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**Statement by Mr. Misra and Mr. Prasad on Sudan
(Preliminary)
Executive Board Meeting 05/100
November 30, 2005**

1. We thank staff for a candid midyear review of the 2005 staff monitored program and the accompanying documents.
2. Notwithstanding the difficult political and macroeconomic situation, the authorities continued to show commitment toward further reform. Particularly commendable is the progress in the implementation of structural reforms listed in the comprehensive buff statement of Mr.Ngumbullu and Mr.Mafararikwa. Lasting peace is essential for sustained growth and improvement in the business environment. The temporary setback in the implementation of peace agreement earlier in 2005 resulted in the worsening of the fiscal position, expansionary monetary conditions and buildup of inflationary pressures. In April 2005, Sudan faced challenges in five areas, viz., containing inflationary pressures, prioritizing expenditure, strengthening public expenditure management, increasing transparency in the oil sector and containing nonconcessional borrowing. The progress in many of these areas has been lower than expected and we welcome the corrective actions that are being put in place by authorities to improve the situation.
3. The growth outlook for 2005 is positive. The balance of payments outlook is also favorable, reflecting higher oil exports. The increase in non-oil imports does not seem to be of major concern to us because of the links of machinery and manufacturing imports to growth. It is of concern that inflationary pressures have built up. The slow pace of the implementation of the peace process has resulted in expenditure overruns leading to a weaker than expected fiscal performance. The fiscal deficit would have been even higher if the transfers had materialized. The resultant monetization of the fiscal deficit has led to an increase in reserve money and broad money growth, adding to inflationary pressures. Noting from the buff statement of Mr.Ngumbullu and Mr.Mafararikwa, the circumstances under which Sudan resorted to nonconcessional external borrowing this time, we continue to feel that there is no room for maneuverability on this front as debt remains unsustainable, far exceeding the HIPC threshold.
4. It seems that net domestic assets are rising due to central bank financing of the fiscal deficit and net foreign assets are increasing due to intervention in forex marks. But, the

authorities are not sterilizing enough, and by not doing commensurate operations in the domestic money markets, money supply is growing very fast and inflation has crossed the double digit mark. Mopping up the existing monetary overhang at these rates of inflation is bound to be costly. In the current environment, high inflation is hurting the competitiveness of the non-oil sector anyway and hence the argument that the authorities are avoiding further appreciation to avoid competitiveness erosion does not make too much sense as inflation is working against them, despite central bank actions resulting in containment of inflation to some extent. The authorities must concentrate on implementing the remaining structural reforms on the agenda and modernizing the financial sector to improve competitiveness.

5. We are broadly in agreement with the revised financial program for the second half of 2005. We are of the view that that with additional sterilization, there is scope for a lower inflation target in the program. The revised revenue target seems appropriate and so does stalling of non-concessional external borrowing. The intention to restrain growth in nonpriority spending is commendable although we observe that current expenditures are set to increase sharply due to subsidy element for oil. We see little justification for an oil exporting country like Sudan to give government subsidy for fuel. While we welcome the intentions of the authorities to increase fuel prices by end-2005, coinciding with the start of oil production, we look forward to a shorter time line than indicated toward automatic adjustment of fuel prices so that the subsidy funds so released could be better targeted for other priority spending.

6. Sudan has been regular in making monthly payments to the Fund. However, we agree with the suggestion of staff that Sudan should strengthen its payments effort in relative terms in view of its improved balance of payments outlook and urge the authorities to increase the level of payments to the Fund in 2006.

7. We support Mr.Ngumbullu's and Mr.Mafararikwa's request for Technical Assistance.

8. We thank staff for the update on the fundamental issues in resolving external debt problems and achieving debt sustainability for Sudan. Sudan's external debt situation is clearly unsustainable and progress is constrained since the options for receiving concessional donor financing are limited pending satisfactory resolution of conflict in Darfur. Efforts to expedite inclusion of Sudan and other protracted arrears cases in the MDRI are necessary and in the same vein as Mr.Shaalan and Ms.Choueiri, we concur with staff that bilateral contributions remain the preferred option. In fact, upfront commitments from bilateral donors will provide greater comfort to the authorities to take the reform process forward with greater momentum. As we had mentioned earlier, limited grandfathering seems to be a satisfactory option on the way forward. We look forward to the forthcoming follow up paper.