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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 08/52-2

10:45 a.m., June 16, 2008

2. Benin—2008 Article IV Consultation, Fourth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, and Request for Augmentation of Access

Documents: EBS/08/62 and Correction 1, and Correction 2, and Supplement 1; SM/08/161

Staff: Matungulu, AFR; Ogada, LEG; Plant, PDR

Length: 1 hour, 24 minutes

Executive Board Attendance

M. Portugal, Acting Chair

Executive Directors	Alternate Executive Directors
L. Rutayisire (AF)	R. Gesami (AE), Temporary K. Assimaidou (AF) D. Vogel (AG), Temporary S. Na (AU), Temporary J. Prader (BE) M. Agudelo (BR)
H. Ge (CC)	R. Guzman (CE) Y. Alvarez (CO), Temporary
A. Fayolle (FF)	S. von Stenglin (GR) P. Ray (IN), Temporary G. Cipollone (IT), Temporary N. Imamura (JA), Temporary J. Kwakye (MD), Temporary A. El-Ganainy (MI), Temporary T. Galac (NE), Temporary
J. Henriksson (NO)	A. Shabunina (RU), Temporary A. Al Nassar (SA) C. Sucharitakul (ST) N. Raman (ST), Temporary M. Lanz (SZ), Temporary M. Kaplan (UA), Temporary V. Pillai (UK), Temporary

B. Esdar, Acting Secretary
W. Rahman-Garrett, Assistant

Also Present

IBRD: A. Bassani, E. Kennedy. African Department: H. Bredenkamp, B.V. Christensen, R. Corker, L. Dwight, T. Krueger, M. Matungulu, J. Mongardini, C. Mummsen, D. Nellor, I. Samake, J. Wakeman-Linn, P. Youm. Finance Department: R. Basu. Legal Department: C. Ogada, N. Rendak. Policy Development and Review Department: M. Fisher, M. Plant. Secretary's Department: P. Martin, P. Ramlogan. Western Hemisphere Department: A. Bauer. Advisor to Executive Director: H. Yung (CC). Senior Advisors to Executive Directors: G. Collange (FF), F. Haupt (GR), S. Polak (BE), M. Sidi Bouna (AF), A. Umaña (CE). Advisors to Executive Directors: A. Maciá (BR), A. Matoto (ST), G. Mpatswe (AF).

2. BENIN—2008 ARTICLE IV CONSULTATION, FOURTH REVIEW UNDER THE THREE-YEAR ARRANGEMENT UNDER THE POVERTY REDUCTION AND GROWTH FACILITY, AND REQUEST FOR AUGMENTATION OF ACCESS

Mr. Rutayisire submitted the following statement:

On behalf of my Benin authorities, I would like to thank the Executive Board, Management and Staff for their continued support to Benin's efforts towards sustained reforms and sound macroeconomic policies. I would also like to thank staff for the fruitful discussions held during their recent visit to Cotonou. The reports tabled for the Board's discussion represent a candid assessment of the Beninese economy, and my authorities are thankful for constructive policy advice therein.

Recent Developments

Benin's economic performances under the PRGF-supported program continues to be broadly satisfactory, as reflected by the observance of all quantitative benchmarks for end-September and performance criteria for end-December 2007. With real GDP growth rate at 4.6 percent in 2007 and projected at 5.3 percent in 2008, the Beninese economy is firmly recovering from its downward trend of 2000- 2005, thanks to the steady resumption of cotton production, good performance in non-cotton agriculture, and the strong activities in the port as well as related transport and commerce sectors.

The fiscal consolidation engaged by the authorities since 2006 continues to yield positive results. Following a sustained implementation of reform measures to improve both governance and efficiency in the tax and customs administration, revenue collection has increased to 20.6 percent in 2007, outpacing the program target of 17.2 percent. On expenditure side, the authorities continued to tighten control over spending in line with the country's absorptive capacity and the needs to ensure quality. The resulting surplus on the narrowly defined primary fiscal balance of 3 percent of GDP in 2007, compared to 1 percent targeted, enabled Benin to meet the WAEMU convergence criterion on the non-negative narrowly defined fiscal balance.

The implementation of fiscal structural reforms also continued to move forward, despite at slower path than wished by the authorities due partly to difficulties that were initially unforeseen. Two structural benchmarks for the period under review—namely, the introduction of Single Taxpayer Identification Number (TIN) system and a study of the efficiency of customs—were completed before end-2007. In addition, appropriate steps have been taken to ensure successful completion before the year end of the two non-observed structural benchmarks, namely the audit of PFM information systems and the design of a strategy for the reform of the civil service pension fund.

Owing to prudent monetary policy, as well as to good harvest, average inflation eased at 1.3 percent in 2007, compared to 3.8 percent in 2006. However, the recent surge in food and fuel prices on the international market and its consequent inflationary pressures pose a threat to the macroeconomic stability already achieved and complicate the authorities' structural reform implementation agenda.

My authorities attempted to mitigate the impacts of world food price increases, particularly on vulnerable groups, by temporarily eliminating customs tariffs and reducing customs fees on highly consumed staple food items as well as through subsidies to the energy utility company. While the measures were initially designed to end by mid-March 2008, the persistent international food crisis warranted their continuation whilst government is designing support mechanisms that better target the poor and help avoid distortions in the domestic supply of the affected products. In addition, government is searching for long-term solutions to the crisis, including through regional concerted efforts toward the development of the agriculture sector. Government have also mobilized financial resources to cover the revenue loss from the tax cuts and subsidies, but additional resources are still needed, including from the Fund to help cover the resulting balance of payments financing gaps. My authorities would much appreciate the approval of the requested support.

Policy and Structural Reforms Agenda for 2008 and Beyond

Over the medium-term, my authorities intend to further push ahead their structural reform agenda, in order to resolve the challenging obstacles to a strong and sustained economic growth, to competitiveness and effective poverty reduction. Importantly, Benin authorities will continue to strengthen public investment, particularly

in social, agriculture and infrastructure sectors, and improve the business climate. In line with these reforms, economic growth is projected to reach 5.3 percent in 2008 and average 5.5 percent annually through 2011.

The authorities intend to achieve the above overall objective through the maintenance of a prudent fiscal policy over the medium term in line with their PRGF program, which aims principally at preserving the macroeconomic stability achieved so far. They will strive to meet the WAEMU fiscal convergence criteria and keep demand-induced inflationary pressures in check. In 2008, they target a primary budget surplus of 0.5 percent, which in turn would allow to contain the overall fiscal deficit to equivalent of 4.4 percent of GDP and the level of debt at sustainable path, whilst effectively responding to expenditure needs particularly in the social, productive and infrastructure sectors. To this end, my authorities aim to increase revenue collections to 18.4 percent of GDP by capitalizing on the recently introduced measures to broaden tax base as well as to further improve governance in the tax and customs administrations.

As a step in pursuing further their fiscal consolidation, the Beninese authorities have requested Fund's assistance to help review the country's tax structure. The findings of the review would allow the authorities to harmonize their tax rates with regional peers, to find ways of further enhancing domestic tax performance in light of the expected revenues losses from the signing of the economic partnership agreements (EPA) with the EU, as well as streamlining the effectiveness of the tax regime in promoting the development of domestic private sector. The technical assistance mission is expected in the course of June 2008.

On expenditure side, an increase of 12.2 percent is projected to help cater for the infrastructure rehabilitation program that started in 2007, the recent increase in the salaries of public sector teachers as well as the new recruitment of public servants to reinforce the capacity of key sectors. At the same time however, a tightened control over current expenditure will sustain, particularly on goods and services and wage bill. To the later end, the authorities have reaffirmed their preference to keep the wage ceiling as program conditionality, along with improvements in payroll systems and progress in the reform of the civil service pension fund. My authorities will step up efforts to address problems in public procurement and projects' management

systems. They will also build capacity to conduct feasibility studies, select and identify sources of financing for key infrastructure projects, and monitor their implementation. In this context, bi-monthly project execution reports will be discussed by the Council of Ministers and posted on the President's Office website.

My Benin authorities will continue to adhere to the prudent monetary policy conducted by the regional central bank BCEAO, which aims at preserving price stability. The Central bank targets an increase in the broad money at a rate of 8.3 percent equivalent to that of the nominal GDP in 2008 and the authorities will continue to restrain the net claims of the banking system on government following expected improvement in the public finances. As in 2007, this will allow for increase in credit to the private sector.

Steps continue to be taken to addressing the current vulnerabilities in the banking system. Government is carefully monitoring the implementation of the BCEAO decision to adjust the minimum capital from CFAF 1 billion to 10 billion over three years. Further, it is working with parliament to speed up the ratification of the regional agreement enhancing the supervisory powers of the WAEMU Banking Commission. With support from BCEAO national office, the technical ministry in charge of microfinance is increasing its supervision capacity, while oversight of large microfinance institutions falls under the BCEAO national office's responsibility. An evaluation of financial services demand has been completed under MCA-Benin's support. With all these findings as well as those from the recent regional FSA, the Beninese authorities intend to design a comprehensive strategy for development of the financial sector, which will help identify additional measures not only to reinforce the banking sector compliance but also to improve access to credit, especially by small - and medium-sized enterprises. The development of the financial sector, together with efforts supported by MCA-Benin to improve land tenure and the legal system, will help in creating an enabling environment for private sector businesses and diversification of the economy.

The implementation of other structural reforms will also continue to move forward, despite the challenging socio-political environment and insufficient capacity that constrain the political will of the authorities to accelerate them. With local elections recently completed, a new impetus to the reform program is expected,

including pushing ahead the administrative and financial decentralization agenda. Furthermore, the authorities are determined to continue enhancing dialogue on the economic benefits of the structural reform agenda by further involving participation of stakeholder groups and requesting technical support from donors.

Following the recent disappointing attempt to disengage the state from SONAPRA, principally due to limited private sector interest, the government is preparing a comprehensive strategy for the reform of the cotton sector. The new strategy will go beyond the solely state disengagement from the ginning activities, and tackle all aspects of the production and marketing chains. As an initial step, the government recently decided not to interfere with the awarding of contracts for importation and distribution of fertilizers and other inputs. In addition, a Strategic Policy Paper, which gives the main orientations of the reform, was approved by the Council of Ministers on May 19, 2008. The next step is the conduct of participatory consultations involving key stakeholder groups with a view to securing broad-based ownership of the reform. The process for the design of the strategy is expected to be completed by end-December 2008, while the implementation of the agreed measures is initially set to extend over a 2-3 year period.

Regarding the privatization of Bénin Telecoms, the implementation of its restructuring plan is under way, as approved by government and endorsed by main creditors. Furthermore, the policy measures taken by the authorities in 2007 have helped the GSM mobile phone telecommunication companies to fully resume activities and the interim regulatory authority—le Conseil Transitoire de Régulation des Postes et Télécommunications—has started to effectively perform its oversight prerogatives. As for the Société Béninoise d'Electricité et Energie (SBEE), the implementation of the restructuring is to last 2 years effective from January 2008 through December 2009, after which the government will make assessment to determine the nature of privatization.

Implementation of reforms to enhance the efficiency and competitiveness of the Port of Cotonou is advancing well. A “Port Expert”, who will help in the day-to-day management of the port, is to be operational by end of this month. Further improvement in the port competitiveness would derive from the effective implementation of the Virtual One-Stop Shop and the Consolidated Electronic Billing System

(Bordereau de Facturation Unique), which are expected by end-September 2008.

My Beninese authorities are thankful to the international community for its continued support, and for having chosen Benin among the 10 countries for which increased international support is being planned as part of the UN push to fast-track progress toward the MDGs. The Government believes that its reform agenda as embedded in the Growth Strategy for Poverty Reduction Paper (2007-2009) offers an appropriate framework for channeling the envisaged scaled-up aid. It looks forward to the completion of the assessment of the macroeconomic implication of the anticipated higher external assistance, expected later in 2008, as well as to continue working with the donors' community on building the country's capacity for policy design and implementation.

Conclusion

With the above commendable achievements, my authorities have once again demonstrated their commitment to—and ownership of—policies reforms laid out under the ongoing PRGF-supported program. Though challenges are still daunting, and some of the reforms will take time to fully yield sustained results, my authorities are committed to pursue their endeavors, accelerate the pace of the reforms to transform the Beninese economy. In view of the achievements during the period under review and the continuing commitment of the authorities to push ahead their reform agenda, I will appreciate the Board's support for the completion of the fourth review, and the approval for the requested augmentation of access under PRGF, as well as the completion of the 2008 Article IV consultations.

Mr. Bakker and Mr. Galac submitted the following statement:

We understand that Benin's macroeconomic performance continues to improve, and that its medium term growth prospects appear favorable. However, echoing concerns of Benin's donors, we are disappointed by the lack of progress on structural reforms, most of them being unaddressed or unsuccessfully approached by the authorities. We agree with staff that Benin's growth is likely to continue to fall short of what is required to rapidly reduce poverty and attain MDGs, absent a marked acceleration of structural reforms.

Therefore, we urge the authorities to be forward looking, and proceed forcefully with the already identified steps to carry out the much needed structural reforms, especially those that are part of the conditionality of the ongoing PRGF program, even if political support for their implementation has subsided recently.

