

SUR/08/113

December 1, 2008

**The Acting Chair's Summing Up
Sudan—2008 Article IV Consultation and Second Review
Under the Staff-Monitored Program
Executive Board Meeting 08/104
November 26, 2008**

Executive Directors agreed with the thrust of the staff appraisal. They welcomed Sudan's overall satisfactory performance under the staff monitored program (SMP), notably the implementation of key structural reforms. Economic growth in both the oil and non-oil sectors has been strong, and macroeconomic stability generally has been maintained.

At the same time, Directors noted that Sudan continues to face large and complex challenges, which are exacerbated by the prospect of declining oil revenue and the global economic slowdown. Directors urged the authorities to maintain prudent macroeconomic policies and to accelerate fiscal and financial sector reforms, so as to strike the right balance between lowering inflation and sustaining growth. They also stressed the important role of political and social stability and internal security in building confidence and fostering development.

Directors welcomed the improved fiscal performance in 2008, commending the authorities for the steps taken to widen the tax base, improve tax administration, and strengthen public financial management. They underlined the need to maintain a cautious fiscal stance in 2009 in the face of expenditure pressures and declining oil revenue. They called for a strong effort to improve the non-oil primary fiscal balance, including through an increase in non-oil revenue and restraint on non-priority spending. Directors observed that additional fiscal measures may be needed to achieve the agreed cash deficit target for 2009, and advised that contingency plans be developed for this purpose. They also encouraged the authorities to use the opportunity of declining oil prices to phase out subsidy schemes in favor of a targeted safety net, while recognizing the technical challenges involved.

While acknowledging Sudan's considerable reconstruction and development needs, most Directors urged the authorities to minimize or refrain from nonconcessional borrowing in view of Sudan's unsustainable external debt burden. They noted that this would also give a strong signal of Sudan's cooperative effort and avoid complications in the event of a future debt-relief operation. Directors acknowledged the authorities' effort to keep nonconcessional borrowing well below the allowed ceiling in the SMP.

Directors encouraged the authorities to continue to build on the progress made with fiscal reforms, which are crucial to improve the non-oil fiscal balance. Existing VAT exemptions should be streamlined, the personal income tax reformed, and key tax administration reforms expedited. Directors supported the re-orientation of spending toward

the social sectors and infrastructure, and many Directors also encouraged stronger incentives for prudent financial management and increased revenue collection at the sub-national level. Directors noted that capacity and political constraints would call for careful prioritization of reforms.

Directors welcomed the recent decline in inflation, while calling for a continued prudent monetary stance. They encouraged the authorities to monitor price developments closely, to improve coordination between the central bank and the finance ministry on the timing and amount of arrears clearance, and to adjust monetary policy and the pace of arrears clearance as needed to contain inflationary pressures. Directors supported the authorities' plans to develop indirect monetary instruments.

Directors noted that the real exchange rate appears broadly in equilibrium, although the real appreciation since 2005 may have contributed to the weak performance of non-oil exports. They emphasized the need to remove structural bottlenecks to competitiveness, and urged reforms to improve the business environment and boost productivity. Directors also recommended greater exchange rate flexibility to buffer the economy from external shocks and to protect reserves.

Directors noted that sustained economic growth and improved monetary control will require deeper financial intermediation. While they welcomed the improvement in financial soundness indicators in the first half of 2008, they expressed concern about financial sector vulnerabilities. They pressed for prompt action to resolve or restructure the state-owned Omdurman Bank based on the results of the recently completed audit. Directors also called on the central bank to actively enforce prudential standards and regulations.

Directors considered that the SMP has served as a valuable tool to support Sudan's reform momentum and maintain macroeconomic stability, and they welcomed the authorities' intention to negotiate a new SMP in 2009. Directors generally welcomed Sudan's record of cooperation on economic policies and payments to the Fund. At the same time, a number of Directors emphasized the importance of maintaining timely repayments to the Fund, and looked forward to a further increase in repayments. A few Directors also reiterated their call to allocate payments to charges falling due rather than to principal in arrears.

A number of Directors considered that the SMP meets the standard of upper credit tranche conditionality, except for the allowed level of non-concessional borrowing. A number of other Directors felt that Sudan's broadly satisfactory performance under the successive SMPs should be reflected in the timetable for arrears clearance. These Directors called for a timely road map for arrears clearance, while recognizing that this would require broad support from the international community.

The next Article IV consultation with Sudan is expected to be held on the standard 12-month cycle.