the rate of price change, and the most recent experience with the exchange value of the shilling had not been altogether satisfactory. He would welcome assurances from the staff that exchange rate policy was sufficiently flexible.

He would have welcomed some further elaboration by the staff on how the amount of the proposed purchase under the stand-by arrangement had been arrived at, Mr. Prowse said. It appeared that the amount depended on an assumption that the Board would also approve a purchase of SDR 57 million under the compensatory financing facility. He was led to ask in the circumstances why the staff had not brought to the Board the proposal for a purchase under the compensatory financing facility together with the request for a stand-by arrangement; in many ways, it would have been preferable to look at the two requests as a package.

The key to the program was the promotion of efficient resource allocation, which, as Mr. Abdallah had suggested, required improvements in the public sector enterprises, Mr. Prowse commented. The Government currently seemed unable to exercise effective control over the numerous public enterprises in Kenya, and the accounting practices and record keeping of those enterprises was evidently deficient. The authorities were in the process of reviewing and reconstructing the accounts of the public enterprises; however, at the current rate of progress, it would take at least four or five years for officials to review the accounts of the wholly owned enterprises, which represented only a portion of the more than 100 companies in which the Government owned a majority or minority share. A full review would take about 15 years. Much more improvement was needed in the area of public enterprises in Kenya. In a recently circulated staff paper on Somalia, the staff had set out a schedule for the reform and possible divestiture of public enterprises in that country; it would be appropriate to consider setting up a similarly specific and coherent program for dealing with public enterprises in Kenya.

Mr. Chatah stated that he was in broad agreement with the staff appraisal of Kenya's financial program for 1985, and he could therefore support the proposed decision. The objective of minimizing economic and financial disturbances created by the recent drought while maintaining the medium-term sustainability of the underlying budgetary and balance of payments deficits seemed appropriate, given the country's circumstances.

The recent severe drought had overshadowed the adjustment achieved under the previous program and had necessitated a shift in policy to deal with the emerging crisis. Nevertheless, the reduction in the financial imbalances in 1983/84 had placed Kenya in a better position to generate the resources needed for drought relief; together with policies envisaged under the new program, that "cushion" should enable Kenya to overcome its present exceptional circumstances without jeopardizing the aim of medium-term viability of the country's financial position. He had found useful the quantitative estimates provided in the staff paper of the effects of the drought on the budget and the balance of payments. Those estimates had helped him to place the program targets on policies in the appropriate perspective by separating the transitory effects of the drought from the underlying movements in those key economic variables.

The target for the total fiscal deficit in 1985 seemed reasonable, Mr. Chatah continued. While higher than in 1984, the target implied some reduction in the underlying nondrought-related deficit, and a reduction in the total deficit was expected in 1986. The 1985 objective was based on revenue and expenditure measures that were already in place, including increases in excise and sales taxes, which should more than compensate for the reduction in import duties implemented under the policy of trade liberalization. The 10 percent general cutback in current expenditures, in addition to the postponement of certain development projects and the reduced loans and transfers to parastatals, should keep the ratio of government spending to GDP during the program period at about the same level recorded in 1984. Despite the policy of fiscal restraint, the increase in development spending in 1984/85 would outpace the growth in GDP for the second successive year. The containment of current expenditures also should be helped by the improved control over the wage bill through the requirement of registration of civil servants.

There had been no cost of living adjustments in the public sector since 1981, despite an increase of approximately 40 percent in consumer prices during the period, Mr. Chatah noted. Such wage restraint, which was continuing under the proposed program, was certainly consistent with the overall adjustment effort; however, he wondered whether the wage increases that were still being granted in the private sector would not represent a further enticement to skilled public sector personnel. Of course, it was possible that the public sector wage scale had originally been higher than that of the private sector or that nonwage benefits in the public sector compensated for any wage differential. He would welcome clarification of that matter from Mr. Abdallah or the staff.

Progress had not been satisfactory in the effort to control the public and semipublic enterprises, Mr. Chatah commented. Those enterprises played a major role in the Kenyan economy, and further delays in implementing effective measures to monitor their activities and control transfers between them and the Government could increase the drain on the budget in future. The flow of the resources seemed to have been all in one direction, as the Government had been forced to finance some of the losses of the public sector enterprises without receiving its share of profits where those had been made. Perhaps it was understandable that the parastatal reform effort would meet strong resistance; however, the authorities' concern that more decisive action might frighten off private investors was not totally convincing. In the longer run, distortions created by the lack of control over the flows between the Government and the enterprises might prove more costly to investment productivity and to the confidence of private investors, both domestic and foreign. One of the reasons given for the slow pace at which the review and reconstruction of financial accounts of enterprises seemed to be proceeding was the shortage of technical personnel. It would be helpful to know from the staff whether the authorities had considered technical assistance in that area from outside sources.

Monetary policy under the proposed program seemed to provide a reasonable balance between the need for financial restraint on the one hand and the need for drought relief and economic revitalization on the other, Mr. Chatah said. Clearly, the level of credit expansion that would be consistent with the program's objectives depended partly on the balance of payments support that the Government was able to obtain and which would reduce the utilization of bank credit by the Government. It was therefore important that the program provided for adjustments in the credit ceilings to offset any external support that was utilized through the budget and that was currently not accounted for in the ceilings.