Benin is a member of the West African Economic and Monetary Union (WAEMU). Staff analysis shows that Benin's competitiveness has been undermined by a real appreciation of its effective exchange rate, deterioration in the terms of trade, and some weakening in the business environment, and asserts that, as a small coastal economy with a fixed exchange rate, Benin must be especially ambitious in implementing structural reforms to address the competitiveness issue. We fully subscribe to this view, and note how it reinforces the argument for speeding up structural reforms. On a technical note, staff concludes that "a variety of macroeconomic analyses do not on balance provide evidence of significant misalignment of Benin's current account balance or real exchange rate." In this regard, we caution staff that according to the PDR guidance note (August 2007) the reference to "misalignment" should only be used at the level of the currency union.

Benin's three-year PRGF arrangement was recently extended until August 2009, performance on the program was generally satisfactory, and all quantitative benchmarks for end-September and performance criteria for end-December 2007 were observed by large margins. Noting that the authorities have taken some concrete steps to address the two missed structural benchmarks, we support the staff recommendation to conclude the fourth review under PRGF and grant waivers for the missed structural benchmarks.

The authorities have requested an augmentation of access (in the amount equal to 0.2 percent of the projected 2008 GDP) to deal with rising food and oil prices. Staff support the authorities' request, based on Benin's good capacity to repay the Fund (still low total access under the current program after augmentation) and its excellent debt servicing record. Moreover, staff contend that the request is justified on the basis of a weakening external current account, with the import bill projected to increase by 2.3 percent of 2008 GDP as a result of the shock from rising oil and energy prices, that would create a financing need for the overall balance of payments in the amount of 0.8 percent of 2008 GDP. Moreover, the authorities are already

actively discussing additional financing with other multilateral and bilateral donors that can help them in these difficult times. Against the above background we can agree to augmentation of access under the ongoing PRGF program. However, looking forward, we encourage the authorities to reconsider whether they can fine-tune their existing reform agenda for the agricultural and energy sectors to address long-term food and oil price risks. Staff comments are welcome.

Ms. Lundsager and Mr. Kaplan submitted the following statement:

Exchange Rate and Competitiveness

We congratulate the staff for its detailed analysis of real exchange rate developments in Benin, using a range of models and methodologies. The selected issues chapter, in particular, builds on the generally very high quality staff work that we have seen for the WAEMU and its members. We look forward to subsequent staff work to revise and extend the methodologies for similarly situated countries. The general conclusion is that Benin has lost competitiveness against other WAEMU members, which must be addressed through structural reform. Efforts to improve access to markets by eliminating physical and procedural constraints, such as Port of Cotonou improvements being financed by the Millennium Challenge Corporation, will help further strengthen the sustainability of Benin's balance of payments and foster economic growth.

Augmentation for Food and Fuel Shocks

Colleagues will recall that this chair recently abstained on the proposed augmentation of Mali's PRGF to emphasize our disagreement with the staff's strategy for responding to food and fuel shocks. Regrettably, we have similar concerns with the augmentation proposed today, and therefore wish to be recorded as abstaining.

Net Balance of Payments Impact

There is a case for Fund financing to help cushion necessary external adjustment when price shocks are having a significant impact on the balance of payments, but these conditions are not present in Benin. Petroleum imports are projected to increase by CFAF 25 billion in 2008, CFAF 6 billion worse than forecast at the January review. However, Benin's overall external position remains sound, with

stronger inflows from donors and private sources contributing to a small overall BOP surplus that exceeds prior expectations. Notably, Benin's share of regional foreign exchange reserves are projected to reach 15 months of imports.

Facilitating Adjustment

Although the BOP is sound, the authorities' fiscal policy response thus far—reducing customs tariffs on certain food imports and providing subsidies to the energy company—has cost 1 percent of GDP in revenues. The staff report indicates that these measures “are likely to be an inefficient and costly way to limit the impact on the poor and should be replaced by more targeted measures.” Mr. Rutayisire reports that his authorities are discussing moving to a more targeted fiscal safety net, but this remains a medium-term aspiration. The staff's newly negotiated quantitative performance criteria accommodate current policy through end-year, after which this PRGF will expire. In short, the augmentation partially offsets the fiscal cost of the authorities' response to the shock, but the program does nothing to promote necessary adjustment to food and fuel prices that will remain elevated at least through the medium term.

Role of the Fund and of Donors

Mr. Rutayisire also reports that his authorities are searching for long-term solutions to the crisis, including through regional concerted efforts toward the development of the agriculture sector. Our own Millennium Challenge Corporation has a focus in Benin on increasing access to land through more secure and useful land tenure. In view of the sharp increase in food and fuel prices, the authorities are reportedly consulting donors on incremental financial assistance for compensatory response, but we understand that no definitive commitments have been made.

For our part, we do not measure the relevance of the Fund by the speed with which it can increase its relatively unconcessional lending. Given that the Fund is not a development institution, we believe it is inappropriate for the Fund to have moved ahead of the donor effort. We strongly urge those donors with relevant expertise to assist Benin to design targeted social measures to help the poorest people. Can World Bank staff comment on whether its policy engagement is being retailored to address these issues?

Amended Decision

In the case of the last review for Benin, management amended the proposed Decision to facilitate a Board consensus on the review, with an abstention on the extension. We would accept a similar outcome in the current case to clarify our lack of support for the augmentation, but willingness to support the conclusion of the review. We appreciate the strain that the authorities are under in responding to the population's concern with sharp increases in food and fuel prices, and recognize that policy options are limited. We wish the authorities success in swiftly adjusting their policies to protect the poorest while maintaining hard-won macroeconomic stability.

Mr. Gakunu and Mrs. Gesami submitted the following statement:

We thank the staff for their informative set of papers and Mr. Rutayisire for his helpful buff statement. We commend the Benin authorities for pursuing prudent and sustainable macroeconomic policies, which should provide the foundation for further development. Having achieved this hard-won stability on the back of debt relief, Benin's challenges fall under the category of "which way now?" As staff quite rightly point out, growth while encouraging, is not sufficient to achieve the Millennium Development Goals and price stability has been threatened by the surge in world food and oil prices. Therefore, the main priority will need to be an intensification of structural reforms and absorptive capacity to achieve broad-based growth.

We are comforted by the indication in Mr. Rutayisire's buff that the authorities are committed to expanding the economy through acceleration of reforms, prudent fiscal management and continuous engagement of the private sector and, development partners. As we generally agree with the thrust of the staff report, we confine our comments to just four areas, namely the delayed reforms to the cotton and utilities sectors, the importance of improving the absorptive capacity, efforts to maintain debt sustainability, and the continuing implementation of measures to enhance the competitiveness and management of the port reform.

We are concerned that the much publicized acceleration of the structural reform agenda has not materialized and consequently the highly critical reforms to the cotton sector remain delayed. Given the large part of the population that is directly and indirectly involved in

the sector, it is vital that appropriate reforms are advanced as expeditiously as possible. Nonetheless, we are sympathetic to the authorities' reasons for the earlier delay in advancing state disengagement from SONAPRA. The World Bank's involvement, given their wide expertise in developing a comprehensive reform strategy for the sector, is welcome and urge the authorities to make full use of this opportunity. On wider structural reforms, we are encouraged by Mr. Rutayisire's statement that the authorities have renewed enthusiasm and commitment to engagement in a comprehensive reform agenda. Given the critical nature of the reforms to propel future growth, we urge the authorities to remain committed to their plans.

The second major issue appears to be advancing fiscal reforms. For a country like Benin to commit to saving better-than-programmed revenue performance, while fiscally prudent, is perverse given its pressing developmental needs. We would appreciate staff's clarification on what steps, are envisaged to improve the absorptive capacity and in the context of the PRSP, to promote greater efficiencies in expenditure?

On short-term measures to maintain spending discipline, we appreciate the authorities' request to continue using wage ceilings. However, we agree with staff that this cannot be a sustainable policy. It is clear that the long-term solution would need to involve improving the absorptive capacity. On a related issue, we note that a significant portion of the improved revenue performance in 2007 was a result of one-off sources. How do the staff see the evolution of revenue performance going forward?

We welcome the positive assessment of Benin's external debt sustainability. However, we are concerned about the deficit financing already contracted in the regional market through bonds issue whose proceeds were not used for projects now delayed. Against the need to maintain sustainable debt levels, we wonder whether such action was necessary.

Since MCA-Benin assumed management of the port reform, progress in devising an action plan has been encouraging. Inroads are being made into privatizing management of port facilities and improving customs administration—critical steps to enhance port competitiveness. We note the ongoing implementation of state

disengagement from the electricity and telecommunications sectors, and encourage the authorities to adhere to the reform timetables.

In conclusion, on the basis of substantial adherence to the program targets and benchmarks, which have all been met, we support the completion of the fourth review and the request for augmentation of access.

With these remarks, we wish the authorities continued success in the smooth implementation of the program.

Mr. Prader and Mr. Polak submitted the following statement:

We thank the staff for a frank assessment of the economic situation in Benin and

Mr. Rutayisire for his helpful buff statement.

We support the completion of the Fourth Review and the requested augmentation of access. The higher access will provide immediate resources to deal with the rising oil and food prices. The current need to increase the financing of the trade deficit also points to the high sensitivity of the economy to external shocks. Evidently, the authorities have to make a more substantial progress in structural reforms in order to improve the resilience of the economy.

In addition, although Benin's economic performance has continued to improve, it falls short of what is needed to achieve the MDGs. In order to succeed in reducing poverty, growth should be at least at the level of 7 percent. The staff have rightly emphasized that the main concern of donors is slow progress in implementing structural reforms. It is, therefore, necessary that the authorities proceed quickly and implement the long-overdue structural reforms. Doing so will boost potential growth and maintain the involvement of donors in Benin.

At the time of the Second Review, it was expected that the new government would strengthen the implementation of structural reforms, especially taking into account the favorable conditions after the Multilateral Debt Relief Initiative. However, progress with regard to implementing structural reforms has been very slow and we wonder why it has been so. Do the authorities face severe capacity constraints

or do they lack the political will or has there been a change in their approach to reforms?

During the WAEMU Board discussion on May 28, 2008, Directors agreed that regional monetary and economic cooperation had played a positive role in improving the macroeconomic environment in the member countries of WAEMU. Also, on that occasion, Directors suggested a closer coordination of fiscal policies of member countries to address the weakening global environment and rising commodity and food prices. Given that Benin is the only WAEMU member meeting the convergence criterion on fiscal balance and the fiscal policy remains the main domestic macroeconomic instrument, we would be interested in staff's view on additional fiscal measures needed. In addition, the ongoing negotiation on economic partnership agreements with Europe provides a good opportunity to harmonize the tax system within the WAEMU. Could the staff provide some insights as to what this would mean for Benin and the region?

Like last year, we once again urge the authorities to implement the civil service pension fund reform which is essential for securing Benin's fiscal sustainability over the medium term. We also note the staff's conclusion in the selected issues paper that in order to safeguard the medium-term external sustainability the current account deficit of 6 percent of GDP should be reduced to the corresponding sustainable level of 4 percent. This would require the real exchange rate to depreciate by around 10 percent. Given the absence of an exchange rate policy in Benin, this can be achieved indirectly by enhancing the productivity and flexibility of the economy which could help in keeping inflation relatively lower than in other countries of the union. Therefore, once again, we urge the authorities to press ahead with structural reforms which will ultimately advance the supply side of the economy and the credibility of the authorities' economic program.

Mrs. Sucharitakul and Ms. Matoto submitted the following statement:

We thank the staff for their concise set of papers and Mr. Rutayisire for his informative buff statement.

During the Board meeting on the third review in January, we characterized Benin's main challenge as one of moving forward on structural reform, in view of the impressive gains in establishing

macroeconomic stability. Unfortunately, it would appear that external shocks could divert the authorities' focus back to issues of stability, most notably on inflation, fiscal sustainability and the external deficit. In such difficult circumstances, the Beninese authorities should be commended for their unwavering focus on sustaining macroeconomic performance. While welcoming the rebound in growth in 2007, and the projected acceleration this year, the pace of expansion is not likely to significantly reduce poverty. We fully appreciate the authorities' focus on immediate term issues, but we urge them to remain steadfast in their medium-term structural reforms as they are critical to achieving the sufficiency and stability that is needed to safeguard against external shocks, and in achieving the MDGs.

We welcome the authorities' commitment to implement the PRGF-supported program and the improvements made. Given the overall satisfactory macroeconomic performance, with all but two targets met, we support the completion of the fourth review and the request for waivers. On the request for augmentation of the PRGF, we agree that implementation of the program has been satisfactory, and that there could be potential balance of payments and fiscal needs that the additional funds could help offset. Having said that, there is a judgment that needs to be made on whether an actual funding need is likely or whether a more precautionary arrangement is called for, which may be the case for countries that have managed to sustain prudent fiscal positions and comfortable reserves levels. There could be a case for judging that Benin's needs fall under the latter, though we agree that there are significant risks should the former scenario come to pass. Therefore, we can go along with agreeing to the authorities' request. More generally, we think it would be prudent on the part of the Fund to provide a full toolkit of instruments—including contingent financing on concessionary terms to PRGF-eligible countries—that will be needed in dealing with the current food and fuel price crisis. A contingent financing arrangement would also exert less pressure on the authorities' debt servicing obligations than a front-loaded disbursement, even if on concessional terms. In this connection, we would appreciate an elaboration from PDR on whether it would be possible to provide a contingent line of credit under the PRGF umbrella. If not, would the envisaged work program on modifying the ESF consider this need?

The rest of our comments mainly follow up on the queries we raised at the last review. We remain concerned that expenditure management is still not as efficient as it could be, leading to the authorities depositing proceeds from the regional bond sales with local commercial banks. We understood at the time of the last review that this was seen as the more prudent move, given the higher interest rates offered by the local commercial banks compared to the BCEAO. At that time, it was envisaged that these funds would be placed temporarily with these institutions and would be drawn down as the infrastructure projects took off. We now note that government deposits have risen. Staff elaboration on the status of the infrastructure projects would be appreciated. We are also concerned that this large increase in base money has the potential to complicate monetary management and would appreciate staff's assessment in this regard.

The second key issue remains the slow progress in reforming the parastatals, especially SONAPRA. We note that cotton production and export growth are projected to remain below potential due to this slow progress. At the time of the third review, there was considerable discussion on the need to go back to the drawing board on this issue, and that the World Bank's engagement in helping the authorities design an appropriate privatization program had fallen through. While welcoming the authorities' new timetable in this area, we are concerned that the World Bank is not involved in the current efforts. We would appreciate hearing from staff of the Bank on whether any discussions are taking place with the Beninese authorities, and the Bank's assessment of the authorities' work program. On the other hand, we are pleased to note that the authorities are continuing to implement measures to enhance the competitiveness of the Port of Cotonou. The authorities' intention to set up a one-stop shop at the port is encouraged in order to improve customs effectiveness in mobilizing revenue and facilitating trade. We agree with staff that the authorities should accelerate the restructuring of the telecommunication and electricity companies to improve service quality and reliability, and to enhance competitiveness. Given Benin's narrow economic base and its vulnerability to external shocks, we support reforms to strengthen the judicial and land tenure to support private sector development and allow for diversification of the production and export base.

With these remarks, we wish the authorities continued success in their endeavors.

Mr. Ge and Mr. Yung submitted the following statement:

We support completion of the fourth review of the PRGF arrangement for Benin. According to staff's assessment, Benin observed all quantitative performance criteria in 2007 and its economic performance has been broadly satisfactory. We commend the authorities' efforts to improve revenue collection, control public spending, and address infrastructure problems and projects conducive to Benin's medium- to long-term macroeconomic stability. We are also reassured by Mr. Rutayisire's helpful buff statement that the authorities remain committed to the reforms laid out in the ongoing PRGF arrangement.

We approve the authorities' request for augmentation of the access under the PRGF arrangement. We agree with staff that the proposed increase in the access can be justified by Benin's excellent debt servicing record and its relatively low indebtedness to the Fund. Furthermore, with the shock of rising food and energy prices, there is a genuine need for Benin to actively seek additional resources to meet financing pressures.

We share staff's concern on the destabilizing effects the spike in food and energy prices is having on Benin's fiscal and external current account positions. While the authorities were quick to cut taxes and provide subsidies to help bring food and energy prices down and relieve some social pressures, the measures are likely to pose risks to fiscal targets. In addition, prolonged tax cuts and subsidy measures may distort the markets of affected products and have limited reach to the poor. In this regard, we join staff in encouraging the authorities to replace these short-term safeguards with more targeted long-term support measures and to expedite discussions with the donor community to help ease the financing pressures.

We welcome the authorities' renewed commitment to move forward with structural reforms to enhance the competitiveness of the Beninese economy and reduce poverty. It is particularly crucial that the authorities continue to address structural weaknesses in the port, cotton, and public utilities sectors that are key to economic growth. We also encourage them to seek opportunities to diversify the economy and prepare a relevant strategy to maintain growth sustainability. Staff comments are welcome.

Two structural benchmarks—an audit of public finance information systems and a draft strategy for reforming the civil pension fund—were missed. Staff contends that the authorities are taking appropriate steps to complete these measures before end-2008. It is important that these structural benchmarks are met since they are indicators of the progress in fiscal consolidation. In pursuing fiscal consolidation further, we note that a review of the country's tax structure will soon be carried out by the Fund's technical assistance mission.

We wish the authorities continued success in the smooth implementation of the program.

Mr. Murray and Mr. Na submitted the following statement:

We thank staff for a well-focused report, and Mr. Rutayisire for his helpful buff statement.

We note that the conditions for completing the fourth PRGF review have generally been met, as reflected in measurable improvements in public finances and in the rebound in growth despite a difficult international environment. We also note that the authorities are taking steps to ensure finalization by the end of 2008 of two missed structural benchmarks that were not observed due to difficulties in mobilizing the necessary donor support. In light of this, we support the completion of the fourth review of the PRGF arrangement.

In relation to the request for augmentation of Fund resources amounting to 15 percent of quota, we agree with staff that Benin's capacity to repay the Fund is sound, considering the authorities' current indebtedness to the Fund and its excellent debt servicing record. Furthermore, as price hikes in oil and energy could seriously dampen external current accounts, with the import bills projected to increase by 2.3 percent of GDP, we also support the authorities' request for the augmentation.

In a broader sense, given the significance of the global price hikes at this juncture, and as the effects from food and fuel prices widen, we also call for the Board to discuss the implementation of augmentation under the PRGF some time soon.

With these remarks, we wish the authorities all the success in their future endeavors.

Mr. Charleton and Mrs. Alvarez submitted the following statement:

We thank the staff for its comprehensive report and Mr. Rutayisire for his helpful buff. The modest revival in growth and low inflation levels that have characterized economic activity in Benin over the last two years follow implementation of prudent fiscal policies. We welcome the authorities' commitment to build on this record by maintaining the current strict fiscal stance and stepping-up implementation of the reform agenda to improve the business climate and stimulate growth. We support completion of the fourth review of the Poverty Reduction and Growth Facility (PRGF) as all quantitative benchmarks for end-September and performance criterion for end-December 2007 have been met.

The current risks from high and rising food and oil prices will test the authorities' resolve to maintain sound macroeconomic policies. Their concerns about the impact of these rising prices on real domestic incomes and the projected weakening in the current account are valid especially in a small low income country like Benin. This Chair has expressed general concern that countries like Benin, which has received debt relief, could find themselves borrowing to meet food and oil payments, and that this could start a new process of increasing debt. Indeed, there is a strong onus on donor countries to step-up their aid in the current circumstances. However, if we are to be relevant to our members we need to be responsive to the needs of the members as they perceive them. We understand why Benin is seeking assistance from the IMF by requesting augmentation of access under the PRGF. The staff has carefully analyzed the situation, and we are willing to accept the authorities' request.

Regarding the tax cuts and subsidies that the authorities have introduced to deal with the food and oil shocks, like the staff, we consider them to be inefficient and very likely to undermine achievement of the fiscal targets. We support more targeted and cost efficient support to the most vulnerable groups, and encourage the authorities to seek TA to move in this direction urgently rather than in the medium term. Other supportive policies over the longer term like enhancing price flexibility, boosting activity in export agriculture, and raising local food production should help to increase food security.

Over the medium term, the authorities will have to accelerate implementation of their reform agenda to build resilience to exogenous shocks and enhance competitiveness. Progress in reducing economic vulnerabilities under the program has been disappointing, which if not addressed urgently, will compromise the authorities' objective of rapidly reducing poverty and achieving the MDGs. The authorities' renewal of their commitment to structural reforms is therefore welcome, and we urge them to address the continuing delays in the reform of the cotton, port and public utilities sectors. They also need to strengthen the judicial and land tenure systems and facilitate access to credit for more small and medium-sized enterprises.

With these brief comments, we wish the authorities success in their future endeavors.

Mr. Alazzaz submitted the following statement:

I thank the staff for a well-written set of papers and Mr. Rutayisire for his helpful buff statement. Benin's macroeconomic performance continued to improve last year under the PRGF-supported program, with growth increasing and inflation declining. However, a further pickup in growth is essential to significantly reduce poverty and make more rapid progress toward the MDGs. To this end, it is important to accelerate structural reforms to enhance competitiveness. In addition, as the staff notes, Benin will need to weather in the short term the strains, including on the balance of payments, of rapid commodity price inflation. In this regard, I support the authorities' request for an augmentation of access under the PRGF arrangement.

On the fiscal front, I welcome the overperformance in 2007, reflecting both improved revenue mobilization and better control over spending. Indeed, it is encouraging to note that in 2007 Benin became the only WAEMU member country meeting the convergence criterion on the basic fiscal balance. I am also reassured by the ongoing efforts to sustain improvements in the revenue ratio, including through strengthening tax and customs administration and rationalizing the tax system. This should help create fiscal space for increased pro-growth and pro-poor spending. On the expenditure side, I welcome the cautious approach of the authorities, given Benin's limited absorptive capacity. To this end, it is important to strengthen capacity in public investment planning and project evaluation. I am also encouraged by

the authorities' intention to consolidate recent gains in debt sustainability.

To enhance growth performance further, it is important to remove structural obstacles, including infrastructure gaps, a weak business environment, and an underdeveloped financial sector. Indeed, while Benin is one of the most competitive countries in the WAEMU, its low ranking in the World Bank's 2008 Doing Business Indicators and in the World Economic Forum's 2008 Global Competitiveness Index underscores the need for additional efforts. In this connection, as the staff notes, reforms to strengthen the judicial and land tenure systems and facilitate further access to credit for small- and medium-sized enterprises would support private sector development and allow for diversification of the production and export base. Given the importance of cotton sector, I look forward to the finalization of the new reform strategy. Reforming the parastatals is also important to strengthen competitiveness.

With these remarks, I support the proposed decision and wish the authorities further success.

Mr. Fayolle submitted the following statement:

We thank staff for the very interesting set of reports and Mr. Rutayisire for his helpful and informative buff statement.

Given the overall performance under the program, we support the completion of the fourth review of the PRGF arrangement. We take note that macroeconomic performances in 2007 were broadly satisfactory and that fiscal performances exceeded expectations. All quantitative benchmarks for end-September and performance criteria for end-December 2007 were observed by large margins. The authorities deserve credit for these results.

In light of the projected deterioration of the terms of trade and the impact of higher food and oil prices on the external current account balance, we also support the authorities' request for an augmentation of the access level under the arrangement. We believe that the size of the proposed augmentation of access, although limited, will be helpful in mitigating the impact of price shocks. As Mr. Charleton and Mrs. Alvarez, we also believe that it is important for the Fund to be responsive to the needs of the members as they perceive them.

Moreover, we note that Benin's capacity to repay the Fund remains sound. When we look at the figures (15 percent of quota is equivalent to 0.3 percent of 2007 GDP), this is not so much an issue in terms of debt sustainability.

We broadly agree with the staff's appraisal, and consequently we would like to limit our comments to the following issues.

We take note that the medium-term economic prospect, although remaining broadly favourable, is heavily dependent on performances in the port and cotton sectors. In this regard, Mr. Rutayisire reassures us in his statement that the authorities remain committed to sustaining the momentum of economic reforms. We are pleased that a "port expert" will be operational at the end of this month and that the authorities are finalizing the cotton sector strategy. However, we believe that a thorough dialogue among all the actors of the cotton sector would be useful before adopting the strategy.

We are encouraged by the authorities' determination to further accelerate restructuring of the electricity and telecommunications companies. Improving the quality of utility services is vital to enhance Benin's economic competitiveness and potential. Efforts should also be made to address weaknesses in the banking system, as pointed out by the Banking Commission.

Improving public expenditure management is crucial so as to ensure the best use of available resources. In this regard, we are reassured by the authorities' intention to modernize public expenditure management systems and enhance budget management. We also encourage the authorities to pursue actions aimed at addressing capacity constraints that have prevented the implementation of the public investment program.

As Mr. Bakker and Mr. Galac, we would like to point out that the staff report's reference to the "misalignment", regarding a member of a currency union, is not in accordance with PDR's guidance. We would also like to caution staff, once again, on the use of doing business indicators in the staff report. We recall that such aggregated and perception-based indicators are highly sensitive and subject to significant technical uncertainties, as evidenced by recent discussions at the World Bank Board.

Finally, the authorities' affirmation of their strong commitment to pursue a prudent debt policy in order to ensure the preservation of external debt sustainability is welcome.

Mr. Daïri and Mr. Kwakye submitted the following statement:

Supported by prudent policies and debt relief, Benin has experienced rising growth and low inflation in recent years. Implementation of the current PRGF-supported program has been strong. Structural weaknesses, however, persist, leaving the economy vulnerable to shocks. Recent developments in the global economy, particularly surging food and fuel prices, pose further risks to the outlook. Reinvigoration of reforms to bolster the economy's resilience, strengthen institutional and absorptive capacity, and improve the business environment is critical to accelerating growth to achieve substantial reduction of poverty. Staff rightly point to the importance of rallying domestic support for reform, especially in light of the unfavorable external environment.