On the external side, the balance on current account was expected to deteriorate in 1985, although an improvement was projected in the following year, Mr. Chatah noted. It was encouraging that the increase in the current account deficit in 1985 was expected to be less than the total impact of the drought on imports and exports. However, the sharp improvement in Kenya's terms of trade in 1984--which had largely been due to transitory factors--was expected to be partially reversed in 1985. It was therefore important that export competitiveness be maintained, particularly since the continuing policy of trade liberalization would inevitably lead to increases in imports. In that regard, he took note both of the authorities' intention to maintain the flexibility of the exchange rate and the staff's judgment that Kenya's exchange rate policy was appropriate in present circumstances.

The authorities were taking steps to fill the balance of payments financing gap projected for 1985 through increased donor support and some borrowing on commercial terms, Mr. Chatah observed. As was clear from the medium-term projections, however, the viability of the balance of payments depended on continued caution by the authorities with respect to their external commercial borrowing. The need for such borrowing clearly depended on the success in achieving a steady and substantial growth in exports along the lines assumed in the staff projections. In the circumstances, export promotion should be given increased emphasis.

The proposed program was reasonable in both its objectives and its policies, Mr. Chatah remarked. If it was fully implemented and if the assumptions regarding more normal climatic conditions were to materialize, Kenya should again be on course toward medium-term financial viability, which should allow the authorities to focus more sharply on structural reform and development policies. The involvement of the World Bank, which had been dissatisfied with Kenya's performance under the structural adjustment loans, had been substantial through project as well as structural adjustment loans. Adverse external circumstances had affected Kenya's performance; but intensified efforts toward comprehensive structural reform would be needed if the longer-term objective of sustained growth--both in total output and in per capita terms--was to be realized. The program was assuming a compensatory financing facility drawing equal to SDR 57 million between April and June 1985, and the financing gap of SDR 93 million was in addition to that amount. It would be useful if the staff could confirm his understanding; he would welcome an explanation for the apparent delay in the submission of the compensatory financing facility request.

Mr. Suraisry, agreeing with the thrust of the staff appraisal, observed that all performance criteria under the recently expired stand-by arrangement had been met, and the program objectives had been achieved. Progress had been made in reducing internal and external imbalances and in establishing a sound basis for sustained growth; indeed, the authorities' firm commitment to a balanced combination of demand and supply-side policies, and their ability to react quickly to changing circumstances, provided a good example to other countries. Unfortunately, Kenya's achievements and prospects were being jeopardized by the recent drought, which was continuing to have a negative impact on growth, the public finances, and the balance of payments. To their credit, the authorities had reacted prudently by giving first priority to drought relief efforts while working to maintain the underlying strength of the economy and to preserve the momentum of adjustment. At a time of real emergency, such objectives were commendable and deserved Fund support.

The proposed program seemed well designed to address Kenya's current situation, Mr. Suraisry said. The remaining financing gap should be covered as quickly as possible, and arrangements toward that end were being made. One of the possibilities being considered was a Eurocurrency loan. Given the indication of the staff that, at the end of 1983, nearly 70 percent of Kenya's external debt had been in the form of bilateral and multilateral loans on concessional terms at well below market rates, part of the financing gap could be met through a Eurocurrency loan, particularly since the debt service ratio in Kenya was projected to decline from 29 percent in 1985 to 18 percent in 1990. However, was commercial borrowing consistent with the effort toward a viable balance of payments position in the medium term? Taking on such a loan could have an adverse impact on the viability of the balance of payments if the drought were to persist for a number of years. In those circumstances, the authorities might need to take additional adjustment measures, and continue their commitment to fiscal restraint, despite the need to finance drought relief operations. Commendable steps already had been taken to increase revenue and simplify the structure of indirect taxation, but strict control over current expenditure was also essential in order to contain the budget deficit. Therefore, he supported the authorities' firm stand on public sector wages and their efforts to reduce the number of government employees, and he agreed that there was scope for more decisive action to streamline the public sector enterprises, which played a major role in the economy. Although some progress had been made, delays had been experienced in bringing the operations of the public sector enterprises under appropriate government control. It was important to close that gap in fiscal management, particularly at a time when the Government's scarce resources must be put to their most productive use.

The proposed credit ceilings seemed appropriate, given the objectives of facilitating drought relief and allocating sufficient credit to productive sectors, Mr. Suraisry continued. The authorities intended to maintain strict limits on domestic bank financing of the budget deficit. They would be able to carry out their plans to finance part of the deficit through long-term bond issues, which should help to keep inflationary pressures down and could contribute to the development of a more active domestic capital market.