As Mr. Rutayisire underscores in his insightful statement, fiscal policy has been prudent and has achieved remarkable results, underpinned by strong revenue-mobilization efforts and effective control of current spending. Implementation of the development and social budgets has, however, been slowed by capacity constraints. The fiscal program duly targets primary surpluses that accommodate a gradual increase in pro-growth spending and are consistent with long-term sustainability. An ambitious revenue mobilization strategy is envisaged as a key component of the program based on increasing efficiency of customs and tax administration, rationalizing the tax structure, and making the tax system more competitive. Expenditure management is also being reinforced, including through strengthening of control and reprioritization. While pressures on public sector wages continue to mount, they are confined mainly in the key sectors of education, health, agriculture, and revenue agencies. Mr. Rutayisire reaffirms the authorities' commitment to maintaining the wage bill at levels consistent with the program ceilings, as well as improving payroll systems and reforming the pension system. As intended, absorptive capacity would be expanded to increase the rate of execution of pro-growth expenditure programs. The World Bank's assistance in this task as well as in the use of PPPs in infrastructure projects will be helpful.

After falling markedly in 2007 with the help of improved local food supply, inflation has risen recently owing to higher world food and fuel prices. A tight monetary policy would help counter any second-round effects. The authorities' recent decision to keep the reserve ratio at 15 percent would seem appropriate, although they note a possible winding down, as conditions permit, from what is obviously a high level. The exchange rate peg has served the economy well as a policy anchor and a source of confidence. Staff's comprehensive analysis on external sustainability and competitiveness in the Selected Issues paper does not indicate any substantial misalignment of the exchange rate. Sustained CFA appreciation could, however, be damaging, especially in light of below-potential export growth and high dependence on donor resources to finance the current account deficit, which is slightly above what staff consider to be the sustainability threshold. The clear message is to reinforce structural reforms to bolster competitiveness. The authorities acknowledge weaknesses in the banking sector, including low capitalization, high level of nonperforming loans, and high credit concentration. We welcome measures being taken to address these weaknesses, including adjustment of capital requirements and enhancement of the supervisory authority of the regional Banking Commission. As recognized, improvements are also needed in corporate governance, information systems, and risk management. The recent WAEMU FSAP should guide actions in these areas.

Structural reforms should be reinvigorated to boost the economy's efficiency and flexibility and improve conditions for private investment. Although quite competitive within WAEMU, Benin still has a lot of ground to make up in global competitiveness rankings. In general, it needs to improve the legal and judicial system for protection of property rights and enforcement of contracts, ease the business regulatory burden, improve infrastructure, and reduce business taxation. It also needs to build institutional and technical capacity to support the business sector. As assured by Mr. Rutayisire, the authorities are expected to push ahead reforms in the sectors of cotton, port, and utilities to enhance the business environment and reinvigorate growth. To mitigate the effects of the global food crisis, the authorities introduced temporary tax cuts and limited price controls. They recognize that the long-term solution lies in increased food production, which can be achieved through provision of appropriate incentives and, as mentioned by Mr. Rutayisire, concerted

regional efforts. We urge the development community to support this effort, in addition to backing more targeted measures.

The medium-term outlook seems favorable, with rising growth and low inflation. The external debt burden has been substantially reduced by the HIPC-Initiative and MDRI relief, and the risk of debt distress is moderate. Debt and fiscal sustainability is, however, susceptible to shocks, highlighting the importance of implementing appropriate reforms, maintaining a strong fiscal effort, and following a prudent debt policy. The heavy borrowing from the regional financial market to accumulate funds in the banking system raises concerns, given the high interest rates and the risks from maturity mismatch. Expanding capacity to accelerate use of investment funds would ease this anomaly.

Notwithstanding capacity constraints and external pressures, the authorities have remained steadfast in implementation of their program. Recognizing lags in the reform agenda, they have reaffirmed their commitment to its acceleration. We, therefore, support completion of the fourth review of the PRGF arrangement and augmentation of access to help the authorities deal with rising food and fuel prices. We also support Mr. Rutayisire's call for maximum support from the development community for their efforts.

Mr. von Stenglin and Mr. Haupt submitted the following statement:

We thank the staff for a comprehensive set of papers and Mr. Rutayisire for his informative buff statement. Benin's recent experience of price stability and a modest pick-up in economic activity is facing new headwinds through a deterioration in terms of trade. Looking ahead, structural reforms and an improvement in the business environment will be critical if Benin is to achieve higher economic growth and reverse the trend of increasing poverty rates.

Fourth PRGF Review

We can support the completion of the fourth review of the PRGF arrangement, given the satisfactory performance on the macroeconomic front, reflected in the observance of all quantitative benchmarks and performance criteria.

It is, however, regrettable that only two of four structural benchmarks for the second half of 2007 were implemented. As a result, three of four structural benchmarks for the second half of this year constitute actions that should really have been taken in 2007. For the remainder of the PRGF-supported program, we urge the authorities to intensify their efforts in the structural area and to implement agreed measures in a timely manner. We also invite the staff to explain why it was decided to do completely without structural performance criteria, i.e. measures that are considered to be necessary for keeping the program on track.

On a specific point, we are concerned that in the important but non-core area of the cotton sector, the authorities still have not secured World Bank technical assistance. Ownership of the program in our view calls for the authorities' willingness to seek the expertise that is necessary for implementing agreed structural benchmarks.

Request for Augmentation of Access

We note with concern that this is another request for PRGF resources without a clear balance of payments need. Our surprise also comes from the fact that, as we recall, Benin was not on the list—provided by the First Deputy Managing Director during end-April's briefing on the impact of high food and energy prices—of twelve sub-Saharan countries discussing a possible request for Fund financial support with the staff. Benin's overall balance of payments is expected to remain positive in 2008. To be sure, the current account balance is projected to deteriorate somewhat. However, the level of gross international reserves remains broadly stable, and compared to the end-2007 forecast, the projected level has even increased, also in terms of import coverage. Furthermore, it is important to note that the reserve level itself must be regarded as highly comfortable amounting to about fourteen months of imports.

This suggests that the augmentation of access is requested essentially to finance the tax cuts and subsidies introduced to countervail higher food and energy prices. We fully agree that many countries adversely affected by higher food and energy prices need appropriate support of the international community to help them address this difficult challenge. However, to the extent that budget support is needed, this is not so much the task of the Fund as that of donors and bilateral and multilateral development partners who should

provide assistance on more concessional terms, preferably as grants. For one thing, the Fund is not a development agency, as also noted by the Managing Director in the context of Strategic Directions in the Medium-Term Budget. Secondly, Benin is considered by the staff to be in moderate debt distress and would breach the NPV of debt-to-export threshold in some of the less adverse scenarios.

On a more general note, we reiterate our call on staff, in the context of the upcoming review of lending facilities, to analyze the concept of balance of payments need with a view to finding a clearer and more operational definition. On that occasion, special attention should also be paid to the role the concept takes on in currency unions such as WAEMU.

Finally, our concerns are also related to Benin's track record of structural reforms over the last couple of years. We are struck by the staff's disappointment with the slow progress of reforms, as candidly expressed in the report. With these reservations we are nonetheless willing to consent to the proposed augmentation, given that the overall program is broadly on track and that we have supported previous PRGF requests in response to higher food and energy prices, notwithstanding similar concerns.

Article IV Consultation

We congratulate Benin on being the only WAEMU member country meeting all first-order convergence criteria including that on the basic fiscal balance. We strongly encourage the authorities to maintain their prudent fiscal stance going forward. This also implies taking a continued cautious approach to spending growth until absorptive capacity constraints have been addressed. On the stance in 2008, we note that the primary fiscal surplus (without one-off receipts from cellular phone licenses) is expected to decline by 2½ percentage points of GDP, whereas the food- and oil-price related tax cuts and subsidies are estimated to amount to 1 percent of GDP. Could the staff elaborate on what factors account for the residual weakening of the primary balance by 1½ percent of GDP?

With regard to the new tax cuts and subsidies, we fully concur that these are likely to be an inefficient and costly way of limiting the impact of rising food and energy prices on the poor. Furthermore, there is a high chance that the price increases will at least partially

persist, making structural adjustments inevitable. We therefore strongly support the authorities' intention to phase out the measures and replace them with more targeted ones, as needed. Furthermore, we encourage the authorities to press ahead with improvements in public payroll systems and wage management to allow for an elimination of the wage ceiling under the program.

The unfavorable evolution of cost competitiveness, the deteriorating business environment, and limited absorptive capacity underscore the need for structural reforms. We urge the authorities to follow up on their previous announcements and accelerate the reform agenda. We are encouraged by the commitment expressed in Mr. Rutayisire's statement in this context. Pressing tasks include, in particular, the preparation of the new cotton sector strategy and actions to make up for the delays in reforming parastatals. Other areas in need of reform include the judicial and land tenure systems, and access to credit for small- and medium-sized enterprises.

We take note of the weaknesses in banking sector indicators, including maturity mismatches and high concentrations of credit and non-performing loans. Moreover, the number of banks in compliance with prudential indicators appears to be on a declining trend. These issues bear close monitoring, and we welcome that the authorities intend to address the situation.

Finally, like Mr. Fayolle and Messrs. Bakker and Galac, we would like to point out that the use of the term "significant misalignment of Benin's current account balance or real exchange rate" in the staff report is not in accordance with relevant PDR guidance in the context of members of currency unions.

Mr. Henriksson and Mr. Bartkus submitted the following statement:

We thank staff for their analysis, and Mr. Rutayisire for his informative buff. We note that although the Beninese economy has experienced a pickup in real GDP growth and low inflation during the last two years, the economic situation continues to be vulnerable and subject to external shocks. We concur with staff's view that the economic recovery in Benin remains below what is required for rapid poverty alleviation. Significant progress in implementing structural reforms is needed to unlock growth potential and to address competitiveness.

However, we regret that progress in implementing structural reforms has been disappointing so far. Even though Benin now faces less favorable external conditions and high food and energy prices, we encourage the authorities to overcome these constraints and to decide on growth enhancing reforms as soon as possible.

On the fiscal front, we consider the policy measures set in the fiscal policy outline broadly appropriate. We commend the authorities' commitment to prudent fiscal discipline, especially the progress made in improving revenue mobilization and governance in the revenue agencies, and take note of the rapid fiscal consolidation in 2007. However, it is essential to further improve public expenditure management, especially as regards capital expenditures.

While performance under the PRGF arrangement so far has been mixed, we agree that the program implementation is broadly on track, as all quantitative benchmarks and performance criteria set for end-September and end-December 2007 were observed. At the same time, we regret that the auditing of the public finance information management systems and the draft strategy for reforming the civil service pension fund were further postponed. However, we take note that the authorities have taken steps to address these structural benchmarks, and we expect them to be observed by the end of this year. Therefore, we support the completion of the fourth PRGF review.

We acknowledge the challenges faced by the Beninese authorities in dealing with high food and oil prices, and urge the authorities to rapidly develop and implement a targeted cost efficient policy to protect the most vulnerable groups. A prolonged continuation of the current tax cuts and subsidies policy poses risks for fiscal sustainability. As regards the authorities' request for an augmentation of access to deal with rising food and oil prices, we take note of the authorities' efforts to preserve prudent fiscal discipline and thereby avoiding a re-accumulation of unsustainable debt. Therefore, we agree with the request for augmentation of access under the PRGF. We ask staff to comment whether other measures could be applicable within a framework of sound macroeconomic policies in the face of high food and oil prices.

With these remarks, we wish the authorities success in their challenging endeavors.

Mr. Yamaoka and Mr. Imamura submitted the following statement:

We thank the staff for their comprehensive report and Mr. Rutayisire for his informative statement.

We welcome the recent recovery of Benin's economic performance. We note that the major challenges for the country are to: mitigate the impact of worldwide inflationary pressures, and facilitate structural reforms, particularly in the cotton sector. We concur with the staff that the performance under the PRGF-supported program is broadly satisfactory and, therefore, we support the completion of the fourth review.

However, from the perspective of a donor to the PRGF-ESF Trust desiring an effective use of scarce trust resources, we are yet to be convinced of the relevance of granting the requested augmentation of access. Staff pointed out that the rationale for the augmentation is to address the widening current account deficit and the remaining fiscal gap. Nonetheless, in this regard, we would like to express the following concerns:

Even though an unfilled fiscal gap may eventually translate to the balance of payments, the country's official reserves have already accumulated to cover 15 months of imports. Government deposits also amount to 5.1 percent of GDP. Furthermore, since Benin is a WAEMU member country, the burden of defending its currency is substantially reduced. (Otherwise, the benefits of participating in a currency union would be limited.) In this regard, we welcome the staff's further clarification of the rationale behind the necessity of the augmentation.

Since most price development basically reflects the balance of supply-demand, in order to stabilize and reduce commodity prices it is necessary to strengthen the supply side of commodities (e.g., local food production). On the other hand, although we understand the need to protect the poorest people, income transfers to the demand side (such as subsidies and temporary tax-cuts to reduce food prices) may distort price mechanisms that promote the necessary adjustment of supply-demand balances, thereby prolonging the commodity price hike while deteriorating fiscal balances. In this regard, granting the augmentation to address the fiscal gap caused by such subsidization cannot decisively resolve the current problems, and might bring about the risk of becoming unable to escape the "vicious-circle" of

continuous inflationary pressures and subsidization. We would welcome the staff's assessment regarding this issue, especially with respect to the time-horizon of the augmentation.

Needless to say, the increase in commodity prices also increases the income transfers from commodity importers to commodity exporters. Thus, the effects of the increase in commodity prices should be assessed in a comprehensive manner, taking into account not only the effects of food price increases but also those of other commodity price developments. Moreover, each country should be responsible for improving its own infrastructure regarding commodity production and exports, such as taking steps to improve the business environment, judicial systems and ports. In this regard, the Fund should continue to carefully examine members' requests for augmentation of access in order to avoid distorting its message of encouraging maximum self efforts by member countries.

With these remarks, we wish the authorities success in their future endeavors.

Mr. Larsen and Mr. Pillai submitted the following statement:

We thank staff and Mr. Rutayisire for the helpful information and analysis they have provided for today's meeting. We broadly concur with staff assessment and make the following points for emphasis.

We welcome the overall progress being made by Benin through the PRGF, and support the completion of the fourth PRGF review, noting the measures that have been taken to address the two structural benchmarks that were missed. While overall growth and revenue performance has been good, there remains an unfinished agenda on structural reforms. We believe staff have set out a clear case for the urgency of reforms in the cotton, port and public utilities sectors. Going forward addressing these structural reforms along with using the increased fiscal space for quality development spending should be important priorities in addressing the poverty challenge.

Like other countries in the region rising food and oil prices pose risks to the fiscal situation and the external position. We concur with staff recommendation on an augmentation of PRGF resources for Benin. We believe it is entirely appropriate for the Fund to be

responsive to short-term reversals from exogenous shocks. And Benin remains in a sound position to repay the Fund—during the remainder of the program period the annual average debt service to the Fund would only be 0.04 percent of government revenue. In terms of medium-term measures we encourage the authorities to develop appropriate actions in the agriculture and infrastructure sectors, which would be important in securing future benefits from growth and poverty reduction efforts.

Mr. Guzmán and Mr. Umaña submitted the following statement:

Macroeconomic performance in 2007 has been broadly satisfactory and has continued to improve. Growth has picked up to 4.6 percent, rising above the WAEMU average for the first time in the last 5 years. The fiscal position has also strengthened considerably. Fiscal performance was much better than expected, 2 percentage points above the target, but public investment has lagged, which seems to point to execution capacity problems. Unfortunately structural reforms have also lagged and are moving at a very slow pace, in particular plans to reform the cotton and utilities sectors.

Inflation has been low but has picked up due to the food price increases and is likely to continue this trend. The impact of higher energy prices also poses a significant threat since there is a gap in electricity demand and supply. Tax revenues nearly reached the WAEMU target of 17 percent of GDP and Benin has also benefited from a one-off non-tax receipt of 2.3 percent of GDP from cell phone licenses. The rate of execution of domestically-funded investment outlays rose to 68 percent in 2007 from 57 percent the year before.

Although the authorities have been able to open fiscal space for pro-poor spending, capacity problems have limited the translation of higher fiscal space into more development spending.

The government's capacity to target cost efficient support to the most vulnerable is a real problem. Improvements in public expenditure management are critical, in particular with respect to capital spending.

Unfortunately, structural weaknesses in the economy have not been addressed, and only two of four structural benchmarks for the second half of 2007 were implemented, one with a delay. Private investment is low and the business environment could be improved considerably. Reforms in the cotton and utilities sectors must be continued. Other key measures to enhance competitiveness should be undertaken, including a road rehabilitation program, a strategy to diversify the economy, and reform of land tenure and judicial systems. We encourage the authorities to accelerate the pace of structural reform.

But overall performance under the program has been satisfactory, quantitative benchmarks for end-September and performance criteria for end-December were met by large margins. Therefore we agree with staff that the conditions for completing this fourth review have been met. We support the staff's recommendation to complete the review.

Based on the effect of food and oil price increases on the Balance of Payments, authorities have requested an augmentation of access to Fund resources by 15 percent of quota. We share the concern expressed by authorities on the impact of deteriorating external environment but we must reiterate our call on staff to provide us with a clear and solid foundation to the use of PRGF in the current circumstances;

- We, like others, fail to see the BoP need. The external account deficit widened because of terms-of-trade deterioration and real-currency appreciation, however large inflows of official capital grants contributed to a sizable surplus in the balance of payments, also keeping official reserves at very high levels.
- We would also like to have a statement by the authorities and staff of having studied all the alternative options to increasing debt.

Our general view is that the PRGF has a focus on macro stability and poverty reduction in the context of a comprehensive growth-oriented strategy, which is, by its own nature, a longer-term issue. Hence, the PRGF is not the appropriate instrument to achieve short-term, temporary goals. The Fund created the ESF specifically for this type of event. While in the past the PRGF has occasionally been

used as a means of providing some exceptional emergency assistance, we do not believe that this is the way to go when we know that the global food crisis is generalized to a number of countries at the same time. Therefore, just like the World Bank has recently developed a new \$1.2 billion rapid-financing facility to address immediate needs, including \$200 million in grants targeted at the vulnerable in the world's poorest countries, I think we should concentrate on a fast reform of the ESF instead of picking the easy way forward.

The case of Benin highlights not only a degree of confusion in the way we use our toolkit—due perhaps to the urgency to respond to this essentially humanitarian crisis—but also a degree of inconsistency in our advice. In a recent informal session FAD presented us with a template that listed the possible policy reactions to the food price hikes, their advantages and disadvantages. But when we address the case of Benin we must be aware that the advisable “targeted and temporary” measures are by and large forgotten, and the IMF basically goes on to finance via PRGF a fiscal need generated by the suppression of certain food import tariffs. We hope the reinstatement of those fiscal resources will come as soon as possible.

Finally, we consider that the Fund gets into uncharted territory in terms of the reputational risk we run by using PRGF resources to address what we consider is a humanitarian crisis. We are certainly disincentivating grants from other donors (15-month reserves), making other multilaterals job more difficult or rendering them mission-less. And while succeeding in becoming relevant and helping limit the damage of price increases in these countries, we are also linking humanitarian aid to the whole conditionality attached to PRGF agreements (i.e., cotton and utilities reform in Benin).

We await the explanations by staff and authorities and we will approve this request if the Board reaches a majority in favor.

Ms. Agudelo and Mr. Maciá submitted the following statement:

We thank staff for the illustrative report and Mr. Rutayisire for his insightful buff statement. We support the completion of the forth review of the PRGF program and the augmentation of access.

We are pleased with Benin's continued economic growth supported by a surge in port and commerce activities, favorable cotton exports and a good food harvest. This latter helped maintain inflation at low levels in 2007 though the spiral in global prices prompted the authorities to take fast fiscal measures at end-2007. Higher food and oil prices also made a negative impact on the current account deficit though the flow of official capital grants has strengthened reserves further.

We acknowledge Benin's continued good performance under the program. We also note the strengthened macroeconomic stability and a healthy fiscal position, but we urge the authorities to keep prudent spending to meet fiscal targets. A sound debt management must continue with the support of grants and concessional borrowing efforts into the future. However, the most pressing concern on the macroeconomic front is the limited absorptive capacity of the country. Under these circumstances, the call to be prudent on the public expenditure side is even more relevant and spending growth should take care to not crowd out the private sector. In the same vein, the authorities aim to increase pro-poor expenditures and infrastructure projects should be accompanied by a better expenditure management. On the income side, we welcome the introduction of the single taxpayer number (TIN), the customs efficiency study, and the request for Fund's TA assistance to review the country's tax structure. These steps, as detailed in Mr. Rutayisire's buff statement, are deemed crucial to enhance fiscal consolidation goals into the medium term in a still challenging socio-political environment where consensus requires continued perseverance.

To address the issue of increasing potential growth, reducing poverty and addressing long-term competitiveness concerns, structural weakness in the economy have to be addressed. In that sense we are please to note the authorities' commitment to structural reforms in the area of port services, cotton activities and public utilities reforms, among others. However, with respect to this last issue we would like clarification if the reforms consist only on privatization of public companies or if there is a complete strategy to make the sector more efficient and competitive to improve service. Experiences show that changing ownership is not sufficient to achieve this goal. Finally, given the emphasis that staff put in the report on the lack of the advances in the structural agenda, we would like staff comments on

the two pending structural benchmarks in the agenda and their importance under the program.

A new strategy effort for the disengagement of the commercial and industrial activities under the support of the World Bank is welcomed. This demanding reform agenda is deemed crucial for Benin to preserve the competitiveness leverage at hand well into the future

On poverty, we look forward to the 2007 progress report (APR) updating the progress made on the poverty reduction strategy 2007-09 PRSP.

With these comments, we wish authorities well in the demanding reform agenda that lies ahead.

Mr. Lushin and Ms. Shabunina submitted the following statement:

We thank staff for a set of insightful papers and Mr. Rutayisire for his informative buff statement. The authorities should be commended for continuing sound fiscal policy and meeting all quantitative criteria. We are concerned, however, by the slow progress in the implementation of structural reforms with only four out of seven structural benchmarks met. We support the completion of the fourth review under the PRGF and the request for augmentation of access. In this regard, we wish to reiterate our position that it is important to keep the right balance between the speed of providing financing to deal with external shocks and the need for a more ambitious policy response by the authorities.

Fiscal Policy

Like many other countries in the region, Benin is facing additional budget pressures from the current food and oil price rises. Several fiscal measures, including import tax cuts on main food products, were introduced to protect the country's poor. We note staff's assessment of these measures as inefficient to protect the poor and we welcome the authorities' intention to design a better targeted support system. Does staff have some estimates of time and resources needed to create it? Does Benin need additional technical assistance for this and is it available?

We welcome the improvement in revenue collection and low budget deficit levels. At the same time, the share of capital expenditure remains too low at 7.4 percent of GDP. Although it is projected to grow to 8.5 percent of GDP by 2013, it seems unlikely to be enough to reduce poverty significantly in a country like Benin with pressing infrastructure needs. We would like to ask staff whether there is any scope for reprioritizing the budget expenditures.

We commend the authorities for restraining from non-concessional external borrowing. We are concerned, however, with the growing domestic borrowing by the government at high interest rates. Does staff think it poses any danger to economic growth by crowding-out the private investment in the economy?

Exchange Rate and Competitiveness

We note the difference in the estimates of Benin's REER equilibrium level coming from different estimation approaches. Several methods, including the regression analysis of macroeconomic fundamentals indicate that the current REER is in equilibrium. External sustainability analysis, however, shows that real depreciation of 5-12 percent is required to bring the current account balance to a sustainable level in the long term. It is important to know whether the external balance sustainability approach gives the same results for other WAEMU countries suggesting that measures should be taken at the level of the monetary union. Considering that inflation in Benin is lower than the WAEMU average, we wonder what factors are driving Benin's REER appreciation higher than the union average?

Banking System

We are concerned with a very high level of nonperforming loans in the banking sector and a high share of banks noncompliant with the prudential indicators. In this regard, we would especially note a low share of banks satisfying the "loan to bank managers" criteria (Text Table 3, p.22). We encourage the authorities to continue with implementing measures to improve the commercial banks' compliance. Deterioration of the portfolio of microfinance institutions is also worrisome. Taking into account a rather successful experience that microfinance organizations had in other countries, we would like to know the root of the problems for microfinance institutions in Benin.

Structural Reforms

Slow progress in reforming cotton and energy sectors, delays in implementing important structural benchmarks on public finance management and a civil service pension fund are disappointing. Comprehensive competitiveness analysis provided in SIP emphasizes the importance and urgency of structural reforms in Benin. We believe it is crucial that the reasons for these delays are well pronounced in order for the solutions to be found to speed-up the structural reform process. Staff comments are welcome.

With the above remarks, we wish Benin's authorities every success.

Mr. Sadun and Mr. Crispolti submitted the following statement:

We thank staff for the well-written set of papers and Mr. Rutayisire for his candid and insightful buff statement.

Benin's economic performance under the PRGF-supported program has been broadly positive, despite repeated delays in structural reforms. All structural benchmarks for end-September as well as the end-year performance criteria were observed. However, recent surges in fuel and food prices pose new risks to macroeconomic stability calling for well-targeted policy responses from the authorities and continued assistance from the international community, including the IMF. We therefore support the proposed decision while joining other Directors in expressing our disappointment for the limited progress in structural areas.

Since we share the thrust of the staff's appraisal, we limit our comments to two areas:

Fiscal Policy

We welcome the strengthening of Benin's fiscal position during recent years. This progress is a necessary step to stabilize the debt-to-GDP ratio as shown by staff in the last DSA (EBS 07/151 Supplement 1). We understand that recent sharp increases in food and fuel prices require some short-term measures to alleviate the impact on the poor. However, only well-targeted and temporary measures will ensure providing the needed support to the most vulnerable part of

population without severely undermining the recent fiscal stabilization. Moreover, these measures should be replaced by more effective safety nets in the medium term. Against this background, we urge the authorities to remain committed to the fiscal consolidation by achieving the envisaged fiscal objectives for 2008. To this end, recent revenue-enhancing measures need to be complemented with swift actions to reinforce revenue administration and reform the tax system drawing on the Fund's TA. Likewise, more ought to be done to monitor current spending while improving public finance management and project evaluation.

Structural Reforms

We note that the implementation of the authorities' structural reform agenda continues to be disappointingly slow, particularly in the cotton, port, and public utilities sectors. Indeed, repeated delays in key areas are significantly hampering Benin's economic prospects, notably undermining its competitiveness, constraining private sector development, and limiting the diversification of the production and export base. We therefore urge the authorities to show their strong commitment to reforms by forcefully implementing pending measures to remove long-standing bottlenecks in the economy. In this context, we look forward to the adoption of a comprehensive strategy to develop Benin's financial sector, including strengthening the regulatory and supervisory framework and improving access to bank credit for small and medium enterprises.