He could support the objective of limiting the expected deterioration in the balance of payments caused by the drought, and the authorities should continue their commitment to a flexible exchange rate strategy of the sort that had served the economy well in the recent past, Mr. Suraisry said. Also, he could support the plans, outlined in the letter of intent, to promote nontraditional exports. Despite the present emergency, the authorities should continue the process of import liberalization, which had already contributed significantly to improved supply conditions in the economy as a whole. If outward-looking policies could be maintained, prospects were good for achieving a sustainable balance of payments and a manageable debt service ratio over the medium term. Finally, the proposed program should provide a good basis for tackling persistent structural weaknesses in the economy. It was thus disappointing to note from Attachment V that the World Bank was not satisfied with Kenya's progress in several important areas. The authorities should make a renewed effort to improve the management of public finances, strengthen development planning, and liberalize the trade system in coming months. Action in those areas was essential if Kenya's development strategy was to succeed.

Mr. Alfidja observed that Kenya had performed well under the previous stand-by arrangement. In 1983, real GDP had grown by nearly 4 percent, inflation had declined, and exports had expanded, albeit moderately. Also, the adjustment effort had led to a halving of the fiscal and current account deficits and to significant repayment of bank loans by the Government. Performance in 1984, though less spectacular, nonetheless bore testament to the resilience of the economy in reacting to the difficulties arising from the severe drought and the unsettled world economic environment. The fiscal deficit and inflation were estimated to be broadly in line with program projections; bank credit to the Government was likely to be much lower than planned, while the foreign exchange reserves position more than met expectations. Those results reflected, inter alia, the effects of the numerous actions taken by the Kenyan Government under the stabilization program and the spirit of commitment and display of prudence with which those actions had been implemented. The substantial increase in producer prices beyond the rise in the consumer price index, the prudent wage policy pursued by the authorities, the imposition of higher taxes on already heavily burdened commodities, the gradual liberalization of import restrictions, and the adoption of a more flexible exchange rate policy had all helped to bring about the aforementioned results.

He could support the Government's intention to continue to work toward a restoration of fundamental equilibrium in the economy in spite of the devastating effects of the drought, Mr. Alfidja continued. On balance, most of the macroeconomic targets in the proposed program seemed reasonable. The moderate rise in the fiscal and external current account deficits forecast for 1985 suggested that the underlying adjustment effort must be maintained. In that regard, he could support the thrust of the policy orientation and the measures envisaged or already undertaken under the proposed program. The continuing freeze of wages and salaries of government workers was certainly an indication of the authorities' commitment to the pursuit of the domestic adjustment effort. The outcome of that effort would be more rewarding, however, if factors beyond Kenya's control were to have a less adverse impact on the economy. For example, the effort toward import liberalization could not but be hampered by the deterioration in the terms of trade forecast for 1985.

Finally, Mr. Alfidja noted that Kenya's debt service ratio was estimated to have increased by 10 percentage points over the past four years and was projected to increase further to 31 percent in 1985. While much of the debt was related to loans granted on concessional terms--and was therefore not as worrying as it might otherwise be--the Government should nonetheless take steps aimed at keeping the debt service payments to more manageable levels. In sum, he was heartened by the gains achieved under the previous adjustment program and could support Kenya's request for assistance under the proposed arrangement. It was to be hoped that donor countries would show the necessary support during their upcoming meeting in which Kenya's request for financial assistance was to be considered. Also, he looked forward to hearing the views and recommendations of management with regard to any request that might be forthcoming from the authorities for a purchase under the compensatory financing facility to finance the increased cost of cereal imports.

Mr. Ortiz remarked that since the approval of an 18-month stand-by arrangement at end-1982, Kenya had undertaken a strong and successful adjustment effort. Not only had the authorities adhered strictly to the program's targets, but also some of the results had exceeded expectations. For example, the budget deficit and the improvement in the balance of payments had been considerably better than expected; the liberalization of the import regime and the external payments system had been on schedule; domestic and cultural prices had been raised in real terms, providing incentives for food production; monetary policy had been consistent with credit expansion objectives; and incomes policy had been prudent. Unfortunately, just when all had been going well, Kenya and a number of other African countries had been severely affected by a damaging drought, although the Kenyan authorities to their credit had continued to follow recommended policies in spite of the magnitude of the economic crisis brought about by the drought. Of course, it had been the earlier decision of the authorities to follow appropriate pricing policies for agricultural goods that had permitted the accumulation of strategic grain reserves, which had allowed the authorities to cope initially with the worst aspects of the crisis, avoiding to some extent the disastrous effects experienced in other countries. Their success underlined the importance of maintaining appropriate pricing policies in the agricultural sector.

He strongly supported Kenya's request for a stand-by arrangement, which had appropriately been made contingent upon the securing of adequate financing, Mr. Ortiz continued. Also, he could support the proposed program for 1985, two elements of which were deserving of particular comment. First, the accumulation of drought-related effects on the balance of payments, the government budget, and the general course of economic activity posed some problems in Kenya. The program rightly contemplated a temporary increase in the current account deficit and in the budget deficit for 1985, although the underlying "basic" deficits were to be reduced further. He questioned whether the provisions of the program would be sufficient to meet the drought-related expenditures; even if they were realistic, there remained a rather large financing gap, which had not yet been filled.