Mr. von Stenglin made the following statement:

As we stated in our gray, we had to put aside tremendous reservations before we decided to consent to the proposed augmentation. I have a lot of sympathy for Ms. Lundsager's position to abstain from the decision. However, the main reason why we did not abstain is that we have agreed in similar cases to the access or the augmentation to the access, notwithstanding our concerns.

We all agree that it is not the task of the Fund to provide budget support independent of the balance of payments (BOP) situation. But, in the "notional" case of a true BOP need—which we cannot see in the actual Benin case, and besides the fact that for members of currency unions there cannot be any true BOP need—how does staff assess the fact that members of WAEMU do not have—and

probably rightly so—unlimited access to their high level of international reserves? In other words: How do staff define the BOP need in the case of a country that is a member of a currency union? What role does the Fund play and what is the purpose of the comfortably high level of reserves? Can access to the reserves for individual countries be increased?

Finally, regarding the Public Information Notice: I think that the table “Selected Indicators” of the PIN is not consistent with table 2, p31 in the main document. My understanding of table 2 is that the projection of the overall BOP for 2008 has been revised upwards from -0.8 to +0.4. The same is true for the change in the terms of trade. Before being published, the PIN should be corrected.

The Acting Chair (Mr. Portugal) stated that Mr. von Stenglin had raised very important points, which would not necessarily be decided at the current meeting. If there could be no balance of payments need for members of a currency union, that would mean that the Fund could not lend to members of a currency union, including the European countries. It would be a big change in how the Fund proceeded and would also perhaps be a disincentive for the formation of currency unions. The staff would address some of those issues.

Mr. Lanz made the following statement:

This chair can go along with the conclusion of the fourth review and the requested augmentation of access. However, we have reservations with regard to both requests.

First, like Ms. Lundsager and Mr. Kaplan, we are in favor of separating the decision on the conclusion of the review from the decision on the augmentation. This should apply to all augmentation cases, just like in the HIPC Initiative where separate decisions on reaching the completion point and on topping up are presented. There may indeed be cases where program performance warrants the conclusion of a review, but an augmentation of access is not justified.

Second, we are not 100 percent convinced that the request for augmentation is justified for the reasons laid out by Mr. von Stenglin and our Canadian, Japanese, Spanish, and U.S. Directors. We would have liked the staff to elaborate more on the consequences of the deterioration of Benin’s current account given the large continuing capital inflows and comfortable level of gross reserves, which amount

to 15 months of imports. The staff report seems to imply that the laudable debt servicing record could be a motivation for the IMF to increase loans, which are relatively expensive to service. We share the concerns of other Directors that the Fund should not compete with the developing agencies to provide financing to create fiscal breathing space. We wonder how the discussions on the additional financing from other multilateral and bilateral donors cited in the staff report have advanced. The staff's comments would be appreciated.

Third, on program performance, we regret the mixed program implementation with progress achieved only in revenue collection, and the lags in advancing structural reforms. Let me briefly comment on fiscal pressures, the lack of progress in growth enhancing structural reforms, and the appreciation of Benin's real effective exchange rate.

On the fiscal pressures, we encourage the authorities to address these rapidly. The current response to food and oil price increases is costly and poorly targeted. It might also affect domestic food supply as the measures distort markets and lower production incentives. Moreover, it will be very difficult to phase out these measures. Thus, introducing targeted social safety net would be important to safeguard scarce resources while protecting the poor. In this regard, policy emulation among WAEMU countries could be useful. The staff papers for Wednesday's Board discussion on Senegal present a detailed analysis of various short-term and long-term policy responses. In particular, a conditional case transfer system is proposed. We encourage the staff to disseminate this analysis on the regional level. On the expenditure side, we note the ongoing problems with payroll management. In particular, it is curious that the authorities explicitly asked for a wage ceiling to be included as a quantitative target. This could put the Fund in an uncomfortable scapegoat position and we thus see this only as a temporary solution to address the wage problems of Benin's civil sector.

On the structural front, only two of four structural benchmarks were observed and the deadlines to implement the missed end-2007 benchmarks have been reset only to end-December 2008. Given the importance of structural reforms in fostering economic growth in the long run, there is a need to renew reform commitments, in particular with regard to improving public finance management, and liberalizing the cotton sector and public utilities. In this context, we would like to know more about Bank-Fund collaboration. We are a bit puzzled in

this respect by the staff papers which state that the IMF mission worked with parallel World Bank teams but then in paragraphs 24 and 25, assign primary responsibility to the Bank for most structural reform areas. Finally, in the Annex, the staff explains that the Bank and Fund teams are closely coordinating their policy advice to the authorities without delineating who does what. In short, given the importance of structural reforms in Benin, we would like to know if the Bank and Fund are effective in bringing about structural progress in Benin. How can we ensure that the tasks that need to get done in the structural areas get done even when not in our direct expertise?

Finally, with regard to the analysis of real exchange rate developments, we note that Benin is experiencing the sharpest appreciation among all WAEMU members. The selected issues document acknowledges that it may still be useful to examine Benin's individual performance in relation to its peers. But, it does not go further. Like Mr. Lushin and Ms. Shabunina, we are interested in the staff's views on the relatively sharper real exchange rate appreciation in the case of Benin.

The staff representative from the African Department (Mr. Matungulu), in response to questions and comments from Directors, made the following statement:

As we saw in the different papers that were circulated, the questions were essentially in four main areas: the PRGF-supported program, fiscal policy and debt sustainability, monetary and exchange rate policy, and the structural reform agenda. We will try to address these questions in different areas in turn. I am going to leave the questions in relation to the broader Fund policy issues to my colleague, Mr. Plant. I will address those issues that are more specific to the case of Benin.

In particular, in the context of the PRGF-supported program, there was an issue as to how the authorities are addressing the rising food and fuel prices over the medium-term horizon. The authorities view this shock as permanent. Therefore, they believe that the increased donor support is not the proper response over the medium term. They also believe that the tax cuts and subsidies that are currently in place are not adequate responses to the medium-term concerns that they have. For that reason, the authorities have indicated that they will phase out the tax cuts and subsidies beginning in the second half of the year, even though for the time being we do not have

a specific calendar for this step. In addition to phasing out the tax cuts and subsidies, which they feel is important to ensuring that the higher prices are passed through to the consumers to facilitate the economic adjustment, the authorities also are of the view that what is needed is the introduction of targeted social safety nets. The authorities have asked for technical assistance from the donors to try to develop this support system, which is not in place yet. My understanding is that they have approached the World Bank, Germany, and Denmark in this regard.

The authorities also think that looking at this issue over the medium-term horizon it is going to be important to increase support to agriculture. We have been told that the African Development Bank and the IFAD have indicated a readiness to provide financing for agricultural projects. Over the weekend, we also heard that the major donors in the capital city of Cotonou have met on Friday, and have voiced support for the country to help it address the rising food and fuel prices.

There were questions raised in regard to the pending structural benchmarks under the program, which had not been completed by the initial deadlines under the program, in particular those related to the audit of public finance IT systems, the completion of a strategy to improve public finance management, and the preparation of a strategy to reform the civil service pension fund. As we had indicated in the Board papers, the authorities have committed to completing these measures before the end of the year. The staff and the authorities concur that completion and early implementation of the reform strategies for the pension fund and for public expenditure management are going to be critical to enhancing the efficiency of expenditure in the country and to preserving fiscal sustainability over the medium term.

There was also a question on program conditionality in general, with a specific concern that was raised about the fact that the program at the moment does not have any structural performance criteria (PC). As we have seen in the papers that have been circulated, the program does contain macro-critical elements in the structural area we thought are essential to helping improve the overall competitiveness of the economy, improving revenue mobilization and expenditure management, all of which are essential to ensuring continued budget viability over the medium term. In the staff's view, and taking into

account the need to continue having a streamlined overall structural conditionality framework, some of the measures that flow from the strategies that are being prepared could eventually be brought to the level of structural PC going forward. But for the time being, that is not the case. For the most part, we have worked on measures that constitute structural benchmarks.

The second series of questions was in relation to fiscal policy and debt sustainability. A question was raised about revenue prospects going forward. It was noted that part of the strong revenue performance in 2007 was related to the one-time receipts of government revenue from mobile phone companies. We would like to stress the fact that over the last two years, we have seen the government realize major progress in improving revenue performance in general. That was a reflection of the fact that they have been very committed in implementing key revenue management recommendations from various technical assistance missions that have been in the country. As we speak now, there is a tax policy mission that is taking place. If we can go by the level of commitment in the recommendations and the implementation that the authorities have shown in the last couple of years, we are very confident that going forward, the authorities will implement those recommendations, including the new ones that flow from the mission currently in the field. It could be possible not only to maintain the revenue performance of the last couple of years, but also to even do better.

There was a question about the economic partnership agreements with Europe, and how these would eventually impact conditions in Benin. As we have indicated in the papers, unfortunately for the time being, there is no comprehensive assessment at least at the country level of the impact of this agreement on Benin. This is one of the key issues that will be looked at by the authorities with the fiscal policy mission that is now taking place. But the authorities are keenly aware of the fact that as there is more regional integration in the WAEMU and in ECOWAS, and more generally when eventually the partnership agreement with Europe is implemented, there will definitely be a shift in the revenue structure away from customs to internal revenue sources. The authorities are aware that to successfully engage in that direction, they will have to introduce important reforms in revenue management. The authorities are ready to work with the international community, and in particular with us through mostly the Fiscal Affairs Department and West AFRITAC, not only to develop

such reform measures, but to implement them in a way that would ensure that they do not see a weakening of revenue performance going forward.

There was one question on the weakening of the primary balance in 2008, given that the authorities in 2007 had a surplus on the primary balance of about 3 percent of GDP. This year we are looking at that performance declining to about 0.5 percent of GDP. There are several factors that explain this trend. It is important to say that in 2008, contrary to the situation in 2007, the authorities will not have the one-time exceptional receipts from the mobile phone companies which last year represented 2.3 percent of GDP. In addition to that, there is a fiscal cost associated with the rising food and fuel prices. We have indicated in the papers that this amounts to about 1.5 percent of GDP. One element of the fiscal cost of the way the authorities are addressing the rising food and fuel crisis, in addition to the revenue loss that is associated with the tax cuts, are the transfers made to public utilities to help mitigate the impact of the rising food and energy costs.

There was one question on the status of implementation of the infrastructure projects. We have indicated throughout the paper that the authorities are facing severe capacity limitations, which have prevented them from ensuring an adequate implementation of the investment budget. We can report since returning from the field back in March/April that we do see considerable improvement in capacity, which has translated into increasing rates of execution of the investment budget in the last several months. As a result of that, we have also seen government deposits with the banking system decline as the rate of execution of the investment budget increases.

There was also a concern that was raised in the monetary and exchange rate policy area. On the impact of government borrowing from the regional financial market on the effectiveness of monetary policy, we would like to report that the authorities have not engaged in any additional borrowing from the regional financial market since January of 2007. At that time, they realized that due to capacity limitations, they could not use the proceeds of the borrowing as quickly as they had hoped. We had a lengthy discussion with them to the effect that it did not make sense to continue borrowing when there was such a long delay in using the proceeds from the loans. This advice has been well taken by the authorities and we do not consider this to be an important issue at present.

Generally speaking, the view of the staff is that the borrowing from the regional financial market is unlikely to affect the effectiveness of monetary policy in Benin or in the region in general, as monetary policy is conducted at the regional level. Staff expects to see the regional central bank continue monitoring developments in monetary aggregates and adjust its monetary policy instruments in ways that would make it possible to achieve the broader monetary objectives of the region.

With regard specifically to borrowing from the regional financial market, it is important to say that one key feature of the banking system is that they are in a situation of structural excess liquidity. When governments borrow from these banks, this results in a contraction of the excess or reduction of the excess liquidity that is prevalent in that region. In principle, this would tend to facilitate rather than constrain the effectiveness of monetary policy in regulating liquidity in the economy.

With regard to developments in the real effective exchange rate, as most Executive Directors had noted, Benin's appreciation of the real effective exchange rate has been much larger than in most of the other countries in the region. Essentially, this has been due to the fact that with the exception of 2007, inflation in Benin was above the average in the region. It was only in 2007 that they had a relatively better performance on the inflation front. Their hope has been that this good performance on inflation will continue so that we could see an improvement or some stability in the real effective exchange rate going forward.

The last series of questions was in the structural area. There was a question regarding the slow pace of implementation of structural reforms, and the reasons for this performance or lack thereof. Looking at the situation in the country over the last two years, we have essentially identified three main reasons for the slow pace of economic reform, in particular on the structural front in Benin. There has been a wait-and-see attitude on the part of the authorities to some extent in the last year or so, because they were faced with two main election cycles. First, in 2007 they had parliamentary elections, and in 2008 they have had municipal elections. In addition to that, we know that the country has quite limited domestic capacity in undertaking and managing these reforms. To some extent, we have also been told that the less than perfect experience of some of the other countries in the region in the

area of structural reform, and in particular concerning the electricity sector, has not been a good incentive for the country to move forward. In other words, a constituency against reforms has used this as an element to explain the relatively limited adherence of the country to the proposed reforms. By and large, there seems to also be some widespread domestic resistance to reforms. But as the electoral cycle comes to an end, with the completion of municipal elections last March and April, we are convinced the authorities would accelerate the pace of implementation of these structural reforms.

There was a question on the nature of public utility reforms and the content of such reforms. As we had indicated in the papers, for the most part these are reforms aimed at improving the efficiency of these parastatals, with a view to improving overall economic competitiveness in general. In the case of SONAPRA and Benin Telecom, what is envisaged is the opening of the capital so that there is a majority ownership of capital by strategic private sector operators. In some cases, like in the case of the electricity company, it is going to be about essentially putting in place a management contract with a partner of international repute in that area.

Concerning the strategy to diversify the economy, we can report that the authorities have completed preparation of such a strategy with the World Bank, which will focus on export agriculture and on tourism.

In the area of structural reform, there was a question on the reasons for the weak performance of macro finance institutions in Benin. We would cite a couple of main reasons. The first reason is weak supervision, given that a large portion of the sector operates informally: about 500 units out of 720 institutions are said to be operating in the informal sector. There is also weak management capacity within these institutions. To address some of these issues, it has been decided at the regional level that supervision of the bigger micro finance institutions will be put under the direct responsibility of the regional central bank.

The staff representative from the Policy Development and Review Department (Mr. Plant), in response to questions and comments from Directors, made the following statement:

I would like to talk about two general areas. One area is the appropriateness of the PRGF and possible other instruments that might be used for funding this kind of BOP problem. The second area is the notion of budget gaps and BOP gaps.

Several Directors commented on the possibility of providing some other type of loan to low-income countries facing a price shock from food and fuel. First, I would note that the Fund is unlikely to be able to design a facility that is more concessional than the PRGF. The PRGF already has interest rate of 0.5 percent, and lowering it to 0 percent would not save countries much. The only effective way to increase concessionality would be to increase the maturity which would make them more and more like development loans rather than BOP loans.

Countries that have a PRGF arrangement in place already have in some sense a certain amount of contingent credit available to them. Benin is exercising that contingency today. When a country has a PRGF arrangement in place, and a new balance of payments need occurs, the country can come to the Fund and ask for additional financing. One idea might be to raise or somehow increase the automaticity of giving that financing, or to prequalify countries for increased access. But that in fact would decrease the flexibility of the instrument and the ability to respond to the specific shock. One would have to prespecify the range and types of shocks and how much the Fund could then contribute. In fact, what we have seen with low-income countries is that the types of shocks are quite variable. The PRGF gives a needed amount of flexibility in responding to a range of those shocks. Thus, with six monthly reviews and the possibility of an extraordinary augmentation in absolutely dire circumstances, our view is that the PRGF has sufficient flexibility to meet the needs of those countries already under a PRGF arrangement.

What about these countries that do not have PRGF arrangements? That is what the ESF was designed for and will remain aimed at. There is no need to supplement any PRGF with the ESF. That would be simply equivalent to augmenting the PRGF. Again, that is a procedure that is well established. In looking at the ESF, when we

come back to the Board in the next few weeks, the idea would be to make the ESF more available to those countries without PRGF arrangements. But we would not see any way of linking the ESF with the PRGF.

Let me turn to the issue of budget versus balance of payments need. Any gap in the balance of payments in any country is by definition the sum of two gaps: the savings/investment gap in the private sector and the savings/investment gap in the public sector. That is not matter of economics. That is simply a matter of national income accounting. When the exchange rate is fixed, the private sector/savings investment gap will be zero. Any effort by the private sector to finance its deficit externally would put pressure on the exchange rate peg, and the monetary authorities would be forced to compensate for that pressure, and thereby the private sector would have an access to the money. Essentially, the private sector is separated off.

In a fixed exchange rate system, the only balance of payments gap is the public sector investment savings gap, that is the gap between revenues and expenditures. This gap can be closed in one of three ways. Domestic borrowing from the private sector, borrowing from the central bank, or borrowing externally. In the CFA zone, domestic credit markets, as my colleague has mentioned, are very thin and the credit is relatively expensive. It is difficult and expensive for the government to find money this way. In due course, these domestic credit markets will mature and there will be more viable alternatives for governments at market rates. Central bank borrowing is prohibited by the statutes of the zone as a safeguard against money creation by individual states. That leads to financing from abroad where the Fund is one possible financier. We can argue, and people are indeed arguing, about whether the Fund is the best financier, and whether we could not find other sources of money to fill the particular gaps occurring as a result of the food and fuel price increase.

In the case of Benin, our judgment is that a certain amount of Fund financing is appropriate. Other donors will come to the table in due course and fill other pieces of the gap, but the need was immediate for 2008. We were able to respond immediately with relatively concessional money. In the end, the argument should not be about whether there is budget or BOP financing, as in the CFA country those are equivalent. It should be about the nature of that financing and how that will be filled from abroad.

Let me come back to the question Mr. von Stenglin raised which is why cannot these countries have access to their reserves. It seems they have lots of reserves, and they should be able to get at them. In the CFA zone, the reserves are not strictly speaking Benin's; instead they are Benin's contribution to the reserves of the zone. When Benin gets foreign exchange, it sells that foreign exchange to the central bank. The central bank gives Benin in return domestic counterpart, which the government of Benin then spends. If the government of Benin wants some of its foreign exchange, it can buy that foreign exchange, but it has to have domestic counterpart and in tight budgetary times it does not have the domestic counterpart. In some sense, the reserves themselves do not belong to Benin, but they belong to the central bank. Unless Benin has adequate budgetary resources, they cannot access those reserves.

There is almost a complete analogy between this and a state in the United States. Suppose Kentucky received a grant from a European company in euros. It would exchange those euros for dollars which would then spend in the United States. If it wanted to repay that grant or give some money in euros, it would have to buy those euros on the market. If it had adequate money do that, it could do so. If it did not, it would have to somehow borrow. This is the same case that Benin faces. Right now, they are facing a gap in their financing. They do not have the available financing to purchase the foreign exchange they need. So, they need to look elsewhere for financing, and because of the nature of the undeveloped markets in the CFA, the place they look is abroad. They look to their donor partners. The Fund is one of those. As several Directors have said, it might be debatable as to whether the Fund is the appropriate one. But we should not get confused about the fact that there are reserves that Benin could tap. They are the reserves of the central bank that Benin has contributed to.

The Acting Chair (Mr. Portugal) stated that there was a suggestion from Ms. Lundsager, Mr. Kaplan, and Mr. Lanz that perhaps the proposed decision could be split into two parts. The staff had looked into that suggestion and did not consider that it was possible to do so in Benin's case. He invited the representative from the Legal Department to explain to the Board why that was the case.

The staff representative from the Legal Department (Mr. Ogada), in response to question on whether the proposed decision could be separated into two decisions, explained that the issue was that reviews had both backward-looking and forward-looking elements. With the new PCs that had been established by the

decision today and other conditionality, the program had been designed going forward with the new augmented amount in mind. Thus, it was not possible to split the decision and complete the review based only on the old amount. The new amount of access was an integral part of the forward-looking element. If the proposed decision were split, the review would only encompass the backward-looking element of the SDR 0.91 million from before, instead of the new augmented amount of access which had impacted the way the program had been designed going forward.

The staff representative from the World Bank (Ms. Bassani), in response to questions and comments from Directors, made the following statement:

On the question of the possible support from the World Bank to respond to the food and fuel price shock, the staff has presented a proposal for Benin to access the food price facility, and we hope that those resources will be made available to the country. In that context, we are planning for a multisector mission to travel to Benin before the end of June to review with the government what specifically the support could focus on and to provide more advice to the government on actions to stimulate supply response to the increased agricultural prices. We also have in the pipeline an agricultural development and diversification project that should support increasing both food crop and cash crop production, and intensification of the dialogue with the government on improving agricultural services. The support that could be provided from the food price facility will depend on the relative needs of other countries that have presented similar requests which are being examined by management.

In the area of the cotton sector, since December the Bank has conducted two missions to Benin to discuss with the authorities the next steps of the reform process. The last mission was in early June. During this mission, the Bank held discussions with the authorities on the main content of what was then later presented to the council of ministers as a strategic orientation of a new approach to the reform of the cotton sector. The broad outline of this approach is contained in a document that the Bank received on June 8, which we are examining carefully. The approach is supposed to go beyond the privatization of SONAPRA to cover issues related to the clarification of the role of each actor in the sector, the regulatory framework revisions, and the clarification of the role of the government in terms-of-service provision.

The government has asked the minister of agriculture to prepare an overall strategy based on the strategic orientations, and has asked for Bank technical and financial support, as well as that of other partners, to prepare studies or offer advice in order to inform this new strategy. At the request of the government, the Bank is intensifying its involvement in dialogue. Hopefully we can help them move forward.

In other areas of structural reform, we have also intensified our dialogue in telecommunication and energy. In telecommunication, the Bank has completed a review of the sector which has led the government to prepare a telecommunications sector development policy, to be presented soon to the council of ministers. There is also significant progress on the dialogue for restructuring the sector as a whole, including planned privatization. On energy, the dialogue has significantly improved with an agreement on sector restructuring and priorities for reform.

There was a question on the targeted social measures. In addition to intensifying our dialogue in the area of the cotton sector and the ongoing dialogue on the broadening of the agricultural sector, we have provided recent analytical work to the authorities on health and education that has yielded useful recommendations on how to better target health and education services to those most in need. We also have very strong dialogue on decentralization, and the funding of programs to improve urban sanitation and water supply for rural communities and communes. Finally, an ongoing development project is helping the authorities in targeting intervention to the poorest communities. Overall, we are collaborating very closely with the IMF in these areas of structural reform.

Mr. Kaplan made the following statement:

I would like to come back to the preliminary statement we submitted. We appreciate the fact that Directors can make their views known, even if they are quite critical, while still joining consensus to support a program. In this case, we chose to abstain. It is not a decision we came to lightly, particularly since it follows the recent case of Mali, where the U.S. also abstained. During the last review for Benin, we also abstained, although for several different reasons. To clarify again, the consecutive abstentions on Benin are not because my government has any particular problem or serious concern with the nature of the authorities' response to the food and fuel shock. In fact, my

government is a major donor in the agricultural and other sectors, including to the poor.

In the last review for Mali, we made a comment that had to do with the role of the Fund financing in the CFA zone. We clarified then that these issues of IMF response in CFA countries are awkward, but are well established. When we abstain in this context of Mali and Benin, highlighting the fact that the Fund is operating as a quasi-donor, we are not abstaining because there is a fiscal loan, which is what happens in every CFA country. Nonetheless, the fact that the Fund is essentially operating as a donor makes an awkward situation to think about the role of Fund financing and how quickly it should respond to shocks and what the other donors are doing.

We appreciate the World Bank representative's comments. But we know Benin's situation. I think it was Mr. von Stenglin who mentioned that Benin was not on the original list for the countries the Fund would respond to. My colleagues at the US Treasury Department sent me a list of the countries that the donor group in Africa is looking at for agricultural productivity and food response. And this may be a bit out of date, but Benin is not on that list either. We do not have a textured understanding for how quickly the Bank is responding in the case of Benin or otherwise.

The Fund has a powerful tool, in augmentations of PRGF arrangements, which it can use very quickly. And if the government decides that it wants to spend more money than it planned to, there is going to be a financing gap somewhere. There is no other way to look at this because of the balance of payments being in good shape, because the donors will take their time but eventually will respond, and because the policies that we have on the table are ill-targeted and may not be sustainable. This could have gone on for another six months. The Fund could have waited for the donors. If there was a tremendous need at the end of the year, the Fund could have stepped in at that time. The reason why we are abstaining in this context is because we fear that the Fund's desire to be relevant is leading the Fund to a very quick financial response where perhaps patience might be more appropriate. Maybe this is a comment directed more toward management than the staff. We ultimately see the rationale for a Fund program and for Fund financing as facilitating adjustment of policy. And at this point, in the absence of a compelling need to step in quickly, we do not have that policy package in place yet.

Mr. Fayolle asked Mr. Kaplan whether the United States could be expected to abstain on all the upcoming cases on augmentation of access under the PRGF.

Mr. Kaplan replied that his chair expected to support the upcoming case of Haiti's augmentation to the PRGF. Haiti's balance of payments was clearly under stress, and the objective of the program was to stop or minimize central bank lending to the government, which had experienced previous problems. In the case of the Central African Republic, his chair could also support that program. It would depend on what management would be doing going forward, but hopefully his chair's abstentions would be limited to Mali, whose Board discussion had already taken place, and to Benin.

Mr. Fayolle made the following additional statement:

I must say I am a bit confused about the rationale for the U.S. chair to abstain. I had understood at the end of Mr. Kaplan's intervention it was related to the Fund rushing into this kind of issue. Thus, I had concluded that the same argument should apply to other cases, but apparently that is not the case.

I would very much like to thank Mr. Plant for a very clear presentation of how the CFA works. It is extremely important for the Board to understand what the options are and what the constraints of this exchange rate system are.