The balance of payments forecast for 1985 and following years were based on the assumption that, in 1985, rains would resume their normal pattern, and agricultural production would be stabilized, Mr. Ortiz remarked. While it was encouraging to note early signs of more normal rainfall, he wondered whether, even if rain patterns were to return to normal, it was reasonable to expect the recuperation of agricultural production to occur in only one year. On the one hand, the medium-term balance of payments projections suggested that food imports would drop sharply in 1986 to the equivalent of SDR 14 million, after reaching an average level of SDR 127 million in 1984 and 1985. On the other hand, exports of tea--Kenya's main export product--were projected to increase at an average rate of 8.8 percent in volume terms during the period 1986-89. Considering that the average increase in export volume had been only 3.5 percent during the seven-year period between 1977 and 1983--a period apparently unaffected by natural disasters of the magnitude recently experienced--he wondered whether the projections for import growth were realistic.

Even assuming that the balance of payments projections were accurate, a large financing gap would remain for 1985, Mr. Ortiz noted. The negotiations on a Eurocurrency loan of $100 billion were therefore encouraging, although it would be preferable to cover the financing gap with a greater proportion of aid or other concessional resources, since debt service ratios appeared to be high and their eventual decline was based on the rather optimistic balance of payments outlook to which he had earlier referred.

He took note of the establishment of different consumer and producer prices aimed at strengthening the finances of the National Cereals and Produce Board and thus helping to meet the additional costs incurred in the transportation of grains to the countryside, Mr. Ortiz commented. Such differential pricing schemes usually proved to be self-defeating; producers were tempted to bypass the government agency and sell directly to consumers. In the circumstances, he would appreciate staff comment on the rationale for the differentiation in consumer and producer prices.

Mr. Coumbis said that he had no difficulty supporting the proposed program and Kenya's request for a new stand-by arrangement for 1985. The objectives of the program were to minimize the negative effects of the drought on economic activity while maintaining sustainable budgetary and balance of payments deficits in the medium term. Fiscal, income, and exchange rate policies had been designed to support those objectives. The most crucial problem in the program was the $90 million financing gap expected in the overall balance of payments in 1985; given the high debt service ratio, financing to meet that gap should be obtained quickly on concessional terms. The forthcoming donors' meeting would respond positively to Kenya's request for additional assistance, especially since the Eurocurrency loan currently being negotiated would cover only a small portion of the overall deficit.

Improvements were clearly needed in the financial control of the public enterprises and in their access to bank credit, Mr. Coumbis continued. Shortages in technical staff and certain legal impediments were delaying progress in that area. The authorities should redouble their efforts to review the viability of the public enterprises with the aim of liquidating the inefficient ones and securing better financial control over the remainder.

Also necessary was more rigorous implementation of the export development program, Mr. Coumbis remarked. The actions taken to free the external sector, apply a proper exchange rate policy, and facilitate remittances of investment income were measures in the right direction; however, while they were necessary conditions, they were not sufficient to secure sustainable and diversified increases in exports. Kenya's producers must gain experience in modern marketing techniques, and foreign investors must be convinced that Kenya's economic environment would remain stable before they increased their investment in export-producing industries. Generally speaking, consistent long-term efforts by the authorities and systematic programming would be required to fulfill those objectives.

While projections suggested that Kenya's balance of payments position would be viable in the medium term, Mr. Coumbis observed, there were significant differences between those projections in Table 9 of EBS/84/261 and data for the same items in Table 7 of the previous staff report, particularly in the forecasts for exports and for imports of goods and services. Because the medium-term forecasting exercise was an important part of the adjustment program, he would have felt more comfortable if all the relevant assumptions and hypotheses on which the medium-term forecasts were based had been outlined clearly in the staff report, together with an analysis of the sensitivity of the forecast figures to changes in the basic hypotheses and assumptions. In the case of Kenya, he wondered whether the staff had examined the sensitivity of exports to changes in the prices of tea and coffee over the next four years. The possibility of inadequate rainfall in 1985 could not be excluded, and he wondered about the probable effects of such a development on the balance of payments and its viability in the medium term.

Finally, like others, he found surprising the World Bank's dissatisfaction at the "degree to which Kenya met the commitments included under the program" and the fact that "the World Bank is not presently contemplating the negotiation of a third structural adjustment loan." Given the excellent performance of the Kenyan authorities with respect to Fund adjustment programs, he had difficulty understanding that country's problems vis-à-vis the World Bank.

Mr. Polak said that the Kenyan authorities were deserving of commendation for their determined efforts toward adjustment. Kenya's immediate prospects were not bright: while economic growth had picked up in 1985 at a rate of 4 percent, the weight of the drought bore heavily on the internal and external accounts, and the projections at present were for an increase in both the fiscal and balance of payments deficits. However, the policy measures introduced by the authorities in 1983 and 1984 had helped to strengthen the underlying balance of payments and had increased Kenya's ability to meet the crisis situation created by the drought. As a result of the drought, Kenya would probably be able to qualify for purchase under the compensatory financing facility. Would the staff estimate the maximum amount that might be available to Kenya under that facility and clarify the relationship between that amount and the projected financial gap for 1985?

In October 1984, many Directors had been in favor of an extended arrangement, in combination with a structural adjustment loan from the World Bank, as a follow-up to the previous stand-by arrangement, Mr. Polak recalled. Due to the drought, however, the authorities and the staff had concentrated on the immediate problems in Kenya and had put together the proposed one-year program. If properly implemented, that program could serve as a bridge to an extended arrangement and a third structural adjustment loan. It would be useful for the authorities to look beyond the short-term stabilization effort of the proposed program toward structural adjustment of the sort that would meet the World Bank's expectations and would, in the longer run, help Kenya to function without assistance from the two institutions.

The Government's cautious incomes policy had been successful as a means of reducing current expenditure, Mr. Polak noted. The most recent increase in public sector wages had been in 1981, and no increase was planned for 1985; at the same time, private sector wages had been compensated over the period up to 75 percent of the increase in the cost of living. He wondered whether the tight wage policy could be maintained in the long run or even whether the effort to maintain it was desirable, since it could damage morale in the public sector and lead to a loss of qualified personnel. Indeed, there was evidence that the public sector was already short of qualified personnel, a fact that might help to explain the delay in the country's application for a purchase under the compensatory financing facility. Moreover, the problem seemed to be related in large part of the very slow progress of the auditing review of public sector enterprises.

Noting that projections for developments in 1985 and the medium term were based on assumptions that weather conditions would return to normal, Mr. Polak remarked that adverse conditions could require additional measures or a further strengthening of measures under the program. On balance, the Fund should be pleased with the general approach that the Kenyan authorities had taken toward adjustment, and he could support the proposed stand-by arrangement.

Mr. Salehkhou observed that economic and financial conditions in Kenya remained difficult, despite an impressive performance under a Fund-supported adjustment program over the past two years. The renewed deterioration had been due entirely to the impact of the severe drought, which was damaging most countries in sub-Saharan Africa and which, in the case of Kenya, might have been more destructive if not for the adjustment and strengthening of the economy achieved in 1983 and 1984.

Performance under the most recent stand-by arrangement contrasted favorably with experience under three previous successive arrangements, Mr. Salehkhou continued. All performance criteria had been met, and the program had remained largely on track throughout the adjustment period. Furthermore, while real economic growth had remained rather weak, particularly when viewed against Kenya's high rate of population growth, substantial progress had been achieved with respect to the stabilization of the economy, the curtailment of budgetary and external current account deficits, and the containment of credit expansion and inflationary pressures. The overall balance of payments position had also significantly improved, with a turnaround from large deficits in 1981 and 1982 to relatively sizable surpluses in the past two years, which had enabled Kenya to strengthen its international reserves and should thus cushion to some extent the impact of the severe drought on the economy in 1985.

Some favorable exogenous developments had undoubtedly played a major role in Kenya's good economic performance over the past two years, Mr. Salehkhou remarked. Certainly, improved weather conditions in 1983 and the considerable recovery in the international prices of Kenya's major export items had been beneficial; it was equally clear, however, that major credit for the authorities' success was due to their determination to implement the program and their willingness to take additional measures in order to ensure that the program targets were met. In particular, the authorities had adopted more adequate producer prices in the agricultural sector, implemented a flexible exchange rate policy, liberalized the trade system, and implemented restrained fiscal and monetary policies. Unfortunately, the impact of the drought on the budget and balance of payments would be particularly severe in 1985 and, to that extent, had necessitated a change in the immediate goals of economic policy under the proposed program. While the authorities had been prepared to shift the emphasis of their adjustment policy toward the resumption of appropriate real economic growth and the introduction of structural reforms--particularly through the implementation of the latest Five-Year Development Plan--the severity of the drought had made it necessary for the authorities to focus on emergency measures aimed at giving relief to the population. In the circumstances, the 1985 financial program to be supported by a Fund stand-by arrangement appropriately limited its objectives and aimed at maintaining as much as possible the progress achieved over the past two years while facing the emergency situation resulting from the drought. In that respect, he welcomed the continuation in 1985 of the main adjustment policies implemented under the previous program; those policies should result in a further adjustment in the underlying budgetary deficit. The deterioration in both the budgetary and the external current account deficits projected for 1985 would be due mostly to the impact of the drought, not only through additional relief expenditures and huge emergency imports but also through the impact on economic activity and the availability of exports.

The implementation of growth-oriented policies should not affect the priority given in the development plan to the objective of maintaining the country's food self-sufficiency by promoting the expansion of foodstuffs production, Mr. Salehkhou considered. Although the increase in development outlays should be faster than GDP over the next two years, capital expenditures would remain significantly low in an economy where the public sector played such a major role. The authorities should use any additional foreign grants and loans to restore development outlays to a more appropriate level rather than to reduce domestic financing of the budget, which did not seem to be excessive in view of Kenya's special conditions and the progress already achieved in containing inflationary pressures. On balance, he warmly supported the proposed decision.

Mr. Lundstrom considered that the authorities' successful implementation of the previous stabilization program had put the Kenyan economy on track toward what appeared to be a sustainable balance of payments situation in the medium term and toward reduced imbalances in the domestic economy. The serious drought was impeding those favorable developments and a deterioration in Kenya's terms of trade was in prospect for 1985. In the circumstances, he welcomed the proposed program and hoped that it would lead to a consolidation of the gains obtained in the current account of the balance of payments, improve the underlying fiscal position, and reduce inflation while leading to an increase in the rate of growth.