Regarding one of the issues raised indirectly by Mr. Guzman about the reputational risk and whether we are communicating enough about the fact that we are answering this very specific and urgent need in some of the countries of the membership through augmentation of access under the PRGF, it is probably not going to be clear what is relevant to the normal access and what is relevant to the augmentation of access. Perhaps we do not sell ourselves enough outside of this institution.

Mr. Rutayisire made the following statement:

I cannot accept that there is a rush in the response on the part of the Fund. The Executive Board discussed the Exogenous Shocks Facility (ESF) and approved it. This facility specifies the conditions under which a member country can be eligible. Those countries that have a PRGF can access this facility through an augmented exercise,

which is what Benin is taking recourse to. To say that this would be a different issue would appear like we are changing the criteria that right from the start was there when we were designing the ESF. I think the staff have said correctly that this access is within that context. There is still a need for the staff to explain to us why at this moment we should view this kind of access differently.

Even if we were to consider the medium-term aspect of the factors that underlie a balance of payments problem, it is not true that the Fund is ill-placed to do this lending and that would be a rushed decision because we have facilities that provide for protracted balance of payments problems through which the Fund can also assist member countries. It would be a question of determining whether or not these countries qualify under those conditions. But I cannot accept that clearly the Fund is not prepared for that kind of exercise.

I would like to appreciate what Mr. Kaplan has said about his authorities' support of Benin and Madagascar. Donors were meeting to support Madagascar, implement its poverty reduction program, including a response to the balance of payments implications of the food and oil price crisis. I have noticed the United States as being one of the contributors to the funding that Madagascar required, which totaled around U.S. \$3 billion or 4 billion. I was also in Mali, and the U.S. authorities were again among the most active contributors to the funding requirements of Mali, where about U.S.\$2.4 billion was pledged. I would like to appreciate that part of Mr. Kaplan's authorities, but I would also appeal to his chair to remain considerate on the discussions that we have had on the ESF.

The Acting Chair (Mr. Portugal) made the following additional statement:

There were several issues the Board discussed today. One is the difficulty in defining what is a pure balance of payments need from what is a fiscal need. This reminds me of the old model where there is a foreign exchange gap and a savings gap. Even if the origin can be an external need which is clearly different from the internal need, the impact in the end is both external and internal. The solution would need to help on both the internal and external fronts. This is even more clear in the case of a currency union, as Mr. Plant has explained. I am glad that is not the reason why the U.S. is abstaining on this case, as Mr. Kaplan suggests.

There are two other questions raised by Mr. Kaplan: the Fund is rushing into this lending and it should not rush, and Benin was not on the original list of countries affected by the food and fuel crisis. It is true that Benin was not on that list. The original list was done from Washington before going to the country. When we go to a specific country, it could happen that one country which is on the list should be taken off the list, while another country not on the list should be put on the list. That is the purpose of missions and that is the reason why this country was not on the original list but is now being proposed for an augmentation of access under the PRGF.

There is a question of whether or not we are rushing into this lending. This is a very urgent need. In response to this need, countries are being pressed into responding with not necessarily the best policy measures. It is a global problem for every country in both developed and developing countries. But, for advanced countries it is mainly a problem of second-round effects on inflation. For developing countries, it is a problem of second-round effects on inflation and it could be a problem of balance of payments, which is where we come in. For the very poor countries, which are the African countries, it is a problem of inflation, balance of payments, and it could also become a serious social and political problem. We have seen riots in some countries and have seen governments being toppled. When we have an urgent need, we should respond quickly, and that is what we are trying to do.

All of these issues will be on the table for discussion by the Executive Board. We are planning a series of meetings for Directors to discuss these various issues. There will be a tentative discussion scheduled for June 27 to discuss the response that we are having to the food prices problem. We will have discussions in July on the ESF and on the role of the Fund on low-income countries. I am sure Directors would have an opportunity to discuss these topics in the future. I wanted to give a clarification to explain our rationale on the part of management to act in these cases.

Mr. Rutayisire made the following concluding statement:

I wish to thank Executive Directors for their support to my authorities for a request for augmentation of access under their current PRGF and the completion of this review. The additional resources will help the authorities deal with the short-term balance of payments

consequences of the current global food and fuel price crisis when they are implementing strategies for a long-term solution to the crisis.

In addition, the constructive recommendations and advice provided by Directors through statements and today's discussions will help my Benin authorities in continuing to perfect their macroeconomic management. Thanks also to Mr. Matungulu, the mission chief, and his team for the important work achieved during the past years, and for the comprehensive answers to the questions raised by Directors.

I want to express my gratitude to Directors for their recognition of my authorities' continued efforts to improve macroeconomic stability and achieve the objectives of the current PRGF-supported program. My authorities reiterate their determination to pursue a prudent fiscal policy over the medium term and further their fiscal consolidation initiated in 2006. To this end, they are committed to continue streamlining the country's tax system, enforce fiscal discipline, and improve expenditure management. They will contribute to keeping the public debt at sustainable levels while increasing the fiscal space for growth-enhancing and poverty-reducing spending. They are implementing measures to strengthen the procurement system and management of projects to resolve absorptive capacity problems in the execution of the budget. In the same order, my authorities remain committed to a borrowing strategy consistent with the country's long-term fiscal and debt sustainability. They will continue to seek more grants and concessional loans to finance their development agenda.

The Benin authorities are fully aware of the critical necessity of creating an effective social safety nets to help vulnerable groups of the population deal with the consequences of the current global food and fuel crisis. In this regard, some development partners have already indicated their readiness to provide technical assistance in the establishment of these social safety nets. Meanwhile, the government intends to make use of consumption subsidies to target the needed social groups instead of fiscal measures, if the current price pressures exist. Going forward, the government has decided to allocate additional resources this year to improve the domestic food supply and plans major investments over the medium term to help mechanize the agricultural sector principally with the aim to reducing Benin's dependence on imported foods.

The land reform being implemented under the MC in Benin's support is part of this overall strategy. Support from the African Development Bank, IFAD, as well as other donors are expected. At the same time, initiatives have been decided at the WAEMU regional level. Notably, the meeting of finance ministers held on April 24, 2008 decided to set up a task force to oversee the fiscal response to the crisis. They also decided to provide CFA 340 billion to support short and long-term measures aimed at boosting regional agricultural supply with funding to be raised in part by regional institutions such as West African Development Bank, as well as from donors.

Finally, I wish to reassure Directors that my authorities' political will and determination to pursue their structural reform agenda remain unyielding, notwithstanding the many challenges and obstacles that constrain its implementation. They share Directors' views that accelerating implementation of the reform agenda is critical to help remove obstacles to competitiveness, reduce vulnerabilities of the economy to external shocks, and foster a strong sustained and private sector led economic growth. The authorities have renewed their commitments through a rationalized timetable for the implementation of the reforms, and will continue to enhance internal dialogue on the economic benefits of the reforms by further involving participation of stakeholder groups. They hope to continue benefiting from donor support, and technical assistance in this endeavor.

The Acting Chair (Mr. Portugal) made the following summing up:

Executive Directors agreed with the thrust of the staff appraisal. They commended Benin's satisfactory economic performance over the last two years, marked by low inflation and strengthening economic growth. Directors noted that Benin was the only WAEMU member country in 2007 to meet the monetary union's convergence criterion on the basic fiscal balance.

At the same time, Directors observed that growth continues to fall short of levels required to achieve significant progress in poverty alleviation, and that core economic vulnerabilities remain. In particular, rising commodity and food prices are fuelling inflationary pressures, the external current account is widening because of terms of trade deterioration and real currency appreciation, and Benin's weak absorptive capacity hampers efforts to boost growth.

Noting the slow progress of structural reform, Directors called on the authorities to invigorate the reform process—particularly in the cotton and public utility sectors—in order to reduce Benin’s vulnerability to shocks, strengthen external competitiveness, improve the business environment, and further boost economic growth to accelerate progress toward the Millennium Development Goals. This will also help unlock donor financing. In this regard, Directors were encouraged by the authorities’ renewed commitment to engage in a comprehensive reform agenda.

Directors noted that the fiscal measures taken to address rising food and fuel prices—namely, reduction of tariffs on certain food and oil imports and subsidies to the electricity company—have weakened Benin’s budgetary position in 2008. They called on the authorities to limit the scope and duration of these measures, and supported an early transition to well-targeted and more fiscally sustainable safety net measures. Directors encouraged the donor community to provide additional assistance to help Benin cope with the food and fuel price shock. In this regard, most Directors supported an augmentation of Fund financing to Benin, while some Directors expressed reservations given Benin’s strong international reserve position.

Directors commended the authorities’ prudent fiscal stance and the implementation of measures to improve revenue collection and control public spending. They called for further improvements in public expenditure management, and reiterated that reform of the civil service pension fund will be essential for achieving medium-term fiscal sustainability. Directors encouraged the authorities to remove the ceiling on wages as progress is made on wage management. At the same time, Directors emphasized that project design and implementation capacity needs to be strengthened to permit higher and more efficient development and social spending.

Directors welcomed the authorities’ commitment to maintaining prudent borrowing policies in order to preserve external debt sustainability. However, they expressed concern that substantial borrowing has been undertaken in regional financial markets at high interest rates, only to result in an accumulation of funds in the banking system because of capacity constraints on spending.

Directors looked forward to the finalization of the comprehensive reform strategy being prepared for the cotton sector, and encouraged that the strategy be expeditiously implemented once it is completed. They called on the authorities to adhere to the new restructuring timetable for the telecommunications and electricity companies. Directors welcomed the achievements in port reform, including planned introduction of a one-stop window for customs clearance, which should help improve port management and enhance customs effectiveness. Directors also encouraged timely implementation of measures to strengthen the judicial and land tenure systems and to facilitate further access to credit for small and medium-sized enterprises.

Directors noted the weaknesses in banking sector indicators, including low capitalization, maturity mismatches, and high concentrations of credit and non-performing loans. They welcomed the authorities' endorsement of key recommendations from the recent WAEMU FSAP mission to improve financial sector regulation and supervision. Directors supported the recent regional agreement to strengthen the supervisory authority of the regional Banking Commission, and welcomed the regional central bank's efforts to ensure timely observance of agreed higher bank minimum capital requirements.

It is expected that the next Article IV consultation with Benin will be held within 24 months, subject to the provisions of the decision on consultation cycles in program countries.

The Executive Board took the following decision, with one abstention by Ms. Lundsager (UA):

Poverty Reduction and Growth Facility—Three-Year Arrangement—Review, and Augmentation of Access

1. Benin has consulted with the Fund in accordance with paragraph 2.I.C(c) of the arrangement for Benin under the Poverty Reduction and Growth Facility (PRGF) (EBS/05/114, 07/25/05) (the "Arrangement") in order to review program implementation.
2. The letter dated May 30, 2008 from the Minister of Economy and Finance (the "May 2008 Letter"), along with its Memorandum of Economic and Financial Policies (the "May 2008 MEFP") and the Technical Memorandum of Understanding (the "May 2008 TMU"), shall be attached to the Arrangement, and the letters dated July 21,

2005, October 29, 2006, May 22, 2007 and December 19, 2007, together with their attachments, shall be read as further supplemented and modified by the May 2008 Letter and its attachments.

3. Accordingly, the Arrangement shall be amended as follows:

a. In paragraph 1(a) “SDR 6.19 million” shall be replaced with “SDR 15.48 million”.

b. Paragraph 1(cc) (iii) shall be revised to read as follows:
“(iii) the fifth disbursement, in an amount equivalent to SDR 10.17 million, will be available on or after May 15, 2008, at the request of Benin and subject to paragraph 2 of the Arrangement;”

c. The following subparagraph (v) shall be added to paragraph 1(cc):
“(v) the seventh disbursement, in an amount equivalent to SDR 0.91 million, will be available on or after April 15, 2009, at the request of Benin and subject to paragraph 2 of the Arrangement;”

d. In paragraph 2.I.C (b) the words “as determined at the time of the fourth review” shall be replaced with “as set forth in Table 1 of the May 2008 MEFP and further specified in the May 2008 TMU”.

e. In paragraph 2.I.C (c) the words “as referred to in paragraph 38 of the May 2008 MEFP” shall be added after the words “the fifth program review”.

f. The following shall be added to paragraph 2.I:

“2.I.D (a) if the Managing Director of the Trustee finds that, with respect to the seventh disbursement, the data as of December 31, 2008 indicate that:

(i) the ceiling on net domestic financing of the government of Benin; or (ii) the ceiling on the primary fiscal balance, as set forth in Table 1 of the May, 2008 MEFP and further specified in the May 2008 TMU, is not observed; or

2.I.D (b) until the Trustee has determined that, with respect to the seventh disbursement, the sixth program review referred to in paragraph 38 of the May 2008 MEFP has been completed.”

g. In paragraphs 2.II (e), (f), (g) and (h) references to “Table 1 of the December 2007 MEFP and the December 2007 TMU” shall be

replaced with “Table 1 of the May 2008 MEFP and the May 2008 TMU”.

4. The Fund decides that the fourth review contemplated in paragraph 2.I.C (c) of the Arrangement is completed, and that Benin may request the disbursement of the fifth loan referred to in paragraph 1(cc) (iii) of the Arrangement. (EBS/08/62, 6/2/08)

Decision No. 14125-(08/52), adopted
June 16, 2008

APPROVAL: September 22, 2008

SHAILENDRA J. ANJARIA
Secretary