It was his understanding that a number of Directors had recently been urging the staff to comment more extensively on access limits proposed under stand-by arrangements, Mr. Lundstrom remarked. He had found very little language in EBS/84/261 dealing explicitly with the important issue of access and would welcome staff elaboration on the matter. At first glance, it appeared that access under the proposed arrangement was appropriate, in light of the measures taken to reduce domestic and external balances to more viable levels and taking into account the more comfortable debt situation of Kenya relative to other developing countries. On the fiscal side, for example, if appropriate action was taken in the 1985/86 budget, the overall budget deficit would be reduced to less than 4 percent of GDP. The projected rather slow improvement on the external side should be seen in light of the further import liberalization measures planned by the authorities. Even if Kenya were recognized as a prolonged user of Fund resources, the implementation of the previous program and the structure of the new one were indications of the authorities' willingness and ability to cooperate with the Fund. The share of financing that it was proposed should be provided by the Fund seemed adequate to provide the necessary catalytic effect to the program; a positive response by others to Kenya's request for additional assistance was crucial, and he strongly supported the Chairman's introductory appeal for such assistance. The World Bank remained dissatisfied with program implementation under the structural adjustment loan at the same time that the Fund was expressing satisfaction with experience under the most recent program. He hoped that the staff would be able to shed some light on those differences as they related to the issue of Fund/Bank cooperation in Kenya. In conclusion, he could support the proposed decision.

Mr. Jayawardena observed that Kenya had successfully implemented the 18-month stand-by arrangement ended September 1984. The request for a new arrangement had been necessitated by a severe drought, which had affected Kenya and most other countries in sub-Saharan Africa. Since the proposed program would help Kenya to persevere with the adjustment process initiated in 1983, he could strongly support the proposed decision. While he had some misgivings about the 30-day limit and would have preferred greater flexibility in the decision, he was willing to join a consensus on the basis of the Chairman's indication that such a limit would ultimately help Kenya to obtain the necessary financing.

The proposed 1985 financial program aimed at reducing the fiscal deficit from 5.1 percent in 1985 to 4 percent in 1986 and at reducing the external current account deficit from 5.6 percent in 1985 to around 3.5 percent in late 1989, which was roughly equal to the net official capital inflows projected for Kenya at that time, Mr. Jayawardena observed. The program depended crucially on the maintenance of a real growth rate of 4 percent in 1985, 5 percent in 1986, and 6 percent at the end of the decade, with inflation limited to about 6-7 percent over the medium term. The debt service ratio as a percentage of current receipts was expected to decline from about 29 percent in 1984/85 to about 21 percent in 1989. The targets he had mentioned would be attainable only under fairly normal weather conditions, and Kenya might wish to consider alternative courses of action to be taken in more adverse situations, especially if the growth and inflation objectives turned out to be unattainable. More generally, some sort of contingency planning would be desirable.

Fiscal policy under the program was appropriate, although development outlays were below the levels of four years previously, largely because of the drought, Mr. Jayawardena commented. He was concerned that continued low levels of development spending might have adverse consequences for economic growth in the long run. Greater flexibility and more liberal phasing of purchases might have helped Kenya to deal more effectively with its current difficulties. As it stood, the staff was recommending five purchases: the first SDR 8.5 million on approval, followed by two quarterly purchases of SDR 21.3 million each, followed by two quarterly purchases of SDR 17 million each. In his view, Kenya's problems were immediate, particularly with respect to drought relief, and he was inclined to feel that a front-loaded program would have been more beneficial. Also, Kenya should have considered making a purchase under the compensatory financing facility to help pay for the costs of the exceptional cereal imports necessitated by the drought. He wondered whether recent attempts to reduce access to the compensatory facility might not have prevented Kenya from drawing on the facility. The Kenyan case was the third in recent times in which he had been left with the rather uneasy feeling that the Fund was constrained increasingly in its ability to assist countries meaningfully because of recent efforts to reduce access to Fund resources. That matter should be discussed frankly on the basis of a staff paper at some future date.

Mr. Nebbia noted that the objectives of the stand-by program ended September 1984 had all been met or exceeded. Substantial improvement in the public sector enterprises had been registered. Fiscal policy had been comprehensive and well managed and had led to a sharp reduction in the fiscal deficit. The target for the deficit in 1985, while showing a slight rise from 1984, was appropriate, given the drought relief effort and the expectation of a reduction of the deficit in 1986.

Wage policy in Kenya had been tight, Mr. Nebbia observed, and had led over the years to an impressive drop in real wages in the public sector. He wondered whether a continuation of a wage freeze for FY 1984/85 was appropriate, given the drain of qualified personnel from the public to the private sector. He shared the concern of the authorities with respect to some of the difficulties that they might be facing in future in securing better control over the public sector enterprises.

Recent economic developments in Kenya showed that a mix of low interest costs, long maturity and grace periods, and an improved current account had led to projections for a reasonable debt service burden in the medium term, Mr. Nebbia remarked. Export performance during 1984 had been good, not only because of the flexible exchange rate policy pursued by the authorities but also because of an improvement in the major external market for Kenya's products. The Kenyan case showed that both factors constituted a necessary condition for correcting the external imbalances of any economy. He welcomed the new export promotion program proposed by the Government; the expansion of nontraditional exports should prove promising for the country's economy. At present, of course, Kenya was facing a dramatic and temporary problem because of a severe drought. The staff had evaluated the effects of the drought on the fiscal and external accounts and on growth prospects but had apparently not felt that the emergency situation should have any impact on the process of import liberalization. While he agreed with the trend toward a progressive liberalization of the country's import system, he recognized that the drought and its extended effects might prevent major steps toward import liberalization during 1985. Finally, in expressing the support of his chair for the program and proposed decision, he urged donor countries to fill the balance of payments financing gap projected for 1985, not only as an indication of goodwill toward Kenya but also as a way of sharing the burden of uncertainty in the present international financial environment.

Mr. Zhang remarked that on the basis of its past adjustment record and its urgent present needs, together with the authorities' intention to undertake further strong adjustment measures if warranted, he could support Kenya's request for a new stand-by arrangement.

The staff representative from the African Department, recalling questions by some Directors on the pace of import liberalization under the previous program, observed that Kenya had begun the previous program having just weathered a disastrous coup attempt that had had a marked impact on the country's balance of payments, occasioning substantial outflows of capital. At that time, the progress that Kenya had been making with respect to import liberalization had been reversed for obvious reasons. Once the capital outflows had been stemmed, the authorities had continued to implement the import liberalization program, albeit somewhat more cautiously. In fact, given the drought conditions, import liberalization had proceeded more rapidly than might otherwise have been expected. Moreover, under the proposed program, as specified in the letter of intent, the authorities were committed by the time of the first review to implement a further round of import liberalization measures. Feedback from commercial importers in Kenya and information on investors from other countries suggested that the amount of restraint that was being imposed by the system had been considerably minimized and that imports were, to a great extent, being licensed on an automatic basis. Some groups of imports were more heavily restricted than others, largely on the basis of the "infant industry" argument, and it was those imports that it was hoped would be liberalized during the course of the proposed program.

Similar concerns had been expressed by Directors with respect to the pace of exchange rate adjustment, the staff representative noted. The authorities had been making an effort to bring the exchange rate to the same level that had existed in the early 1970s, which would result in an exchange rate comparable to that obtained under the first extended arrangement between Kenya and the Fund negotiated before the coffee boom and the institution of the restrictive import system that the authorities were currently attempting to liberalize. That restrictive system had emerged after the large investments that had been made during the coffee boom and following the collapse of the East African Community. Against that background, the targeted adjustments in the exchange rate seemed adequate. Also, the staff was projecting an improvement in Kenya's terms of trade in 1985/86 from the position that existed in the early 1980s; that should strengthen the position of the exchange rate.

Directors had shown considerable interest in developments with respect to the public sector enterprises in Kenya, the staff representative recalled. However, some of the problems might have been exaggerated, and more care should perhaps have been taken by the staff to outline actual progress in improving the public sector enterprises. The Kenyan public sector was a large system, with 47 wholly owned enterprises and more than 100 companies with government majority or minority participation engaged in a wide variety of economic activities. However, as noted on page 22 of EBS/84/261, many of the latter were controlled through the wholly owned enterprises, a fact that should allay some of the fears expressed by Mr. Prowse about the pace at which the audit of the public sector enterprises was continuing. An audit of one of the wholly owned enterprises would cover as well a considerable number of the investments made by the company in question. For a number of years, there had been little in the way of budgetary resources transferred to the public sector enterprises, and the Government's effort currently was to ensure that its previous investments were yielding what it considered to be an appropriate return. A problem naturally arose because the authorities were notifying enterprises with foreign and domestic private participation that, henceforth, the Government expected to be repaid for previous loans that had been granted, with the possibility of converting some loans into equity. Too strong an interference might lead to accusations that the Kenyan Government was restraining investment, and the authorities had thus acted cautiously because they were aware of the benefits that private domestic and foreign investment would have for the Kenyan economy. As for the auditing exercise, it was clear that many of the enterprises did not wish to show the Government the sort of profits that they might have been making but not sharing with the Government; consequently, the exercise became a difficult one, particularly in those cases where the Government did not have the legal authority to demand that the books of the individual enterprises be opened to it. In order to make up for a lack of expertise in performing the audit, the Government was in the process of hiring outside consultants.

The impact of the constraint in wages in the public sector had been negative, particularly at the higher levels where there had been some loss of qualified personnel, the staff representative noted. The Government had intended during the course of 1985 to review and perhaps increase public sector wages, but the financial demands brought on by the drought had made such a review impossible. Still, the President had announced during a recent speech that in the course of 1985 a commission would be formed to review public sector wages; and a wage adjustment was likely to be included in the next budget, by which time it was to be hoped that resources currently being utilized for drought relief would be available for other purposes.

With regard to comments on the medium-term projections for Kenya, the staff representative observed that longer-term estimates should be viewed as "directional" in the sense that they indicated possible developments, given domestic policies and trends in the international environment. One of the areas that had received attention had been the slow growth of imports; indeed, several Directors had noted that the projections included a growth of total imports of only 2 percent per year in the period 1986-89, and they had asked whether such growth was consistent with Kenya's efforts to liberalize imports. It was not appropriate to look at the growth of overall imports in that way. After 1985, there should be a substantial reduction in the importation of foodstuffs, which would permit a significant growth in other imports. The program as written included a projection for growth in nonfood, non-oil imports in excess of 6 percent, which was considerably higher than the estimated growth of income during the period.

The medium-term balance of payments and debt service projections were consistent with expectations of capital inflows and repayment projections through 1990, the staff representative said. Noting the increased difficulty that countries were likely to have in obtaining the sort of long-term concessional financing available in the past, the staff had included in its projections a higher percentage of commercial-type borrowing than had been recorded in previous years. Even so, there appeared to be a marked and sustained fall in the debt service ratio over the medium term. Sensitivity analyses on the matter suggested that much depended on the sort of development plan that the Government would be able to implement during the period, the import content of that program, and, more important, its financing. For other assumptions, particularly those regarding export growth in volume terms and projected import prices, the staff had tended to be conservative and even pessimistic.

It was clear from the discussion that most Directors felt that Kenya was adopting a second or third-best solution in meeting the projected balance of payments financing gap by resorting to commercial-type borrowing, the staff representative remarked. However, note must be taken of the fact that the authorities' efforts to obtain additional donor support had not been successful to date, perhaps because others in Africa appeared to have greater needs at present. The Kenyans were concerned that their call for help had not yet produced as positive a response as they had expected, but they were hopeful that the February donors' conference would yield the resources needed. The donors should recognize that Kenya's financing needs were immediate; a large amount of food grains must be imported and paid for during the first quarter of 1985, and an inadequate or inconsistent financing plan for the period could have a negative impact on Kenya's policy stance in other areas.

Responding to those who had asked what would happen if the drought were to continue, the staff representative commented that most of the effects would emerge in 1986, when there might again be a need to import grains equivalent to $200 million; and certain exports, particularly tea exports, would be adversely affected.

One Director had noted a large increase during FY 1983/84 in the banking system's credit to the public sector enterprises, the staff representative recalled. Most of that increase was related to credit granted to the National Cereals and Produce Board for the accumulation of the strategic grain reserve and was not expected to be repeated in 1984/85. Moreover, there had been no crowding out of private sector enterprises. In fact, there had been margins under the ceilings for increased credits, and the banks had had considerable liquidity at the time. The small growth attributed to the private sector had been more a reflection of the slow reversal of private sector activity following the coup attempt and other difficulties. However, in the proposed program, the staff had made sure that the public enterprises would not be a major recipient of credit during the current fiscal year.

In response to a question by Mr. Clark, the staff representative observed that the grants that had been included in the budget were only those confirmed at the time the staff had visited Nairobi; any other grants or loans that might become available should be counted as additional to those in the Government's budget projections. Mr. Clark had also felt that the amount of credit being granted was perhaps excessive, given the expected growth in income. It was precisely that fear that had led the staff to establish the automatic mechanism to reduce credit flows as additional foreign resources were made available. If the full financing gap was met through foreign borrowing, which went through the budget, a very small growth in credit would be allowed, which would be just marginally in excess of the nominal GDP projections. Credit from nonbanks had not been included under the ceiling and was expected to arise largely as a result of the nonbanks being able to meet their liquidity ratio requirements, which forced them to buy a certain amount of treasury bills during the year. In the previous fiscal year, the Government of Kenya had been successful in obtaining resources from nonbanks; indeed, the staff had attempted to calm the authorities' enthusiasm for using that type of resource, which it felt might leave certain borrowers short of available credit. In that regard, the projections for the current fiscal year included only K Sh 1 billion in nonbank borrowing as compared with K Sh 2.2 billion in the previous fiscal year.

A number of Directors had suggested that the tea export projections might be optimistic, the staff representative commented. The tea sector was one of those in which the authorities' pricing and exchange rate policy had been particularly successful: tea planting had expanded at a rapid rate, aided by various government programs specifically targeted for small holders, and projections included in the program simply reflected the planting that had taken place in the late 1970s and early 1980s and that would begin producing in the medium term.

The Executive Directors agreed to resume at 3:00 p.m. their discussion of Kenya's request for a stand-by arrangement.

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/85/1 (1/4/85) and EBM/85/2 (1/9/85).

4. MOROCCO - RELEASE OF INFORMATION

The Executive Board approves the proposal set forth in EBD/85/6 (1/4/85) to release the staff report for the review of the stand-by arrangement with Morocco (EBS/84/256, 12/7/84 and Sup. 1, 12/28/84) to participants in the meeting of the Consultative Group for Morocco to be held in Paris from January 9 to 11, 1985.

Adopted January 7, 1985

5. APPROVAL OF MINUTES

The minutes of Executive Board Meetings 84/85 and 84/86 are approved. (EBD/84/324, 12/27/84)

Adopted January 4, 1985

6. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors and by an Advisor to an Executive Director as set forth in EBAP/85/1 (1/3/85) and EBAP/85/2 (1/7/85), is approved.

APPROVED: October 23, 1985

LEO VAN HOUTVEN
Secretary